The Crash that launched a thousand fixes --- Regulation of Consumer Credit after the Lending Revolution and the Credit Crunch

Iain Ramsay and Toni Williams

Professors of Law, Kent Law School, University of Kent, Canterbury, UK

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I Introduction

The consumer lending "revolution"[1] –with its promise of the democratisation of credit—has been followed by the credit crunch. The credit crunch has stimulated both immediate regulatory initiatives and more fundamental reflection on consumer credit regulation. [2] As the Turner review in the UK notes, conventional regulatory assumptions—that reputable firms do not place risky products on the market, that innovation is stifled by regulation and that regulators are not as well placed as the market to judge the value of products—have been challenged by the credit crunch.[3]

Regulation of consumer credit markets has been on the policy agenda in many countries during the past decade. Objectives have included "modernization" [4], regulation of unfair practices and addressing the problems of overindebtedness and financial exclusion. The credit crunch may increase both these latter phenomena.[5] In the UK the first years of the 21st century were characterized by a flurry of inquiries[6], reports[7], task forces[8] , legislation[9], regulation[10] and "soft law"[11] on consumer

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[1] See Federal Deposit Insurance Corporation "Evaluating the Consumer Lending Revolution" (2003) http://www.fdic.gov/bank/analytical/fyi/2003/091703fyi.html (accessed 29.7.2008) and R. Brown and S. Burhouse (2005) "Implications of the Supply-Side Revolution in Consumer Lending" 24 St. Louis University Public Law Review pp.363 et seq. This revolution included: financial liberalisation, deregulation of interest rates, securitisation, the application of sophisticated computer technology to develop predictive credit scores and risk-based pricing, and the increasing spread of all-purpose credit cards.

[2] UK government promises a White Paper which will " initiate a debate on the long term vision for consumer credit in the UK" See DBERR and "Building Britain's Future" (Treasury, Budget 2009). In US President Obama proposes a Consumer Financial Protection Agency "dedicated to consumer protection in credit, savings and payments markets" See Department of the Treasury, *Financial Regulatory Reform: A New Foundation: Rebuilding Financial Supervision and Regulation* (June 2009). See also the Credit CARD Act 2009 HR 627. Peter Gowan suggests the possibility of returning to a public utility model of financial services. See P. Gowan, "Crisis in the Heartland: Consequences of the New Wall Street System" (2009) 55 New Left Review 5. See also R Wade "Financial Regime Change?" (2008) New Left Review 5. See also. studies by Joint Centre for Housing Studies Harvard University at http://www.jchs.harvard.edu/publications/finance/ : Bar-Gill and Warren argue for a Consumer Credit Safety Commission which would screen credit products for safety. See O Bar-Gill and E Warren, Making Credit Safer http://ssrn.com/abstract=1137981 (accessed 05.08.08): R Shiller The Sub-Prime Solution Princeton: Princeton UP 2008; . M Barr, S Mullainathan and E Shafir, *Behaviourally Informed Financial Services Regulation* (New America Foundation, 2008).

[3] Turner Review 2009.

[4] See e.g. South Africa (2005), EU (2008), UK (2006), Japan, 2006, discussed in S Kozuka and L Nottage, "The Myth of the Cautious Consumer: Law, Culture, Economics and Politics in the Rise and Partial Fall of Unsecured Lending in Japan" in J Niemi, I Ramsay and W Whit ford, *Consumer Credit, Debt and Bankruptcy: Comparative and International Perspectives* (in press Oxford, Hart, 2009).

[5] Financial exclusion has been defined as " a process whereby people encounter difficulties accessing and /or using financial services and products in the mainstream market that are appropriate to their needs and enable them to lead a normal life in the society to which they belong... " See European Commission *Financial Services Provision and Prevention of Financial Exclusion* Directorate General for Employment, Social Affairs and Equal Opportunities Executive Summary at 3. There is no universally accepted definition of over-indebtedness. In the EU see *Towards a Common Operational European Definition of Over-Indebtedness* DG Employment Social Affairs and Equal Opportunities (2008) (concluding that it is caused by combination of risk factors (for example low income, age) combined with change of circumstances compounded in some cases by poor money management and over-commitment). The minutes of the Financial Inclusion Task Force in September 2008 note that "progress on bank engagement and affordable credit has yielded less positive results than had been anticipated due to the changing economic environment". Leyshon and Thrift, discussing the recession of the late 80s and early 90s argue that "financial crises...tend to induce a 'flight to quality'...a search for 'safer' markets...which tends to discriminate in favour of more affluent and powerful social groups and against poor and disadvantaged groups." A Leyson & N Thrift, "Geographies of financial exclusion: financial abandonment in Britain and the United States" (1995) Transactions of the Royal Institute of Geographers 312.

[6] See Competition Commission inquiries into home credit, store credit cards, and payment protection insurance. Available at http://www.competition-commission.org.uk/ .

credit, over-indebtedness and financial inclusion. There has also been an increasing "internationalisation" of regulatory models: this diffusion occurs through regional initiatives,[12] the influence of international institutions, legal transplants, and the practices of international financial institutions.[13] The World Bank has outlined a model of consumer protection in financial services. [14]

Assumptions about the function of consumer credit in contemporary economies will affect the form of regulation. Consumer credit performs several functions. It facilitates consumerism, compensates for stagnant growth in wages, and may smooth fluctuations in income and substitute for social spending in economies with limited social provision[15]. Credit may purchase therefore not only "private" consumer goods and services but also public goods such as education . Mortgage credit is a key to home ownership ---in turn a key to other services such as education—and of great social importance in many countries[16]. Consumer credit may contribute to an individual's capability in society.[17] Consumer credit is therefore a central aspect of contemporary economies, part of the financialisation[18] of modern life. The consequences of a credit crunch are significant for many groups—both middle and lower income consumers.

A society organised around a high level of consumerism and limited public provision will inevitably result in high levels of consumer credit. The US provides the historical experiment of a "consumers' republic" where high levels of consumption facilitated by low cost mortgages and tax-subsidised consumer credit were intended to ensure high employment and productivity and provide equality through consumption without the necessity for a substantial welfare state.[19] Lizabeth Cohen describes the "explosion" of credit in the US between 1945-60 when credit became "an admission

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[7] See e.g. Griffiths Commission, What Price Credit? (London, Centre for Social Justice 2005) and the reports of the Treasury Select Committee on Credit Cards

[8] See the various reports of the Task Forces on Over-Indebtedness and Fuel Poverty (available at the DBERR website http://www.berr.gov.uk/whatwedo/consumers/consumer-finance/over-indebtedness/index.html .

[9] The Consumer Credit Act 2006

[10] See the 2004 regulations on precontractual information and advertising in consumer credit and the Orders made by the Competition Commission in relation to store cards and home credit.

[11] One could include here changes to the Banking Code of Practice, the issuance of guidance by the Office of Fair Trading on debt-collection practices and "irresponsible lending".

[12] See e.g. recent EU Consumer Credit Directive and project on over-indebtedness and financial exclusion.

[13] See J Braithwaite (2008) *Regulatory Capitalism* (Cheltenham: Edward Elgar) for a discussion of the "diffusion" of international norms.

[14] See below 2.1.

[15] Credit cards may provide a substitute for income assistance and public welfare in countries such as the US and UK. See Ramsay, 2003.

[16] See M Stephens, "Mortgage Market Deregulation and its Consequences" (2007) Housing Studies 201-220.

[17] See Sen *Development as Freedom* (Oxford:OUP, 1999) at 39who views microfinance as increasing the capacities of the poor. Discussions often do not distinguish between credit for production and consumption. See M. Hudon, "Should Access to Credit be a Right?" (2009) 84 Journal of Business Ethics 17.

[18] On financialisation see e.g. R Martin *The Financialisation of Daily Life* Philadelphia: Temple 2002. On the relationship of financialization to consumer debt see J Montgomerie *Financialization and Consumption; an alternative account of rising consumer debt levels in Anglo-America* (CRESC Working Paper No 43) (December 2007). See also, P Gowan, "Crisis in the Heartland: Consequences of the New Wall Street System" (2009) 55 New Left Review 5; C Lapsavitsas, "Financialised Capitalism" http://www.soas.ac.uk/events/event43769 ; T. Palley, "Financialization: What it is and why it matters (University of Amherst, Mass. Working Paper, November 2007.

[19] See L. Cohen (2003), *A Consumers' Republic: The Politics of Mass-Consumption in Postwar America* (New York: Knopf).

ticket" to consumer citizenship and prosperity. This model was adopted about a generation later in the UK during the 1970s and 1980s along with a transition from producerism to consumerism in politics and cutbacks in the welfare state. In contrast, several continental European countries continue to have lower levels of consumer credit than the UK and higher levels of social security.

There remain significant differences in levels of consumer credit and approaches to regulation of consumer credit in the EU with contrasts drawn between "Anglo Saxon" approaches to regulation which emphasise freedom to obtain credit and countries such as France and Germany which are more likely to protect an individual from the credit market . The institutional framework of credit markets and regulation also differ within Europe concerning issues such as the role of credit bureaux, the use of interest rate ceilings, credit card practices and regulation, the availability of home mortgage loans and the size of the non-profit financial sector. These differences, which may reflect legal origins[20], political economy , [21] or distinct approaches to consumerism[22], challenge the ambition to create an integrated EU credit market which achieves both a competitive market and the social goals of financial inclusion and affordable access to credit. The relative balance between these goals and the role of regulation in the European market is not merely a technical problem. There is also political competition in the internationalisation of national models of regulation. Until recently the UK compared its model of credit regulation favourably with other countries, claiming for example that restrictive German consumer credit legislation had contributed to the sluggish growth of the German economy.[23] While this may seem now like hubris, it highlights the need for careful comparative study to understand the assumptions, norms and effects of distinct regulatory regimes.

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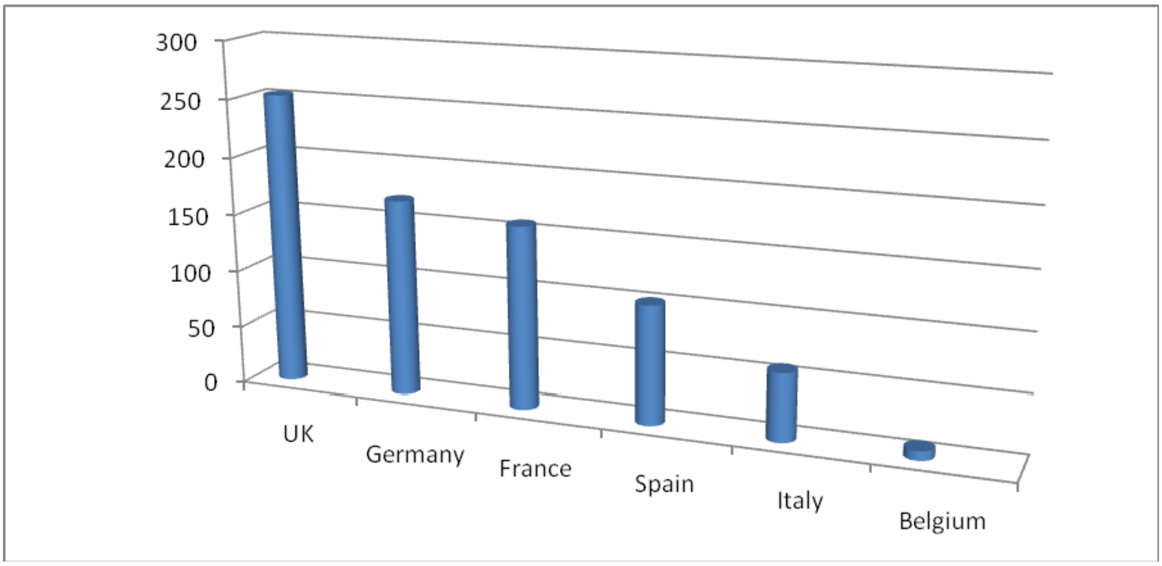
[20] See e.g. R La Porta et al "Law and Finance" 106 Journal of Political Economy 1113-1155: La Porta et al "The Economic Consequences of Legal Origins" (November 2007).. See the review and critique of this approach in C. Milhaupt and K Pistor *Law and Capitalism: What Corporate Crises Reveal About Legal Systems and Economic Development around the World* (Chicago: University of Chicago) (2008).

[21] Reflecting the influence of different political groups or ideologies. See e.g. D Harvey A Brief History of Neo-Liberalism (2005) at 61-62.

[22] See J. Whitman, 'Consumerism versus Producerism: An Essay in Comparative Law' (2007) Yale Law Journal pp. 340 et seq. at 382

[23] This is the tenor of research carried out for the DTI [now DBIS] Policis *The Economic and Social Risks of Credit Market Regulation*

TABLE 1 Outstanding Levels of Consumer Credit Selected European Countries October 2008 [€bn]



Source: Deutche Bundesbank Statistics and Bank of England Monetary and Financial Statistics cited in DBERR Impact Assessment of the Consumer Credit Directive (2008)

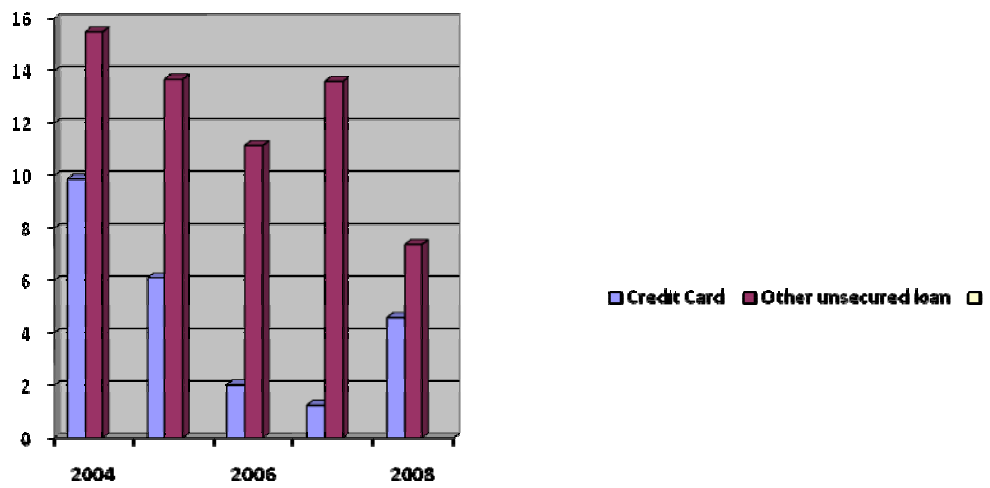
TABLE 2

Consumer Credit per Capita 2004

UK	4200
FRANCE	2200
GERMANY	2700
CZECH	200
FINLAND	1300

Source European Credit Research Institute

TABLE 3 UK Net Unsecured Lending Flows (£bn) 2004-2008



Source Bank of England Lending Trends (2009)

There are two basic conceptualisations of credit regulation in contemporary policy literature. The first is to treat it as a "private" commodity. Even within this conceptualisation there may be substantial scope for regulation based on market failures(information, externalities) on the supply and demand side. Warren and Bar Gill argue that credit products like toasters should meet minimum safety requirements and their safety should be regulated through similar techniques (information, warnings, standards, recalls, bans) to those adopted for other consumer products. A second approach is to view credit services as a service of general interest—as a necessary part of life—and subject to public service obligations. In developed countries financial exclusion – where individuals do not have access to the financial system or have restricted access to only high cost credit – may lead to social exclusion and undermine tax and welfare redistributions. Access to affordable credit may not be a human right but ideas associated with services of general interest such as equality of access, non-discriminatory treatment and corporate social responsibility to clients might be argued as affecting regulation of credit markets and underpin a conception of responsible lending.[24] Gowan sets forth three reasons for treating financial services as a public utility: they are vital public services and inherently unstable; policy questions concerning the channelling of credit to industrial or consumer use raise issues of great economic and social significance; and financial services should be subject to democratic control.[25]

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[24] See Commission of the EU Green Paper on services of general economic interest COM (2003) 270. The EU classifies services of general interest as services of an economic nature" which are "subject to public service obligations". The EU does not currently classify financial services as a service of general interest.

[25] Gowan op cit.

Alternative classifications of consumer credit affect our understanding of the credit contract and the role of lenders and borrowers. If credit is a service of general interest then "responsible lending"—an influential concept in many reform initiatives[26]--- could include not only an obligation on financial service providers to be prudent lenders but also to reach out to groups which are underserved. Three methods to achieve this objective appear in existing literature.[27] First there is the promotion of non-profit institutions such as credit unions (savings banks in Germany, France and Spain). A second approach is to encourage mainstream banks to ensure access to excluded groups. This may be achieved through embedding public obligations as a ground rule of the banking system. Third, the state might provide a dedicated fund as in the UK where small loans may be made available through state agencies such as the social fund. The UK has rejected imposing obligations on mainstream financial institutions and has promoted the "third sector" of credit unions and community initiatives[28].

We do not explore these issues at length in this paper but we believe that public obligations should be embedded in the mainstream financial system using the model (if not the actual practice) of the US Community Reinvestment Act. George Gloukoviezoff has recently argued for a general "solidary objective" to be written into the objectives of the financial system[29] . This would be a true "Third Way" between dominant forms of regulation (financial literacy, better disclosures, and credit data sharing) and state redistribution. Georges Gloukoviezoff argues that solidary outcome objectives would be required for the banking system but banks would not be required to meet these objectives. However, if they failed to do so they would have to make a financial contribution to those who had met the objectives. This would make it less efficient to practice financial exclusion and would promote a more cooperative capitalism. The recent EU report on Financial Exclusion proposes a similar plan that there should be a compensatory financing mechanism for those banks which provide universal services so that they are not disadvantaged competitively[30]. We think that this model should be considered seriously in the UK where UK Financial Investments Limited has already imposed an obligation to lend on financial institutions in which it has a financial stake[31].

In this paper we take the fundamental issues in credit to be those of availability and safety and examine an influential international model of consumer credit regulation, identified by the World Bank, which we characterise as a neo-liberal approach to regulation. However even within this model public regulation of consumer credit markets is accepted as necessary to achieve public confidence and achieve fairness. The recent US proposal to create a Consumer Financial Protection

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[26] Responsible lending was highlighted in the initial draft of the recent EU consumer credit directive. This draft included a suitability of credit requirement along with an obligation on creditors to check credit databases and reflected the Belgian approach to credit regulation. This provision was ultimately watered down to an obligation to explain and advise on credit options so that a consumer is in a position to make an informed decision, and to check credit databases where appropriate. See arts 5, and 8. Recital 26 of the Directive states that governments should promote responsible lending practices throughout the lending transaction "Irresponsible lending" is a factor to take into account in determining whether to grant or revoke a credit licence in the UK The National Credit Act of South Africa 2005 prohibits "reckless lending" (see ss 78-81)

[27] See discussion in EC Directorate General for Employment, Social Affairs and Equal Opportunities, *Financial Services Provision and Prevention of Financial Exclusion* (2008).

[28] The third sector of credit unions etc remains very small in England compared with other countries.

[29] See G Gloukoviezoff De l'exclusion à l'inclusion bancaire des particuliers en France : entre nécessité sociale et contrainte de rentabilité (PhD Thesis, Lyon, 2008).

[30] See EC Financial Services Provision and Prevention of Financial Exclusion op cit

[31] Placing and Open Offer Agreement between the RBS groupPLC, UBS Ltd, Merrill Lynch International and the Commissioners of HM Treasury 13 October, 2008.

Agency is intriguing since a form of this regulation already exists in the UK in the overlapping jurisdiction of the UK Office of Fair Trading and Financial Services Authority over credit markets and we examine the recent regulation of sub-prime lending and payment protection insurance by the FSA. We conclude that this may provide a promising model for future credit regulation, but will not solve the problem of achieving affordable access to credit.

A final preliminary point concerns the variety of explanations for the contemporary global financial crisis. [32] One strand of explanation links the credit crunch to consumer profligacy—the idea that there has been a "credit binge" during the past decade in countries such as the UK and the US in the service of rampant consumerism. Avner Offer develops a more elegant explanation, arguing that consumer overspending represents a pathology of affluent societies.[33] However this is a partial picture. Much credit was used to upgrade assets that were perceived would increase in value (homes). The liberal availability of consumer credit and the housing boom during the late 1990s in the UK compensated for the downward pressure on wages created by free trade and the ability since the 1970s of capital to free itself of labour power, through for example the abolition of controls on the mobility of capital. [34] Free trade also provided cheap imports which could be financed by credit. The rise of securitisation, linking the capital and credit markets, provided a continuing demand from the capital markets for high yield consumer credit receivables, which would meet the needs of high short-term returns in a shareholder driven capitalism.[35]While credit might lead to short term growth, this was consumption rather than investment driven and was ultimately unstable.[36] The sources of problems in the credit markets are primarily on the supply side of the market and a government committed to an economy driven by consumer credit.

II Neo-Liberal Approaches to Regulation

Neo-liberal regulation promotes access to consumer credit and the creation of confidence in an expanding and competitive consumer credit market. Consumer choice and the promotion of individual management and responsibility for one's finances are assumptions guiding regulation. Regulation within neo-liberalism assumes that consumer credit is beneficial by permitting income smoothing over an individual's life cycle, for example permitting younger consumers to accumulate assets during periods of low income and addressing temporary income deficits.[37] Facilitating access to consumer credit may also contribute, albeit indirectly, to alleviating poverty in developing countries.[38] The promotion of fairness in credit contracts is not, in itself, incompatible with neo-liberalism since a fair market promotes confidence and expansion of the market. This was the underpinning for the

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[32] For a useful mainstream account see the UK Financial Services Authority Financial Risk Outlook (2009).
[33] See A Offer *The Pathology of Affluence* (Oxford, OUP, 2006).
[34] See Gowan (op cit), Graham Turner, *Credit Crunch* (2008)
[35] See Montgomerie op cit
[36] Economic growth under New Labour was "sustained by high levels of consumption, which has been driven by easily available credit, which in turn has led to high levels of debt and insolvency…[d]emand has been driven by a consumption binge that was NICE while it lasted—but the hangover may be worse" Consumption expenditure was driven by housing bubble and a 'spend, spend, spend' mentality'.M Kitson & F Wilkinson 'The Economics of New Labour: policy and performance' (2007) 31 Camb J Econ 805 at 811, 814.
[37] See World Bank (2008) *Finance for All: Policies and Pitfalls in Extending Access* (2008) c.3. See also D. Karlan & J. Zinman "Expanding Credit Access: Using Randomized Supply Decisions to Estimate the Impacts" (2006) **http://papers.ssrn.com/sol3/papers.cfm?abstract_id=982921(accessed 31.07.08).**

[38] See Karlan & Zinman above.

overall structure of the UK Consumer Credit Act 1974 which included a mandatory licensing scheme for all credit providers.

The central institutions and policies advocated for consumer credit markets within neo-liberalism are: (1) credit bureaux and positive credit reporting, (2) truth in lending, (3) financial literacy, and (4) financial ombudsmen.[39] Securitization was also promoted as a measure to increase liquidity particularly in developing countries but the institutional structure of securitization created dangers for consumers and contributed to the instability of financial markets. Its future within consumer lending remains uncertain. The four institutions outlined above respond to information asymmetries facing both suppliers and borrowers and are intended to recreate the conditions of a perfect market. Ombudsmen address individual enforcement costs. These regulations will create what the World Bank describes as the optimal "rules of engagement" for creditors and debtors. This model assumes that it is possible to reduce the imbalance between consumers and providers by recreating the conditions of a neo-classical market—addressing informational market failures and redress costs. The premises of UK consumer policy (and the World Bank) are that the discipline of "empowered" consumers will drive a virtuous circle of increased competition, innovation and productivity.

Neo-liberalism is often associated with individualised enforcement through private rights. However, the need to maintain consumer confidence and the legitimacy of the credit system in the face of market failures and scandals often results in pressure for regulation and what Harvey describes as the paradox of "intense state intervention" primarily through experts " in a world where the state is supposed not to be interventionist".[40] In the UK there is *ex ante* control of suppliers' access to the market.[41]

A neo- liberal model must also deal with the inevitable problem of default in a society committed to high levels of credit. In the business context the World Bank, influenced by the law and finance literature, underlines the importance of clear and easily enforced creditor rights in encouraging general credit availability.[42]It is relatively silent on the treatment of consumer overindebtedness. In the consumer context the potential social costs of overindebtedness for a debtor and third parties may not be accurately priced in the original transaction. If creditors are repeat players and are able to develop systematic advantages in using the courts as part of a collection routine there is a danger that rapid enforcement which does not scrutinise closely the validity of the underlying debt will result in overlending and the sanctioning of sharp practice.[43] The system for regulating default may affect the perimeters of credit although the empirical effects of debtor-oriented or creditor-oriented rules on secured and unsecured consumer credit granting remains contested. The US debtor oriented regime of open access to consumer bankruptcy, which existed

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[39] See The World Bank Consumer Protection and Financial Literacy, Good Practices for Consumer Protection and Financial Literacy in Europe and Central Asia - Consultative Draft (2008) . See also "Slovakia: Technical Note on Consumer Protection in Financial Services Vol 1p3. This World Bank study relied on EU Directives, the reports of European financial regulatory and supervisory agencies, the FTC and SEC, 2003 OECD Guidelines for Protecting Consumers from Cross Border Fraud and the 1999 United Nations Guidelines on Consumer Protection.

[40] D. Harvey *A Brief History of Neo-Liberalism* (Oxford: OUP) (2005)

[41] *Ibid*., p. 163.

[42] For the law and finance literature see La Porta et al op citand for an application to a developing country. A Kumar, Access to Financial Services in Brazil (World Bank, 2005).

[43] This point was developed by T G Ison in Credit Marketing and Consumer Protection.

before the 2005 reforms promised an early re-entry to the credit society for a debtor and spread the costs of debt default among private creditors, creating incentives for them to monitor consumer behaviour. It co-existed with the most liberal credit regime in the world. .

The detailed ground rules of consumer credit contract law have an impact on an individual's bargaining power[44] and create a model of how each party should treat the other throughout the transaction. The World Bank is relatively cursory in its discussion of the ground rules of consumer credit contracts. It recognises the necessity of ground rules for credit contracts, including controls on default rates as part of an effective consumer protection framework. However it cautions that such regulation might restrict contractual freedom "to make contracts that may in some cases be more appropriate".[45]

Neo-liberalism is sceptical of using market rules to redistribute the costs of market transactions, for example, through interest rate ceilings [46]. Any redistribution should be made by the state through the tax and transfer system. In addition, direct product regulation is shunned as a limit on innovation. .

Neo-liberalism does not mean therefore the absence of regulation. Nor is it limited to an "informational" approach to consumer protection. This ideal type of neo-liberalism is often associated with Anglo-Saxon (common law) jurisdictions such as the UK and the US. French civil law jurisdictions, it is argued, are more likely to protect an individual from the market. However, in practice even within Anglo-Saxon jurisdictions there are often political pressure for regulation of consumer credit. The elasticity of the market failure concept and the need to respond to scandals and outrages (e.g. concerns about "loan sharks") and maintain the legitimacy of the financial system may result in a significant regulatory response[47]. In societies of high inequality such as the UK and the US, where low income consumers pay much higher credit costs than middle class consumers, thereby undermining the impact of state transfers, the legitimacy of the credit system is always open to criticism.

Challenges for neo-liberalism

1. Competition for innovation or exploitation of behavioural biases?

A neo-liberal model assumes that more competition is a good thing for consumer markets. But aggressive competition in the credit market poses challenges for regulators. Given the long term nature of many credit relationships and the often short term behavioural biases of consumers, competition may often focus on the short term costs and contingencies rather than long term or lower probability events such as default costs. The case of credit cards is a well known example where firms may exploit consumers' behavioural biases--- individuals underestimate their future borrowing on cards—and competition focuses on short term benefits such as no annual fees with high prices on

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[44] I have argued for this in I Ramsay "Consumer Credit Law, Distributive Justice and the Welfare State (1995) Oxford Journal of Legal Studies.

[45] World Bank (2008) Diagnostic Review Czech Republic at 9.

[46] See World Bank *Finance for All?* (note 8), pp. 160 and 179.

[47] For example, in the UK in the early 2000s, the media highlighted the case of a couple whose mortgage loan had ballooned from £5000 to £348,000 because of compound interest on arrears. Questions were asked in Parliament and politicians promised to "do something" about "loan sharks".

longer term contingencies such as borrowing costs and default charges.[48] Bar-Gill has drawn attention to the potentially regressive and socially harmful aspects of this form of pricing. This general structure of pricing seems to exist in both prime and sub-prime consumer credit markets and was a subject of much criticism in the early 2000s .[49] The Competition Commission concluded that high cost payment protection insurance might be compensating for low margins on credit prices.

It is possible that what Barr, Mullainathan and Shafir describe as "high road" firms—those who view themselves as good corporate citizens—may not wish to adopt these pricing practices. However, they do so because they fear being at a competitive disadvantage in a market where it is difficult to correct consumers short term preferences and convince them that an alternative product, for example a credit card with an annual fee and lower interest might be more suitable.[50] The behavioural literature also challenges the view that consumer choices always reflect consumer preferences. A common argument against regulation of sub-prime lending practices such as payday loans is that it interferes with individual choice. But if choices do not always reflect preferences then the argument against regulation becomes weaker and undermines any a priori presumptions against regulation based on abstract concepts such as markets versus regulation. A close scrutiny of the potential harmful effects of biases in particular credit markets particularly the higher costs of credit mistakes for lower income consumers may justify regulation.

The behavioural literature has stimulated several distinct policy responses. First, there is the search for debiasing interventions through more imaginative disclosures and the exploitation of behavioural findings to design more effective "choice architectures"[51] for consumers. Although disclosure remains a central aspect of regulation there is much scepticism about the effectiveness of existing regulation and uncertainty as to what might work, particularly where consumers decision making problems are cognitive rather than informational[52] .The application of social science methods

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[48] See e.g. Bar Gill "Seduction by Plastic" discussed in Ramsay ch 10. For a study on the effect of psychological factors in credit marketing see M. Bertrand, D. Karlan, S. Mullainathan, E. Shafir & J. Zinman (2005) 'What's Psychology Worth? A Field Experiment in the Consumer Credit Market' http://ssrn.com/abstract=770389 (accessed 29.7.2008) concluding that "even in a market setting with large stakes and experienced customers, subtle psychological features that normatively ought to have no impact appear to be extremely powerful drivers of behaviour". See also R. Harris & E. Albin, 'Bankruptcy Policy in Light of the Manipulation in Credit Advertising' (2006) Theoretical Inquiries in Law pp. 431 et seq.

[49] See e.g. Bar-Gill on subprime pricing. O Bar Gill "The Law Economics and Psychology of Sub-Prime Mortgage Contracts" (2008) New York University Law and Economics Working Paper. On payment protection insurance see the Competition Commission in the UK . The pricing of overdrafts in the UK may also reflect these biases. See Office of Fair Trading, Personal Current Accounts in the UK, An OFT Market Study (October 2008).

[50] See M Barr, S Mullainathan and E Shafir, *Behaviorally Informed Financial Regulation* (New America Foundation, October 2008)

[51] See R.Thaler and C Sunstein *Nudge* (2008) for discussion of choice architectures.

[52] See for example National Consumer Council, Warning: Too Much Information can Harm ...(2007); S. Block-Lieb, R. Wiener, J.A. Cantone and M. Holtje (forthcoming 2009), 'Disclosure as an Imperfect Means for Addressing Over-Indebtedness: An Empirical Assessment of Comparative Approaches' in Niemi-Kiesilainen, Ramsay and Whitford ,*Consumer Credit: Debt and Bankruptcy: Comparative and International Perspectives* (Oxford: Hart 2009); I. Ramsay (2005), 'From Truth in Lending to Responsible Lending' in G. Howells, A. Janssen & R. Schulze Information Rights and Obligations, Aldershot: Ashgate, pp. 48-57. In relation to disclosure in US sub-prime markets see L. Willis, 'Decisionmaking and the Limits of Disclosure: The Problem of Predatory Lending: Price' (2006) University of Maryland Law Review pp. 707 et seq. D. De Meza, B Irlenbusch D Reyniers, "Financial Capability: A Behavioural Economics Perspective" (Consumer Research 69)

to understanding and measuring policy alternatives does not promise clear solutions and may increase uncertainty as to what might work. Second, information policies might be supplemented by changing default rules, requiring a consumer to affirmatively opt in to an increase in a credit limit. This approach retains consumer choice and autonomy, best described by Sunstein and Thaler as a form of libertarian paternalism[53]. Barr et al propose a"behaviourally informed financial regulation". This would be a Third Way approach going beyond what they perceive as a traditional dichotomy between either reliance on disclosure regulation or the use of usury ceilings. Their approach takes into account both behavioural biases and market analysis. They propose " sticky" default rules such as a standardised sub prime mortgage product without high costs attached to long term contingencies. Consumers could opt out but only if there are both heightened disclosures and a substantial legal liability on the provider if the loan turns out to be not appropriate for the borrower. This would permit innovation but only where it could be credibly explained to a potential borrower.

A third response to information deficits is greater standardisation of subsidiary terms in credit contracts where there is unlikely to be substantial competition between providers and/or where individuals are unlikely to be able to assess the risks of the term in advance.[54] Standardisation already exists in some financial contracts and the OFT has standardised default charges in credit cards.[55] The argument that standardisation stifles innovation and limits consumer choice should not be discarded but a greater burden might be placed on providers to substantiate these arguments. Standardisation might represent a "collective hands tying". For example, in an expanding competitive credit market few firms will stick to requiring downpayments from consumers even if individually they would deem it wise to do so. Finance Houses indicated to the Crowther committee that they supported the regulation of credit terms including required down payments in order to "protect a great many fools from their folly" but that they could not do so by voluntary agreement among themselves.[56]

2. Increased supply side information for profit maximisation or risk reduction and responsible lending?

Stiglitz and Weiss[57] highlighted the credit rationing effects of information asymmetry in credit markets. A major antidote to suppliers' informational problem in consumer credit markets has been the development of credit scoring and credit bureaux. Sophisticated computer technology has substantially reduced creditors' costs of storing and using credit information on an individual's

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FSA. Research does suggest that consumers do use the APR to compare credit choices. See Ramsay, Consumer Law and Policy at 539; Bar-Gill, "Sub-Prime" at 57.

[53] C Sunstein and R Thaler "Libertarian Paternalism is not an Oxymoron" (2003) 70 U Chi LRev 1159.
[54] See e.g. in relation to credit cards Ronald Mann, *Charging Ahead: The Growth and Regulation of Payment Card Markets* (2007) at 143 et seq. An example of the latter is changing the interest rate on a card retroactively i.e. applying it to existing balances. See the recent US Credit CARD ACT 2009 HR 627.
[55] Effectively reducing credit card penalty fees from £25 to£12. See OFT 842 *Calculating Fair Default Charges in Credit Card Contracts* (2006): Financial Times reported in 24 August 2006 that all 36 main credit card issuers had reduced their penalty fees to £12 in response to the OFT paper and threat to take further action against the previous level of default fees. The work of the OFT under the Unfair Terms in Consumer Contracts Regulations has also resulted in greater standardisation of subsidiary terms.
[56] Crowther para 82.22.
[57] J. Stiglitz & A. Weiss 'Credit Rationing in Markets with Imperfect Information' (1981) *American Economic Review* pp. 393 *et seq*.

creditworthiness. Standardised 'credit-scoring' systems for assessing creditworthiness have been developed by many major creditors. These techniques have facilitated the management of large numbers of small credit accounts – such as credit cards. Credit scoring has also facilitated 'risk based pricing' in the credit card market where credit card companies differentiate more finely between customers in relation to the level of interest payable on outstanding balances and use behavioural scorecards to determine whether to change interest rates on existing accounts.

The development of credit bureaux and credit scoring are central planks in the World Bank's vision of the development of credit markets[58] and the UK government views better data sharing as an important aspect of the control of over-indebtedness[59]. The Competition Commission concluded that better credit bureaux information on low income repayment patterns for home credit would facilitate individuals' access to lower cost credit[60]. Article 8 of the EU Consumer Credit Directive indicates that credit databases should be consulted "when appropriate" by prospective lenders.

The perceived economic benefits of credit bureaux and credit scoring are well known[61]: better assessment of risks and reduction of bad debts, more accurate pricing of credit, and facilitating new entry by reducing the competitive advantages of incumbent banks, increased penetration among higher risk groups. There is an international distinction between positive and negative credit reporting, the former providing a relatively full picture of an individual's payment history, the latter being limited to negative events such as bankruptcies, court judgment and defaults in payment. International financial interests and institutions have favoured positive credit reporting as a method of facilitating credit in developing countries and the entry of foreign financial institutions that can upset the informational advantages of local banks.[62] Countries with negative credit reporting e.g.[France, Australia] have lower levels of consumer credit outstanding than countries such as the UK and the US. Negative credit reporting may be expected to produce greater incentives to repay because in a positive system a borrower knows that one default may be discounted by a lender with a full picture of the financial position of the borrower.[63]

Credit information is not merely used to minimise risk but also to maximise profits[64]. Information may be used by credit card companies to segment markets, develop "behavioural scorecards" and target consumers who are likely to generate high profits through late payments and

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[58] See e.g. *Finance For All,* World Bank: World Bank, *Doing Business Project* ; M Miller *Credit Reporting Systems in the International Economy* (Cambridge Mass: MIT, 2003). For a discussion of credit information systems in Europe see F Ferreti The Law and Consumer Credit Information in the European Community (Routledge, London, 2008).

[59] See DBERR "Removing Constraints to the Sharing of Non-Consensual Credit Data" (February 2008) urn 08/591.

[60] See Competition Commission Home Credit Inquiry http://www.competition-commission.org.uk/rep_pub/reports/2006/fulltext/517.pdf .

[61] See ibid Appendix 2.1. for a summary of the benefits.

[62] See e.g. PERC Center for Competitive Credit "Economic Fairness Through Smarter Lending: Some Factors to Consider on the Eve of Brazilian Credit Reporting Reform" (October 2007) A review of the current regime of negative credit reporting in Australia concluded that the benefits of moving to a positive credit reporting system had not been sufficiently substantiated to outweigh the potential costs in terms of privacy and other costs. See The Report of the Consumer Credit Review (2006) at 280.

[63] A Padilla & M Pagano (2000) "Sharing Default Information as a Borrower Discipline Device" 44 European Economic Review 1951.

[64] See e.g. L Thomas, *Consumer Credit Models; Pricing Profits and Portfolios* (OUP: 2009). The description of this text indicates that "models allow one to make decisions that maximise the profitability of the borrower to the lender".

borrowing on a card. Less profitable consumers may be terminated. Thus the Egg credit card company terminated contracts with those customers who did not use the card frequently and regularly paid off their balances. Ronald Mann argues that through increased segmentation of the credit card market companies target some consumers with high fees while attempting to profit from higher income consumers through affinity cards with relatively high annual fees, whose benefits consumers often mistakenly assume outweigh their costs[65] . During the 1990s it was argued in the UK that credit scoring was used in the UK to exclude individuals from mainstream markets and facilitated the development of sub-prime lending.[66] Most recently credit card companies use risk based pricing to change the interest rate (sometimes by as much as 10%) for existing holders of cards.

Extensive information sharing may facilitate a deeper consumer credit market but not necessarily result in lower levels of indebtedness or even default. One study claims that 'countries with positive registries such as the UK, the US and Sweden…have high levels of indebtedness'[67]. These comments suggest some ambiguity about the overall effects of more creditor information: greater competition that could create incentives to 'oversell', more access to credit but not necessarily a reduction in the level of default. Positive credit reporting therefore has ambiguous effects: more lending, to possibly higher risk consumers but also the possibility of higher defaults as lenders use scoring as a method of increasing profitability rather than reducing risk.

Credit scoring also facilitates forms of lending where lending is centralized, staff costs are reduced through the absence of face-to-face contact through branches and credit processing is computerized. This may reduce the possibility of determining whether credit is suitable or appropriate to the needs of a particular individual rather than the profit maximisation of the lender There is therefore a tension between this form of credit granting and the development of an individualised responsible lending standard.[68]

There is remarkably little "hard" regulation of several aspects of credit bureaux and credit scoring practices in the UK[69] notwithstanding their central role in segmenting, including and excluding individuals from the credit market. .

3. **Upskilling consumers through financial literacy**?

During the past 10 years governments, other regulators and international institutions have joined with financial firms to promote financial literacy as a core element of consumer financial services market regulation. This development illuminates how neoliberal policy-making organises consumer protection policy around individualization, responsibilization and market expansion. In 2003, the OECD launched a "Financial Education Project", sponsored by Prudential plc's corporate responsibility program. Fuelled by beliefs that uneducated consumers cannot cope with the expansion of financial markets and the increased complexity of financial products, and by concerns about the

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[65] See Mann above at 137-138.

[66] See D Burton, D Knights, A Leyshon, C Alferoff & P Signoretta "Making a Market: the UK Retail Financial Services Industry and the Rise of the Complex Sub-Prime Credit Market" (2004) 8 Competition and Change 3.at 12-13 "complex sub-prime providers actually use much more sophisticated credit rating technologies through differential pricing according to the risk profile. This ensures that they make a profit regardless of the level of risk".

[67] European Credit Research Institute (2003) "Briefing on consumer credit, indebtedness and overindebtedness" prepared for the European Parliament Hearing on the Consumer Credit Directive 29 April 2003. (Brussels ECRI) p.5.

[68] See Consumer Credit Directive art5.

[69] Primarily located in the Consumer Credit Act 1974 and the 1998 Data Protection Act

consequences of consumers spending too much and saving too little, this project encourages countries to develop effective regulatory policies to enhance financial literacy. Its publications, which include a substantial report on financial literacy education and a policy paper to guide countries in the development of educational programmes,[70] characterise financial illiteracy as an urgent and pervasive problem for financial markets, and represent literate financial consumers as 'regulatory subjects' whose decisions will increase price competition among suppliers and stimulate innovation.[71] Bolder claims also appear in the Report to the effect that financially literate consumers will improve economic growth in all types of economies, as well as help to reduce poverty and potentially moderate the volatility of financial markets in emerging economies.[72]

Recent national initiatives to promote financial literacy (or financial capability) include: Australia's Consumer and Financial Literacy Task Force (2004) which led to the establishment of the Financial Literacy Foundation in 2005; L'institut pour l'Education Financière du Public (IEFP) created in France in 2006; the New Zealand Retirement Commission's "Sorted" programme, the U.S. Federal Government's Financial Literacy and Education Commission,[73] and the U.K's National Financial Capability strategy (2003), a multi-agency programme of consumer enhancement that is led by the FSA and heavily backed by HM Treasury.[74] Although the particular mandates and specific goals of these initiatives vary, it is common for their work to be characterised as "empowering consumers" at a minimum through the provision of information, the development of financial skills and the activation of a consumers' sense of financial responsibility.[75] These policy initiatives link the enhancement of consumers' financial capabilities to their responsibilization through the idea that financial literacy improves the capacity of consumers to protect themselves against risks of "mis-buying" and mis-selling of financial products. A second important linkage is the idea that financial literacy fuels demand for financial products as consumers become more active and more self-reliant – that is, more self-regulating – about how they manage income smoothing and their future economic security. As consumers become more capable and therefore responsible they in turn are supposed to reduce the need for regulatory intervention.

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[70] OECD, *Improving financial literacy: analysis of issues and policy* (OECD Publishing, Washington 2005); OECD 'Recommendation on Principles and Good Practices for Financial Education and Awareness' (2005)

[71] *Ibid* Improving Financial Literacy at 35. For extensive discussion of the financial consumer as regulatory subject, see Williams, Toni, 'Empowerment of Whom and for What? Financial Literacy Education and the New Regulation of Consumer Financial Services' (2007) 29(2) Law & Policy 226.

[72] .(OECD, 2005a, p. 35)

[73] This agency was established under Title V, the Financial Literacy and Education Improvement Act, which was part of the Fair and Accurate Credit Transactions (FACT) Act of 2003. Its functions are to: "coordinate the financial education efforts throughout the federal government, support the promotion of financial literacy by the private sector while also encouraging the synchronization of efforts between the public and private sectors." There is a vast array of state, private and NGO financial literacy initiatives in the US, most are very recent, e.g. a 2006 report found that only about one in four US financial literacy programmes started before the late 1990s, Financial Literacy and Education Commission, *Taking Ownership of the Future: The National Strategy for Financial Literacy,* (Washington: Financial Literacy and Education Commission, 2006) p. 97.

[74] Financial Services Authority, 'Building financial capability in the UK' FSA (2003); Financial Services Authority, *Building financial capability in the UK* (FSA, London 2003); Financial Services Authority, 'Towards a national strategy for financial capability' FSA (2003); HM Treasury 'Financial Capability: The Government's long-term approach' (2007) ; HM Treasury and Financial Services Authority 'Helping You Make the Most of Your Money: A Joint Action Plan for Financial Capability' (2008)

[75] e.g. (Basic Skills Agency & Financial Services Authority, 2003, p. 4) (Financial Services Authority, 2003c, p. 5). (Financial Services Authority, 2003a) headlines its section titled "What we want to achieve" with "We share a vision of better informed, educated and more confident citizens, able to take greater responsibility for their financial affairs and play a more active role in the market for financial services", at 2.

Financial literacy has become almost an international crusade and it is difficult to find balanced discussion of its role in financial services. The idea of "responsibilizing" consumers by upgrading their financial capabilities fits neatly into strategies of governance in neoliberalism where suitably upgraded consumers in the credit market will become part of the supposed virtuous circle of driving competition, innovation and productivity in financial services. Consumers will also, it is argued, be able to avoid the problems of overindebtedness through better financial management. Financial literacy has become part of the professional discourse of policy makers and the helping professions. There remains however much that is untested in the financial literacy literature and a review of behavioural finance suggests that it is not absence of information but behavioural biases which cause consumers to make repeated mistakes in credit markets[76].

4. Low cost redress: financial ombudsmen

A financial ombudsman disposes of disputes between consumers, small businesses and financial institutions. The financial ombudsman has become an international institution, since its emergence in the UK in the early 1980s.[77] Its characteristics are its ability to determine issues on broad fairness grounds, specialist knowledge, the absence of costs to consumers, the requirement for firms to develop internal complaint systems, and the possibility of identifying patterns of misconduct which can be addressed by regulators. An ombudsman can be therefore part of a meta-regulatory strategy to ensure the responsiveness of large organisations.

Experience in the UK indicates that the FOS has provided a useful service to primarily middle and upper middle class consumers [78]. The FOS now has a large caseload with 127,000 new cases in 2008 and 8,674 cases resolved. ..[to be concluded]

III. A Consumer Credit Safety Commission? The UK Regulatory Triangle

Bar-Gill and Warren proposed a "new deal" consumer credit safety commission which would provide *ex ante* credit product regulation, with the possibility of rulemaking and regulation of the product rather than particular sellers.[79] This model has been adopted by the Obama administration in the proposal to establish a new Consumer Financial Protection Agency[80]. A variation on this model already exists in the UK where the OFT licenses unsecured credit providers and the FSA secured credit providers. Both the OFT and the FSA now have the power to monitor and regulate the business model of credit providers and the addition of irresponsible lending to the criteria for licence revocation provides the OFT with a significant lever for regulating lending practices throughout the course of a transaction. [81]

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[76] See De Meza et al op cit.

[77] See discussion in Ramsay, Consumer Law and Policy Oxford Hart (2d ed) 2007 at 239-254.

[78] The 2008 Annual Review indicates increasing numbers of consumers using the service in the C1 and C2 categories reflecting the growth of its consumer credit jurisdiction and the decline in mortgage endowment cases.

[79] "Making Credit Safer" op cit.

[80] For the details see the US White Paper of June 17 2009 "Financial Regulatory Reform: A New Foundation" at 55et seq

[81] The 2006 amendments to the 1974 Act now permit the OFT to take into account the business model of a firm in assessing its fitness to hold a licence and "irresponsible lending" is included as a criterion in deciding whether to grant or revoke a credit licence. See CCA s25 (2), (2A(e) and (2B). The OFT is under an obligation

Credit licensing by the OFT in the UK had both efficiency and distributional objectives. From an efficiency perspective licensing compensated for general information and enforcement costs facing consumers. The distributional goal was the protection of lower income and vulnerable consumers who would have difficulties in seeking individual remedies against unfair credit practices. The licensing provisions under the 1974 Act did confer broad powers on the OFT to police "unfair practices" irrespective of whether they were proscribed by law. The Annual Reports of the OFT during the 1980s and 90s indicates that they used the licensing process as a method of identifying unfair practices, for example developing guidelines on unfair practices in the sub-prime (non-status) lending market. These practices included irresponsible lending, the use of dual interest rates, and negative option selling of credit insurance. The licensing process did function therefore as a nascent form of industry rulemaking of credit products. The perception was however that the OFTs information gathering and enforcement powers and practices were not effective and that the agency was underresourced . Although self-regulation also developed during this period, its coverage was least effective in higher risk lending. There was also little political support for the OFT during the 1990s while the Conservative government was in power. Indeed reform during this period focused on whether the costs of licensing (overinclusive and costly to administer) outweighed its benefits[82]. In contrast the regulatory impact analysis for the 2006 amendments to the CCA concluded that the costs to consumers and reputable businesses from deregulation would far outweigh the costs saved through deregulation.[83]

COMPARISON OF POWERS OF OFT/FSA WITH PROPOSED US CONSUMER FINANCIAL PROTECTION AGENCY

	CFPA	OFT	FSA
Rulemaking	√√	√	√√
Monitoring/Supervision	√	√	√
Ex ante Licensing for	√	√	√

to provide guidance on the fitness test (s25A),.Under s26 it may make conduct of business regulations.. The OFT has intermediate powers to impose requirements on a licensee where it is dissatisfied with the manner in which it is carrying on its business [s33A] and it has used these powers to impose conditions on debt collectors and on Citibank's standard form credit contract which excluded liability under s75 for overseas purchases. The Office is to prepare guidance on how it proposes to exercise these powers [33E] The Office also has information gathering [36C] and power to require access to observe the carrying on of business and to inspect documents [36C]. The Office proposes a risk assessment approach to credit licensing so that it can focus on higher risk areas such as debt collection, debt management and sub-prime lending. Sub-prime and home lenders will be required to provide a credit risk profile to ensure that they are not lending irresponsibly. See "Consumer Credit Licensing" (OFT 969, January 2008)

The FSA rule-making powers are found in Part X of the Financial Services and Markets Act 2000.

[82] See discussion in Ramsay Consumer Law and Policy (2d ed) at499 et seq

[83] See Consumer Credit Bill Full Regulatory Impact Assessment at 48-49.

safety, fairness			
Enforcement	√	√	√
“Outcomes based approach”	√	?	√
Measures to ensure responsiveness to consumer interests	√	√	√
Funding by industry	partly	Licensing activity funded	√
Separate from prudential regulator?	√	√	X
Promoting Credit Access to underserved groups	√	x	?

The OFT has also engaged in credit industry rulemaking through its general power to enforce unfair contract terms under the UTCC regulations implementing the EU Directive. Thus it has set the terms for default rates on credit cards and currently is engaged in regulation of overdraft charges.[84]

The new OFT licensing model is based on the licensing powers of the Financial Services Authority whose jurisdiction since 2004 includes first charge mortgages and credit insurance. Retail financial services are regulated through conduct of business rules but in recent years the FSA adopted what regulatory scholars describe as a meta-regulatory approach, requiring financial firms to embed general principles such as “treating customers fairly” within their business model and organisational culture. It now refers to this form of regulation as “outcomes based” regulation and treating customers fairly requires a number of “consumer outcomes”[85]. These include: “consumers can be confident that they are dealing with firms where the fair treatment of customers is central to corporate culture and is automatically taken into account in all relevant business decisions”; “products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly”: and “consumers are provided with products that perform as firms have led them to expect and the associated service is both of an acceptable standard and as they have been led to expect”. The FSA expects fair treatment to be “established throughout the firm not just in systems and controls but in business culture including strategy, training, remuneration, and

[84] See discussion in Ramsay “Consumer Law and Policy” op cit at 476-485.
[85] See FSA “Treating Customers Fairly: Measuring Outcomes” (2007) which lists the six consumer outcomes.

staff behaviours". Senior management must have adequate information to monitor TCF. Firms must not rely solely on consumer satisfaction studies to determine whether there is fair treatment of consumers since consumers may be satisfied with an unsuitable product and dissatisfied with a fair product. The FSA's approach does not depend on prescriptive rules and action against deviant firms but is intended to embed attentiveness to consumer welfare into the working rules of financial product design, development and marketing and financial contract formation, performance, complaint handling and redress. While this approach ultimately harnesses self-regulation the FSA has been active in inspecting firms to identify progress with its initiative and taking enforcement action where it identifies significant violations of the principles.

The FSA has been active in its regulation of the sub-prime credit industry since taking over this jurisdiction in 2004. In 2005 the FSA highlighted to firms the importance of making a suitability assessment and treating consumers fairly when selling payment protection insurance[86]. The 2005 review concluded that many firms visited had inadequate documentation to demonstrate suitability when advising on mortgage products. The Authority responded through individual feedback, a "dear CEO letter" and enforcement actions. In 2007 it conducted a further review of substantial numbers of lenders and intermediaries in the sub prime lending market . The review revealed that in the case of intermediaries one third of files showed an inadequate assessment of consumers' ability to afford the mortgage and in almost half the files there was an inadequate assessment of customers' suitability for the mortgage. "Significant numbers of consumers were advised to re-mortgage, thereby incurring early repayment charges, without the adviser being able to demonstrate that this was beneficial to the customer. None of the lenders adequately covered all relevant responsible lending considerations in their policies" and " there were also failings by lenders to monitor the application of their policies, which resulted in the approval of potentially unaffordable mortgages." Five firm were referred for enforcement action.

Payment protection insurance which is often sold with sub prime loans[87] and is part of the business model of selling sub-prime credit[88] has been a target of FSA regulation. Problems with misselling were identified in the 2005 visits to firms in the sub-prime market and from 2006 the FSA took high profile action against large institutions such as HFC, GE Capital and Citigroup [Egg Credit Card] concerning the misselling of credit insurance.[89] HFC (Household Finance) a subsidiary of HSBC was fined over £1 million for its misselling practices. It sold single premium insurance with 75% of its consumer loans which are primarily made to working class and lower middle income consumers. The investigation by the FSA of its internal practices revealed that its procedures for training and monitoring staff were inadequate and that these resulted in an "unacceptable risk of unsuitable sales". The need to monitor staff was heightened by the existence of a bonus structure for meeting sales targets of PPI. In addition to a substantial fine, HFC undertook an independent audit of its compliance and contacted consumers who may have been missold insurance to identify possible

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[86] See http://www.fsa.gov.uk/pages/Library/Communication/PR/2005/095.shtml
[87] See Competition Commission Market Investigation into*Payment Protection Insurance* at para 11 "PPI Consumers are more likely to earn less than the national average income or come from socio-economic groups C and D"
[88] The practice of finance companies selling insurance with credit is known in the US as "insurance packing" "shoving as much insurance onto the customer as possible without the customer's knowledge or without the customer's understanding" Statement of "Jim Dough" to Hearings Before the Special Committee on Aging US Senate (105th Congress) (2d Session) (March 16 1998).
[89] The FSA took action against 20 firms for poor selling practises in relation to PPI. See http://www.fsa.gov.uk/pages/Library/Communication/PR/2009/031.shtml.

compensation. [90] The report of the FSA action also revealed the business model of HFC which involved much refinancing of loans which provided opportunities for selling larger loans, more insurance, and settlement fees. The FSA has now required all firms not to sell single premium payment protection insurance.[91] A consequence of these and other investigations (by the Competition Commission) is that payment protection insurance may no longer be a major supra-normal profit centre for financial institutions. [92] The demise of single premium ppi might be analogised to recall of a potentially dangerous product.

There are several points of interest in the FSAs approach to regulation. First, it is a form of ex ante regulation in the sense that firms must not market dangerous products or have marketing structures that create an unreasonable risk of misselling. Second, the regulator opens up the black box of corporate decision making, requiring firms to develop a business model which does not create this unacceptable risk.. Third,, the FSA has significant informational and monitoring powers. Firms must make monthly reports and are subject to audit visits particularly if they are operating in a potentially higher risk sector. Fourth, the agency has the power to award redress and in a number of cases required companies to write to existing customers with policies outlining the possibility of redress.[93] Fifth, the FSA has gradations of penalties ranging from informal feedback, "dear CEO letters", through financial penalties and the possibility of licence revocation.

The FSA approach is a potentially promising model of consumer credit regulation. However we are aware of potential criticisms . First, Baldwin has pointed to the difficulties of regulators attempting to harness internal organisational structures where there may be confusion and conflict over roles and a tension between shareholder return and regulatory risk.[94] The continued misselling of ppi by large "reputable" organizations after being warned of the dangers by the regulator and in some cases the receipt of a "Dear CEO" letter might support Baldwin's argument or simply suggest that these firms were amoral calculators and therefore unlikely to be able to change their culture. Second, there is the perennial problem of "capture" of agencies by particular interests. This concern has underpinned much UK regulatory thinking during the past decade with the growth of a variety of accountability mechanisms within government and in the case of the FSA the existence of the Financial Services Consumer Panel.[95]. There is little evidence of capture of the agency by any single interest group and the capture theory does not in any event adequately describe the complex interdependence between powerful actors in particular regulatory spaces where "no single actor can hope to dominate the regulatory process"[96].

There is also the role of the FOS and the OFT within the regulatory structure. The former can play an informational role in identifying potentially unfair credit practices in its dispute settlement work and acting as a catalyst for regulatory action. Financial service companies must establish

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[90] The decision indicates: "As a result of the review HFC is in the process of making a significant number of changes to its sales processes. It has also agreed to strengthen its compliance monitoring and oversight arrangements. HFC has also committed to a robust remedial action plan, overseen by third party accountants, involving a programme of customer contact and, if appropriate, steps to ensure that its customers are not disadvantaged."
[91]"FSA wants all firms to stop selling single premium PPI"
24 February 2009 http://www.fsa.gov.uk/pages/Library/Communication/PR/2009/031.shtml
[92] The Competition Commission calculated a return on equity of 490 percent for ppi. See Competition Commission Final Report Payment Protection Insurance (29 January 2009).
[93] See e.g. Final Notice Egg Credit Card 9 December 2008.
[94] R Baldwin, "The New Punitive Regulation" (2004) 67 MLR 351.
[95] See ss8 and 10 FSMA 2000.
[96] Black, 2002 at 00.

appropriate complaints procedures. The existence of the OFT with some overlapping jurisdiction provides the possibility of regulatory competition and the existence of regulatory redundancy. This UK regulatory triangle is complemented by the existence of the "supercomplaints" process which permits consumer groups to place issues [such as ppi] on the regulatory agenda[97]. Third regulators, like consumers, might also be affected by behavioural biases with the danger that they were overconfident in their judgments, responding to highly visible (though not necessarily serious) issues. There are however significant controls on this in contemporary UK regulation through the requirements of RIAs, treasury oversight etc.

A key question is the regulation of "new" products, balancing protection against the value of fostering innovation. For example, how should an agency react to novel products such as payday loans or equity release mortgages where there may be uncertainty as to who will benefit? One possibility would be to apply a precautionary principle to a new product with an initial burden on credit providers to indicate the benefits of the product . The application of this principle to credit products might possibly have protected consumers against some of the initial problems with equity release products. There is always the danger here that existing firms may oppose new entrants (at least until they are able to determine whether it is worth developing the product).

The effectiveness of credit safety licensing depends on high quality information to identify potentially unsafe credit products and the ability to devise a regulation that can achieve an optimal level of safety without unnecessarily decreasing the availability of credit or innovation. Experience of consumer safety regulation indicates that private groups inevitably play an important role in information gathering and standard setting in regulation. Establishing product safety standards is a complex blend of technical expertise and responsiveness to political pressures The FSA is in a continuing dialogue with its stakeholders so that there is the potential to blend both technical expertise and political responsiveness.

The increasing use of broad standards such as responsible lending[98] also argue in favour of the FSA approach. A standard such as responsible lending is subject to the critique that it may increase costs (e.g. legal advice) and uncertainty for lenders which may in turn result in a hesitate to lend to more marginal credit risks. Reliance on private litigation to develop the concept of responsible lending suffers from several drawbacks; the difficulties of courts establishing useful standards to be applied within bureaucratic organizations: the reactivity and lack of expertise of courts, and knowledge about how to change organizational behaviour: the likelihood of being subject to the biases of the litigation strategies of repeat players. The experience of standard setting to protect bank loan guarantors illustrates these limitations. A public regulator will be in a better position to develop guidance, encourage the development of best practices within an industry and monitor the potentially changing nature of the concept of responsible lending.

Regulation is inevitably affected by the political climate towards regulation. It may be difficult for an agency to maintain a cautious approach during a market upswing. One method of compensating for this might be the UK supercomplaint procedure[99] which permits consumer groups

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[97] See s11 Enterprise Act 2002. Supercomplaints have been made in relation to ppi, home credit and credit card practices.
[98] A form of responsible lending is implicit in article 5.6 of the 2008 EU Consumer Credit Directive currently being implemented in the UK.
[99] Supra

to require an agency to respond to a potential market problem, permitting such groups to set the regulatory agenda.

Does the UK structure provide a model for drawing on both public and private actors in the area of consumer credit and achieving efficient and fair markets through regulation which is both effective and accountable? This is an important contemporary question as scholars compare European and US approaches to regulation in a number of areas and the Obama administration propose an agency similar to the FSA. Further comparative analysis would be beneficial in this area although there are substantial difficulties in carrying out such research.[100] The UK model seems at first sight distinct from the stylised description of US consumer protection based on regulation through litigation, the central role of "lawyer entrepreneurs" and a culture of adversarial legalism[101].

IV Conclusion

There are significant limits on consumers as " a market discipline" in credit markets, even if suitably responsibilized through financial literacy . There is therefore the need for greater controls on the supply side of the market in terms of regulating both fairness and the type and manner of product marketing. We have suggested that a suitably resourced FSA or OFT has the potential to meet this need. . Regulation promises greater fairness, perhaps slightly lower prices and greater choice for lower income consumers. Fairness within this approach does not however prevent the Poor from paying more than middle income consumers for credit. In addition, the ultimate objective of promoting confidence in an expanding market for credit assumes that the promotion of access even at very high prices rather than protection from credit is the starting point for analysis. The assumption that credit is "a good thing" will prevent any broad scale measures such as interest rate ceilings, or terms control which would dampen demand. Of course it is precisely this issue of how much credit is "a good thing" which is raised by the credit crunch.

Affordable access to credit for low income consumers, particularly for short term loans remains a problem. A recent history of working class credit concludes that "cheap credit remains elusive for the depressingly large number of families who still have to manage on limited budgets...unfortunately the liberalization of credit that accompanied the great leap into the consumer society has not produced a simple solution for the economic problems of the poorest groups. For them easy terms remain elusive." The UK government in response to the credit crunch is now promoting the mutual sector including building societies and credit unions as methods of providing and alternative to the mainstream banks. [102] Crowther noted in 1970 that "mutual aid ..." was not part of the British tradition in credit compared with the growth of credit unions in other countries." Historically, apart from building societies before they were demutualized, there has been a relative absence of non-

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[100] See Howell Jackson on the difficulties of comparative analysis of the effectiveness of enforcement of securities legislation. Howell E. Jackson, Variation in the Intensity of Financial Regulation: Preliminary Evidence and Potential Implications, 24 YALE J.REGULATION 253 (2007) . One of the authors has drawn attention to the difficulties of comparing consumer bankruptcy across jurisdictions. I Ramsay, Comparative Consumer Bankruptcy (2007) Illinois LRev 241.

[101] See F Cafaggi and Hans-W Micklitz "Administrative and Judicial Enforcement in Consumer Protection: The Way Forward EUI Working Papers Law 2008-09.

[102] See Treasury Financial Inclusion 2008-11 at 2.11 where support for third sector lenders is " at the heart" of government strategy to provide affordable access.

market institutions providing credit. In the 19th century private pawnbrokers were known as the poor man's bank and hire-purchase, moneylenders, and home collected credit provided working class credit. We have the impression that the UK has tended to assume that its approach to credit and regulation reflects a more "modern" and rational approach than countries such as Germany and France. The credit crunch has clearly challenged that assumption and further comparative work within Europe may deepen our understanding of the nature and role of consumer credit and the effects of different forms of regulation.

Appendix 1 : Fines imposed on firms selling PPI for TCF failures, 2006-2008.

Year	Firm	Amount	Summary
2006-09	Regency Mortgage	£56,000	Failures in mortgage related PPI sales in the sub prime market
2006-10	Loans.co.uk Limited (LCUK)	£455,000	PPI selling failures
2006-11	Capital Mortgage Connections Ltd (CMC)	£17,500	Breaches including cold calling potential customers and PPI failings
2006-12	Redcats (Brands) Ltd	£270,000	Failing to treat customers fairly when selling Payment Protection Insurance (PPI) in connection with home shopping products
2006-12	Home and County Mortgages Limited (HCML)	£52,500	Management failures and a lack of skill, care and diligence
2007-01	G.E. Capital Bank	£610,000	Systems and controls failings in selling insurance including Payment Protection Insurance, and failing to treat its customers fairly.
2007-02	Capital One Bank (Europe) plc	£175,000	Not having adequate systems and controls in place to sell payment protection insurance and for failing to treat its customers fairly.
2007-09	Hadenglen Home Finance	£133,000	For inadequate systems and controls when recommending re-mortgages and Payment Protection Insurance (PPI) to customers.
2007-09	Richard Hayes, Chief Director of Hadenglen	£49,000	For inadequate systems and controls when recommending re-mortgages and Payment Protection Insurance (PPI) to customers.
2008-01	HFC Bank Ltd.	£1,085,000	For failing to take reasonable care to ensure that the advice it gave customers to buy Payment Protection Insurance (PPI) was suitable, and for failing to have adequate systems and controls for the sale of PPI.

Year	Firm	Amount	Summary
2008-05	Land of Leather	£210,000	For allowing its sales force to sell PPI on loans without effective monitoring or training in place to ensure that the insurance was being sold fairly
2008-05	Mr. Briant in relation to Land of Leather	£14,000	For failing to properly oversee the sale of PPI by Land of Leather Limited
2008-07	Liverpool Victoria Banking services	£840,000	For serious failings in the sale of single premium Payment Protection Insurance (PPI)
2008-08	GK Group Limited	£51,100	for serious breaches relating to the sale of Payment Protection Insurance (PPI)
2008-08	George White Motors Ltd.	£28,000	for serious breaches relating to the sale of Payment Protection Insurance (PPI)
2008-08	Park's of Hamilton Holdings Ltd	£61,600	for serious breaches relating to the sale of Payment Protection Insurance (PPI)
2008-08	Ringways Garages (Leeds) Limited & Ringways Garages (Doncaster) Limited	£35,000	for serious breaches relating to the sale of Payment Protection Insurance (PPI)
2008-09	Alliance and Leicester	£7,000,000	for serious failings in its telephone sales of payment protection insurance
2008-12	Egg Banking plc	£721,000	For serious failings in its sales of credit card payment protection insurance (PPI).

Appendix 2 The UK and France: Contrasting approaches to regulation?

Is UK credit regulation a neo-liberal model ?

The UK is often identified as a neo-liberal country notwithstanding New Labour's claim to stake a "Third Way" in policy making by blending the market with social values. Government policy views consumer credit as a beneficial product and the maximum number of consumers should have access to credit. This public policy can be traced to the influential Crowther report in 1970 which established the "post-war orthodoxy on credit"[103]. This report, chaired by an economist and former editor of *The Economist* argued for a "competitive environment which will ...offer every incentive for innovation and experiment". The starting point for the report was that the "state should interfere as little as possible with the consumer's freedom to use his knowledge of the consumer credit

[103] See G Borrie, "The Credit Society: Its Benefits and Burdens" (1986) Journal of Business Law 181.

market to the best of his ability and according to his judgment of what constitutes his best interests". [104] Policy should not attempt to limit freedom of access but should help the "minority who innocently get into trouble to manage their financial affairs more successfully...the basic principle of social policy must therefore be to reduce the number of defaulting debtors".

According to Crowther consumer protection legislation would primarily address market failure caused by information with licensing of creditors as both a control on unfairness and a limited distributional goal of protecting low income consumers who would have difficulties in protecting themselves through individual litigation. The Committee endorsed some risk and loss spreading in protections for defaulting debtors. The introduction of connected lender liability was justified partly by noting that "in considering which of two relatively innocent parties should bear the greater loss, it is much easier for the business creditor to do so than the individual debtor." The Committee was however concerned that this risk spreading should not go too far since it would result in the "good customer" subsidising the "bad customer". The Committee concluded that there was little that consumer protection policy could do for the poor except provide protection against hardships caused by repossession and the enforcement of judgments. Even here the committee was concerned that "every restriction on a creditor's remedy must be paid for". Fairness rather than subsidised redistribution was the objective.

The Committee did assume that consumer credit existed within the backdrop of a welfare state and that individuals should not have to meet basic needs by borrowing at interest rates over 100 per cent. This problem should be solved through "social welfare services rather than by the granting of loans at enormous interest rates" [para 6:6.6]. The subsequent CCA 1974 legitimised consumer credit. It would hopefully eliminate the fly by night from the market (through the licensing regime) and many large credit grantors supported the Act. Regulation was a pre-condition for the development of a mass market for consumer credit and the Act was enacted by a conservative government.

Between the 1970s and 2003 there was a transition from producerism to consumerism in politics so that increasingly it is the consumer who is conceptualised as the primary legitimator and beneficiary of policymaking. [105] The growth of secured and unsecured consumer credit was facilitated through the abolition of terms control on hire-purchase and the Bank of England "corset" on lending, the liberalization of housing finance and the ability to use home equity as a source of general financing. This "democratisation" of credit could be viewed as representing a neo-liberal vision of the empowered consumer with a right to choose---a project carried on by New Labour with its emphasis on 'extending choice for the many, not the few' [Blair, 2003]. David Harvey argues that these changes in financial services provision brought " more and more of a debt culture into the centre of a formerly staid British life" (Harvey, 2005: 61-62). There was also a growth in inequality during this period and consumer credit could substitute for relatively stagnant income growth. The "sub prime" market such as doorstep lending substantially increased during this period. Given the defining role attributed to consumption and consumerism in contemporary society, inequality in the price of access to consumption because of high credit costs takes on an increased salience and affordable access to credit has become an important –but tantalisingly difficult to achieve—objective.

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[104] For general background on development of consumer credit see I Ramsay, *Consumer Law and Policy: Text and Materials on Regulating Consumer Markets* (Oxford, Hart 2d ed 2007) ch 10.
[105] Whitman, James Q. (2007) 'Consumerism versus Producerism: On the Global Menace of "Consumerism" and the Mission of Comparative Law' 117 Yale LJ 340

During the decades of the 1980s and 1990s the redistributional aspects of the Consumer Credit Act 1974 were the least effective. Credit licensing was perceived to have failed to protect subprime consumers and the vague "extortionate credit bargain" provisions—regarded as a substitute for interest rate ceilings—were little protection against high credit prices in the sub-prime market. Leyson and Thrift documented the growth of financial exclusion in the 1990s as financial institutions withdrew from low income neighborhoods. Any reform proposals during this period were primarily deregulatory and a review of the Act in 1994 commented that "perhaps the greatest strength of the Act is that it does not seek to meet its objectives through interventionist actions such as interest rate capping or direct control of the substance of contracts. Rather it explicitly endorses freedom of contract within a framework designed to ensure openness: consumer protection is attained in large part through measures to ensure that full and truthful information about credit contracts is available to consumers". [OFT, 1994] The major beneficiaries of the Act were middle class consumers who used credit cards and could take advantage of the connected lender provisions of the Act to hold companies liable for defective purchases. The new Labour government promised in its 1997 manifesto to "get tough" with loan sharks and predatory lending practices, as well as modernise the Act.

In 2003 the White Paper on Consumer Credit stated that "consumer credit is central to the UK economy"(for consumer credit read "the financial services industry"). The government wanted to encourage an "open and fair credit market, where consumers can make fully informed decisions and businesses can compete aggressively on a fair and even basis" [para 1.69]. Fairness would be provided through a beefed up licensing regime, and a more consumer friendly unfairness test (replacing the extortionate credit bargain test) which could be applied by both courts and ombudsmen. One difference between Crowther and the White Paper of 2003 was the recognition in the latter document of over-indebtedness and financial inclusion as problems of social justice [para 1.70]. Education and better access to advice would address overindebtedness but on affordable credit the White Paper states merely that "We want low income consumers to have access to affordable credit" [para 1.70]. The regulatory impact analysis of the Act indicated that a major objective of the reforms was to protect "vulnerable consumers".

The government also developed in the early 2000s an ambitious combination of measures to prevent and treat overindebtedness.[106] The objectives included assuring affordable credit, embedding responsible lending through a new consumer credit regime, encouraging a savings culture to avoid overindebtedness, and the provision of high-quality debt advice. The 'keys to the achievement of these goals' included the development of financial capability among the population, increases in credit unions, the development of alternative forms of affordable credit, and the introduction of a stakeholder suite of savings products. In addition to the consumer credit reforms the government would tackle illegal moneylenders, improve data sharing to promote responsible lending, provide better debt advice, improve insolvency procedures through a Debt Relief Order for low-income individuals with no assets, reform Administration Orders and strengthen repayment schemes. These priorities were underpinned by the government's aim to both create an efficient credit market and to

[106] See generally DTI/DWP, *Tackling Overindebtedness: An Action Plan* (London, TSO, 2004) 5–7.

‘advance equity in line with the Government’s wider social justice agenda’.[107] This is an ambitious agenda but the objective of affordable access has not yet been achieved.[108]

One striking consequence of the introduction of the supercomplaint process in the Enterprise Act 2002 has been the extent to which the Competition Commission has become involved in analysing analysing sub-prime and low income credit markets. The Commission, operating within a neo-classical economic framework, has proposed substantial reforms to subprime lending practices in order to make these markets more competitive.[109] In general its interventions have required greater information provision, opportunities for price comparison and reduction in switching costs. For example, in the home lending market—primarily used by consumers in socio-economic groups D and E—the Commission proposed greater comparative information for borrowers to reduce switching costs. The main home lenders must also record information about borrowers with credit bureaux to permit good payers to have the opportunity to graduate to a lower cost loan. These reforms may make these markets more competitive –individuals will be able to choose between lenders offering loans at 200% rather than 300%--but they will still pay a high price for credit. The Commission considered carefully whether interest rate ceilings should be introduced but concluded that it might make short term loans less available.

The UK now has a dense and overlapping system of state and “soft law” regulation of consumer credit including an *ex ante* system of licensing for all credit providers. It is certainly not light touch and fits Braithwaite’s model of “more capitalism, more regulation”. The existence of licensing means that regulation does not depend on ex post individualised actions.

The UK initiatives indicate that substantial regulation is needed to ensure that credit markets are free and fair. These interventions promise greater fairness, perhaps slightly lower prices and greater choice for lower income consumers. Fairness within this approach does not however prevent the Poor from paying more than middle income consumers for credit. In addition, the ultimate objective of promoting confidence in an expanding market for credit assumes that the promotion of access rather than protection from credit should be the goals in the UK system. There will remain a significant subprime lending market of rent-to-own stores, payday loans, and moneylenders. The UK government assumption is that it is better for individuals to be within this stratified system of credit, with a chance of climbing the ladder of credit, than to be excluded because of controls on the supply side of credit through interest rate ceilings. A general defence of institutions such as home lending in the UK where low income individuals pay high prices for credit is that this form of credit is adjusted to the needs of these higher risk consumers who often need to miss payments because of disruptions in their lives.[110] Mainstream forms of credit such as credit cards could be more dangerous for home credit customers given the high default charges for missing payments.

Affordable access to credit for low income consumers, particularly for short term loans remains an intractable problem. The non-profit sector such as credit unions plays a modest role in providing credit for low income consumers in the UK. Current government policy views the development of the credit union sector and Community Development Finance Institutions as central to the provision of

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107 *Ibid* at para 1.12.
108 See e.g. Financial Inclusion Task Force, Towards a Step Change in 3rd Sector lending coverage and capacity (2008) where the Working Group “conservatively estimates the market for affordable credit as £1.2 billion lent to 3,000,000 customers.”
109 See Competition Commission Reports on Home Lending, Payment Protection Insurance and Store Cards.
110 The Competition Commission inquiry concluded that the home lending sector served about 2.3 million customers annually, lending 2.5 billion in 2004.

affordable access.[111] Crowther noted in 1970 that "mutual aid ..." was not part of the British tradition in credit compared with the growth of credit unions in other countries. Historically, apart from building societies before they were demutualized, there has been a relative absence of non-market institutions providing credit. In the 19th century private pawnbrokers were known as the poor man's bank and hire-purchase, moneylenders, and home collected credit provided working class credit. Scrutiny of the historical debates of attempts to regulate the price of credit indicates that there was always a concern that to do so would limit credit to the working classes. Jeremy Bentham's strictures against usury regulation seemed to have been influential.

Contrasting visions of consumer credit? The Case of France

Recent comparative studies argue that the French legal system is less consumerist[112] than the US and UK, and more willing to protect consumers from easy credit which is perceived to contribute to potential financial exclusion. [113] The World Bank Doing Business project concludes that the French civilian tradition is less hospitable to facilitating credit (a conclusion denied by French scholars!) and La Porta et al argue that the French civilian tradition is associated with an ideology of greater government ownership and centralised regulation than the common law. [114]

There are certainly significant differences between the UK and France in regulation of the consumer credit market. First the existence of interest rate ceilings in France means that there is much less possibility of a legitimate sub-prime credit industry of payday loans, and very high cost lending. Second, credit reporting is operated by a public agency, the Bank of France, and is limited to providing creditors with "negative" information on debtors. Third, there were restrictions on the ability of individuals to use homes as a source of equity finance. This was partly altered in 2006 by the introduction of the "hypotheque rechargeable"[115] ---intended to facilitate home equity credit for consumption ---but there has been little uptake of this form of borrowing.[116] Consumer protection rules differ somewhat from the UK—the most significant being a cooling off period of 7 days after the "offer prealable"—but a close scrutiny of these regulations does not support the argument that, absent the usury ceilings, they are significantly more protective than the UK.[117] Fourth, there is a

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[111] See Treasury Financial Inclusion 2008-11 at 2.11 where support for third sector lenders is " at the heart" of government strategy to provide affordable access.
[112] See Whitman op cit supra
[113] See G Trumbull (2006) Consumer Capitalism (Ithaca: Cornell) at 25. Whitman, 2008...
[114] R La Porta, F Lopez-de-Silanes and A Shleifer, The Economic Consequences of Legal Origins (2007) Civil law ideology is "much more comfortable with the centralized and activist government".
[115] Ordonnance n° 2006-346 du 23 mars 2006 relative aux sûretés modifying Art. 2422. - L'hypothèque peut être ultérieurement affectée à la garantie de créances autres que celles mentionnées par l'acte constitutif pourvu que celui-ci le prévoie expressément.

« Le constituant peut alors l'offrir en garantie, dans la limite de la somme prévue dans l'acte constitutif et mentionnée à l'article 2423, non seulement au créancier originaire, mais aussi à un nouveau créancier encore que le premier n'ait pas été payé.
« La convention de rechargement qu'il passe, soit avec le créancier originaire, soit avec le nouveau créancier, revêt la forme notariée
[116] French housing finance is unique in its use of guarantees rather than mortgages by financial institutions. The process
[117] The 2007 Economic and Social Council report on over-indebtedness claims that consumer protection in France for debtors is more protective than the Anglo-Saxon approach. The report identifies usury regulations, the 7 day cooling off period, the possibility of obtaining a delay in payment, the protection attached to a credit

larger cooperative banking sector in France. Finally, over-indebted consumers have a range of public and private alternatives in England and Wales for which they must generally pay a fee, whereas in France there appears to be a single gateway for the over-indebted consumer. This is the process managed by the Bank of France which runs the network of over-indebtedness commissions in each department and which provide a free service to consumers.

In 2004 outstanding consumer credit per capita was 2,200 euro in France and 4,400 euro in the UK. Younger individuals and those on modest incomes have less access to consumer credit in France than the UK.[118] There are substantially lower numbers of credit cards in France. However there is an initial apparent paradox because about 180,000 individuals in France annually make applications to the over-indebtedness commissions established by the Bank of France whereas in England and Wales a substantially smaller number of individuals apply for bankruptcy or an Individual Voluntary Arrangement.[119] This apparent paradox is explicable by the absence of the many private debt management programmes which exist in England with estimates of 150,000 debt management plans being commenced annually.

Concerns were raised that French consumers are “under-indebted” and that this has had a detrimental effect on the growth of the French economy. In 2006 a French Senate Report raised the question whether consumer credit made too limited a contribution to economic growth[120]. The Bourdin report argued that public policy since the 1980s had been focused on over-indebtedness and protection from debt. This resulted in an over-cautious approach to credit granting with the consequence that some individuals did not get access to credit. The Canivet report on the hypotheque generale saw it as a method of promoting credit to groups which might not traditionally obtain credit. Bourdin argued that the costs of limiting credit included the loss of growth which is linked to economic growth and employment, the costs to the individual of being refused credit and the distributive injustice of those with deposits in banks who finance low cost credit for better off individuals[121]. Bourdin proposed a more liberal regime for accessing home equity, and opening a debate on positive credit reporting and existing usury restrictions.

Subsequently the French government did make it easier for individuals to use their homes as security for ordinary credit purchases and greater use of consumer credit is advocated but without the problems of “Anglo-Saxon” over-indebtedness. However the credit crunch seems to have resulted in a backlash against consumer credit, particularly revolving credit.. The implementation of the 2008 European Consumer Credit Directive has provided the French government with the opportunity of making some modest further reforms of consumer credit law including a mandatory information obligation on consumer credit products that “Un crédit vous engage et doit être remboursé".[122] The introduction of positive credit reporting has once again been raised[123].

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sale, the transparency and information obligations on the cost of credit, and regulation of revolving credit in 2005 providing greater disclosure and the requirement of an “offer prealable” if the creditor wishes to increase the consumer’s credit limit. The Council recommended that borrowers should be provided with a “Coeur du contract” disclosure.

[118] See Les Enjeux Economiques et Sociaux de l’Industrie Bancaire, Comite Consultatif du secteur financier Pastre Report (2006) at 79.

[119] The French data are from the Banque de France

[120] See Rapport d’information sur l’accèss des ménages au crédit en France par M. Joël Bourdin No 261 (2006)

[121] Id. at 51.

[122] Projet de loi portant reforme du credit a la consummation (2 009).

[123] See Senate Report , Rapporteur Philippe Dominati (2 June 2009).

The differences between the UK and France are emblematic of differences within the EU in approaches to consumer credit and tensions between neo-liberalism and a social market approach. On one hand a primary goal of EU policy in recent years has been to foster a competitive and integrated European credit and financial services market. This is part of the Lisbon agenda. Examples include the payments directive,[124] the Green paper on retail financial services[125] and several actions brought by DG Competition concerning credit card services and state subsidies of financial services providers that might inhibit access by competing firms.[126] The recent EU Consumer Credit Directive[127] is primarily concerned with achieving a more competitive credit market and adopts a targeted full harmonisation approach to those issues that are intended to facilitate cross border competition in credit: standardised pre-contractual information and calculation of the APR, a 14 day right of withdrawal, and rules on early repayment. It does not view the current directive as part of "the fight against overindebtedness".[128] However the Commission (through different DGs) has initiated projects to develop a common definition of over-indebtedness and to study financial exclusion [129] and a recent report proposes that financial services should be viewed as services of general interest and that as part of the European model of society all individuals should have affordable access.

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[124] Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market amending Directives 97/7/EC, 2002/65/EC, 2005/60/EC and 2006/48/EC and repealing Directive 97/5/EC Text with EEA relevance.

[125] Green Paper on Retail Financial Services in the Single Market Brussels, 30.4.2007 COM(2007) 226 final.

[126] See in relation to Carte Bancaire Decision of the Commission 17 X 2007 under article 81 of the Treaty COMP/D1/38606 GROUPEMENT DES CARTES BANCAIRES Bruxelles, le 17 X 2007 C(2007) 5060 final; Press release Antitrust: Commission initiates formal proceedings against Visa Europe Limited (26/03/08): Press Release Antitrust: Commission fines Visa €10.2 million for refusing to admit Morgan Stanley as a member 03/10/2007.

[127] Directive 2008/48/EC on Credit Agreements for Consumers (2008) O.J. L133/66.

[128] Evidence of Dirk Staudenmeyer on behalf of the European Commission to the House of Lords European Union Committee reported in 36th Report of Session 2005-06 Consumer Credit in the European Union: Harmonisation and Consumer Protection Vol. 1 Report HL Paper 201-I at 59.

[129] See EU Commission, Towards a Common Operational European Definition of Overindebtedness DG Employment, Social Affairs and Equal Opportunities (2008); Financial services provision and the prevention of financial exclusion Overview Paper March 2007.