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Position on compliance of

a Bill amending certain acts to counter usury

(Sejm print No. 3600) with EU law

About the Submitter – 4finance Group S.A. ("4finance")

Established in 2008, 4finance is one of Europe's largest digital consumer lending groups with operations in 14 countries.

Leveraging a high degree of automation and data-driven insights across all aspects of the business, 4finance has grown rapidly, issuing over €7 billion since inception in single payment loans, instalment loans and lines of credit.

4finance operates a portfolio of market leading brands, through which, as a responsible lender, the firm offers simple, convenient and transparent products to millions of customers who are typically underserved by conventional providers.

4finance has group offices in Riga (Latvia), London, Luxembourg and Miami, and currently operates in Poland and 11 other countries in Europe as well as in Argentina and Mexico. The group also offers deposits, in addition to consumer and SME loans through its TBI Bank subsidiary, an EU licensed institution with operations primarily in Bulgaria and Romania.

I. INTRODUCTION

On the 2nd of July 2019, the Sejm of the Republic of Poland received a **government bill amending certain acts to counter usury** (hereinafter referred to as the '**Bill**'). On the 19th of July 2019, the first reading of the Bill took place at the session of the Sejm.

The Bill provides for the introduction of significant systemic changes in the area of granting consumer credit, including a determination of the maximum amount of non-interest bearing costs, extension of the procedure for examining the creditworthiness of borrowers prior to the conclusion of a consumer credit agreement, and introduction of the criminalization of certain acts linked to the violation of consumer credit rules.

The first version of the project of the Bill was published at the end of 2016. Public consultations related to this project lasted for over two years. In the course of the consultation process, a number of entities (bodies, associations, companies) participated and often with very critical feedback.

The last version of the Bill stipulates that the provisions proposed in it, will come into force six months from the date of publication.

On 28th of June 2019, the Bill was notified to the European Commission (Notification Number: 2019/313/PL). On the basis of the information made available on the European Commission's website, it appears that the period of suspension of all legislative work (*standstill*) on the Act in question, (pursuant to Article 6 of Directive 2015/1535/EU of the European Parliament and the Council of 9

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September 2015 laying down a procedure for the provision of information in the field of technical regulations and of rules of Information Society services,) should expire on the 30th of September 2019.

It should be noted, however, that the Bill introduces measures that may be contrary to the provisions of European Union law, both primary law, i.e. the principles and values of the European Union, and secondary law, i.e. the provisions in force at the EU level in the area of consumer credit and supervision of financial institutions. In addition, it should be pointed out that the situation on the financial services market in Poland after implementation of the proposed measures may lead to a state contrary to the provisions of EU law on fair competition.

For the sake of clarity, the main changes indicated in the Bill will be discussed further below, as well as an attempt to assess them in terms of compliance with the European Union law.

II. OBLIGATION TO OBTAIN FROM THE BORROWER AND VERIFY A DECLARATION OF HIS INCOME AND EXPENDITURES

The Bill provides for the introduction of an obligation to collect from the borrower **a statement on his income and expenditures**, as well as verification - in the manner specified in the Bill[1] – of the information contained in this statement (cf. proposed Article 10a of the Consumer Credit Act).

At the same time, it is proposed to **exempt banks and cooperative savings and credit unions** (hereinafter referred to as the **'SKOKs'**) **from this obligation.**

In this context, it should be pointed out that this measure appears contrary to the Article 8 par. 1 of the Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC (hereinafter referred to as the '**Consumer Credit Directive'**) – to the extent that it introduces a requirement for the potential borrower to submit – subject to verification – a statement of his income and expenditures.

The above-mentioned provision obliges Member States to introduce provisions to ensure that the creditor, before the conclusion of the credit agreement, assesses the consumer's creditworthiness **on the basis of sufficient information obtained from the consumer, where applicable, and, if necessary, on the basis of information obtained from the relevant database.**

The above-mentioned means that the introduction of the obligation for the consumer to submit additional documents or statements should be exceptional (as indicated by the term 'where applicable'). Meanwhile, the Bill imposes an obligation only on lending institutions, as banks and SKOKs are exempt from it, which applies in every situation of concluding a consumer credit agreement.

In addition, it should be noted that the above-mentioned statement, together with documents regarding its verification**, will be an attachment to the consumer credit agreement.**

[1] A creditor (loan institution) will be required to verify the consumer's claims by referring to documents presented by the consumer, prepared by the employer, public administration authorities or data collected by business information offices or banks database institutions (cf. proposed Article 10a (3) of the Consumer Credit Act).

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Although the Consumer Credit Directive does not explicitly prohibit Member States from dictating the catalog of documents/information constituting a consumer credit agreement, it does not seem that such a statement – as to which compliance with the provisions of the above-mentioned, there are reservations in the directive –should be an attachment to the consumer credit agreement. Article 5 par. 2 of the directive clearly indicates what information should be included in such a contract, and there is no document in this catalog related to the verification of the borrower's creditworthiness. It should be emphasized that the documents presented by the consumer may come from various sources, and what is more, they may contain protected legal information (such as data covered by banking secrecy or consumer personal data), and their inclusion in the consumer credit agreement may not guarantee an adequate level of protection.

The points made above leads to the conclusion that **the draft provisions violate Article 22 par. 1 of the Consumer Credit Directive** – to the extent that this directive is subject to maximum and full harmonization. The full directive significantly limit the Member States' implementation freedom in such a way that the national legislator cannot adopt solutions other than those directly contained in the directive, unless the directive states otherwise. In other words, the directive provides for a certain standard (pattern) that cannot be modified in the national implementation act. The degree of interference of the full directive into national law is so great that there is a practical restriction of the freedom of national legislators in choosing the form and means to implement it into national law. Thus, directives based on the principle of full harmonization are approaching in their character Community regulations leading to the unification of law.

Further, it should be noted that the introduction of additional obligations (as well as the consequences of their breach, which will be discussed further below) may significantly **impede the operation of consumer credits and loans by entities from other Member States.** The Bill indicates that the customer statement may be done, by verified against documents drawn up by the customer's employer or public administration bodies, which may be difficult to verify outside of Poland (e.g. due to the loan institution's inability to access such data). Therefore, it should be understood that the proposed measures do not comply with Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the internal market. Especially where the directive prescribes the creation of market conditions that will not impede the provision of information society services – and includes services that grant consumer credit and loans to consumers via the Internet – on a cross-border basis. The unnecessary and disproportionate nature of the additional administrative burden for cross-border services is illustrated by the fact that there is a considerable category of lenders exempted from obligation to verify income i.e. banks.

As a consequence, the draft regulations are also **contrary to the principles of the functioning of the internal market, including the EU freedom to provide services** – to the extent that the draft provisions may limit the functioning of loan institutions from other European Union Member States on the Polish market.

In addition, **it is unjustified to distinguish the legal situation of banks and SKOKs** by excluding the latter from the obligation to obtain from borrowers statements about their income and expenditures. The adoption of such a solution is contrary to **the EU principle of equality**, which was expressed in Article 2 of the Treaty on European Union. Undoubtedly, excluding these entities from this obligation worsens the legal situation of loan institutions, which – as a result of the Bill – will be required to face higher

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administrative costs and take many additional, often paid, actions to obtain and verify the statement of potential borrowers. Moreover, the preparatory works of the Bill do not contain a description of **any objective circumstances** allowing a restriction on the application of the EU principle of equality.

III. CONSEQUENCES OF GRANTING CONSUMER CREDIT WITH VIOLATION OF THE PROCEDURE OF ACCEPTING AND VERIFYING THE BORROWER'S STATEMENT

The Bill introduces disproportionate treatment of loans found to be non-compliant with the new requirements selectively to non-bank loan institutions. It establishes that, in the case of a breach of the procedure for accepting and verifying the borrower's statement, and also when the borrower, according to the information contained in the statement, had arrears in the repayment of another liability of more than six months and the consumer credit was not used for repayment this charge, then:

- the sale of receivables from this contract by transfer or other means is invalid;
- pursuing a claim is only admissible after the date of full repayment of the earlier liability, its expiration or after the court decides legally that this obligation does not exist.

Therefore – as a result of the proposed provisions – **the loan institution's right to pursue its claims in court is significantly endangered.** It is worth stating that there is no credit register available currently that contains consolidated information about all consumer debts, no legislative proposal is announced to establish such a register and there is no practical opportunity for a loan institution to verify information provided by customer in respect of its debts. The Bill does not introduce any threshold neither in respect of amount of debt nor term of delay, therefore, probability of unverifiable information is very high. Finally, the statutory time limit of the claim is not suspended while the customer pays off its earlier debts.

Meanwhile, according to Article 23 of the Consumer Credit Directive, provisions on sanctions applicable in the case of a breach of the national provisions adopted pursuant to that Directive, and therefore also provisions on the assessment of consumer creditworthiness, should provide for **effective, proportionate and dissuasive** sanctions. In addition, which results from the case law of Polish courts, these sanctions should generate consequences in the sphere of public law relations, not civil private law relations[2].

It should be noted that, firstly, **the proposed sanction is disproportionate**, as it makes it impossible for a loan institution to pursue claims efficiently in court, which definitely cannot be considered as a necessary means to achieve the intended purpose (i.e. introducing liability for violation of the proposed provisions)[3]. Secondly, **it generates private-law consequences** in terms of the obligation that arises – as a result of a consumer credit agreement – between the loan institution and the borrower.

In view of the above-mentioned arguments, it should be stated that the draft provisions are **contrary to Article 22 par. 1 of the Consumer Credit Directive.**

[2] See the judgment of the Court of Appeal in Warsaw of 7 May 2014, VI ACa 945/13.
[3] For the definition of 'proportionality' under EU legislation, see the judgment of the CJEU in case C-309/18 (paragraph 24).

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In the context of discussing – also important from the point of view of loan institutions – the consequences of non-compliance with the procedure of obtaining and verifying the borrower's statement, again it should be pointed to **unjustified exemption from this regulation of banks and SKOKs.** As indicated above, such a proposal violates the EU principle of equality, and in addition, it also creates **limited ability for loan institutions to compete with banks and SKOKs**, because the latter entities, even in the case of non-verification or incorrect verification of the consumer's creditworthiness – based on the procedures indicated in these institutions –will still be entitled to pursue these claims.

Referring to this proposal in general, it should also be noted that its introduction will in no way contribute to **increase consumer protection of borrowers**. Moreover, it should be noted that the proposed regulations - provided only for loan institutions – impose additional obligations for consumers (borrowers), involving the necessity of presenting employer certificates or tax documents may discourage consumers from using the services of loan companies. Nevertheless, it cannot be stated that through introducing the additional obligations for borrowers to make declarations, the level of their protection will increase. Already today banks, SKOKs, as well as lending institutions are obliged to carry out an analysis of creditworthiness of consumer. It is in the interest of the lenders to verify the consumer's possibility to repay their obligations. In addition, it doesn't seem that the proposed solution reduces the risk of using prohibited practices by the entities which are allowed to issue consumer credits on the basis of consumer credit act (banks, SKOKs, loan institutions).

Considering the above argumentation, it should be stated that the measures proposed in the draft **don't comply with the general assumptions and objectives of the Consumer Credit Directive**.

IV. SUPERVISION OF THE POLISH FINANCIAL SUPERVISION AUTHORITY OVER THE ACTIVITIES OF LOAN INSTITUTIONS

An important element of the proposed regulation is the introduction of a solution according to which **the activities of loan institutions will be supervised by the Polish Financial Supervision Authority (KNF).**

Polish Financial Supervision Authority, pursuant to Article 3a of the Act of 21 July 2006 on financial market supervision is the competent authority within the meaning of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (hereinafter referred to as the '**Regulation 575/2013**').

It should be indicated here that, in accordance with the scope of application contained in the abovementioned regulation, it applies to credit institutions, investment firms, insurance and reinsurance undertakings. Credit institutions are understood as **enterprises whose business is to receive deposits or other repayable funds to customers and to grant loans for their own account.**

The definition mentioned above drives the conclusion that **loan institutions in no way meet the definition because they do not accept deposits from their customers.** Their activity consists mainly in the granting of consumer loans and credits, also via the Internet.

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It should be pointed out that the Bill proposes not only that the Polish Financial Supervision Authority becomes the supervisory body of loan institutions, but also assumes it being equipped with the same supervisory powers as that body has in relation to banks and SKOKs (e.g. the possibility of imposing fines or removing an institution from the register of loan institutions, which actually means that it is no longer possible to conduct lending business – an entry in this register is a condition for a loan institution to issue loans to consumers in Poland as a business activity). However, it should be emphasized that **this approach is not justified.** Firstly, as the loan institutions don't collect deposits from consumers, the operational risk which they undertake when issuing loans is much smaller for financial market compering to banks and SKOK's), and secondly – no prudential mechanisms are foreseen in relation to loan institutions, even those related to their restructuring.

In addition, it should be pointed out that after the implementation of the proposed changes to the Polish financial system, there will be two Public Authorities with almost the same competencies that will control and supervise the activities of loan institutions - the Polish Financial Supervision Authority and the Office of Competition and Consumer Protection. Considering the open scope of competences of these two authorities especially in regard to the protection of consumer rights and interests listed in the Bill and in the regulations provided for the Office of Competition and Consumer Protection, it cannot be ruled out that their supervisory activities will overlap, which will negatively affect the sense of legal certainty among entrepreneurs (loan institutions). It seems that, assessing the compliance of lending institutions with the provisions implementing the Consumer Credit Directive exercised by the Office of Competition and Consumer Protection - the KNF should only have an auxiliary role, and should not have additional, typically regulatory competences, as the introduced supervision activities concerns only the sphere of consumer protection (provided in Poland by Office of Competition and Consumer Protection).

It should be also stressed that the Polish Financial Supervision Authority critically assessed the introduction of this proposal, arguing that the activity of the loan institutions is already supervised by the Office of Competition and Consumer Protection and there is no need to extend the competences of KNF in this scope[4].

Considering the circumstances described above, especially the fact that loan institutions don't collect consumer deposits and are supervised by the Office of Competition and Consumer Protection it should be noted that the **proposed solutions are contrary to the assumptions of Regulation 575/2013.**

V. THE EFFECTS OF THE INTRODUCTION OF PROPOSED REGULATIONS ON THE FINANCIAL MARKET

It should be pointed out here that the proposed solutions will have significant effects on the financial market.

[4] C.f. The statement of the KNF dated on the 6th of March 2019, https://legislacja.rcl.gov.pl/docs//2/12292908/12397488/12397491/dokument383861.pdf.

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First of all, it should be noted that the introduction of changes in the area of maximum non-interest costs will be associated with a **significant reduction in the viability of loan institutions in Poland.** It is estimated that the proposed solutions will lead to a decrease in income of loan institutions by up to 58% y/y[5]. It is worth pointing out that both banks and SKOKs will not feel the (financial) impact of the draft provisions so significantly, because their activity is funded by variety of other financial products to consumers and organizations, which is not the case for specialized loan institutions.

As a side note, it should be pointed out that in the course of public consultations, both entrepreneurs as well as organizations and associations of Polish entrepreneurs repeatedly presented reliable calculations indicating the high probability of losing economic viability for lending institutions to continue issuing consumer loans in Poland. Unfortunately, at no stage of the public consultations procedure, did the authors of the project (Polish Ministry of Justice) refer to the financial analyses presented to support the calculation of economic viability of lending services nor did they present their own data that would examine other consequences of the changes.

What is important, the element characterizing the Polish market of loan institutions is the way of obtaining financing for commercial activity - issuance of bonds by these entities. It is estimated by the Polish Association of Lending Institutions that the value of issued bonds is over PLN 500 million. As a result of the very low interest rate ceiling coupled with other restrictions it is highly probable that specialized consumer lending will not be economically viable anymore in Poland. That almost certainly will prohibit some loan institutions to serve their debt on bond market. As a result it may lead to the deterioration of the financial situation of investors, including the financial stability of institutional investors.

Bearing in mind the above, it must be stated that the deterioration of the investors' situation certainly will affect bonds listed on the Warsaw Stock Exchange. Such significant interference of the Polish legislator in the business activities of loan institutions, which are an important element of the bond market, may consequently impact the stability of the financial system as a whole.

The introduction of measures that significantly affect the profitability of loan institutions may result in a significant decrease in bonds issued by them, and in consequence a significant deterioration of investors' financial standing. It will be highly probable, if the proposed provisions are implemented, that the loan institutions will not buy bond coupons. Investors for whom the loan market so far has been a stable market, and most importantly - constantly developing and implementing new and innovative solutions (especially in the field of fintech), will be destroyed as a result of the implementation of the act.

It should be emphasized here that the highly probable **decrease in the supply of consumer credits and loans offered by loan institutions will not be combined with a decrease in demand for such services on the part of consumers.** In addition to loan institutions, such services are also provided by banks and SKOKs, which may justify the claim that **as a result of the entry into force of the proposed changes – from a business point of view – these entities will benefit the most.** As a side note, it is worth pointing out that the largest Polish banks comprising almost 43% of total bank assets[6], also operating in

[5]Analysis of loan institutions offers done by Polish Association of Lending Institutions.

[6] Cf. https://prnews.pl/aktywa-bankow-najwieksze-banki-polska-443675.

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the consumer credits and loans sector, belong to the State Treasury, which illustrates the political and competition context of the changes introduced.

The above-mentioned situation should be considered at risk of unlawful state aid within the meaning of the provisions of the Treaty on the Functioning of the European Union. Although the Bill does not explicitly indicate any support for banks, including banks belonging to the State Treasury, or SKOKs (potential beneficiaries), nevertheless the market situation, which will most likely occur as a result of the introduction of the proposed changes, will justify the claim that these entities may benefit the most as a result of changes in law.

In addition, it should be noted that the effect of introducing these provisions will also **significantly strengthen the market position of the largest banks and SKOKs.** It is impossible to state that such action is in line with both the principle of competitiveness expressed in the TEU and the EU competition rules set out in the Treaty on the Functioning of the European Union. Such significant structural changes in the consumer credit and loans market may in the future lead to both the use of restrictive practices by banks (and to a lesser extent by SKOKs) and abuse of a dominant position. Importantly, the circumstances of these risks are not addressed by the authors of the project.

VI. SUMMARY

The introduction of the provisions proposed in the Bill, relating both to the maximum non-interest cost limit for consumer credit, as well as to the additional obligations imposed on credit institutions, will highly **adversely affect the financial market in Poland with no benefit to consumers.** Moreover, bearing in mind that some operators (loan institutions) operating in Poland are among the pan-European capital groups, the effects of these changes can be felt in other Member States.

It should be noted here that the solutions proposed in the Bill **are contrary to the provisions of European Union law.**

Critically the **proposed provisions are incompatible with the Consumer Credit Directive** – to the extent that they go beyond the allowable freedom of the Member States in shaping national provisions on granting consumer credits to consumers. From the point of view of consumer protection, it does not seem necessary to impose additional obligations not explicitly imposed on consumers and loan institutions. Further, it should be noted the disproportionate and – most important – interfering in the private law sphere of relations between loan institutions and borrowers related to a significant limitation of the right to claim in the case of a breach by the creditor of the procedure of assessing the consumer's creditworthiness, in particular in connection with obtaining and verifying his statement on income and expenditures.

It should be noted here that **the regulations described above are reserved exclusively for loan institutions, with the deliberate exclusion from their scope of banks and SKOKs** (entities also granting loans and consumer loans). This solution leads to a situation in which the proposed provisions **violate the EU principle of equality**, because there are no objective circumstances that would justify the departure from these obligations in relation to banks and SKOKs.

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The Bill also provides for the introduction of measures that **do not comply with the provisions of Regulation 575/2013**. There is no justification for extending to loan institutions the same capital requirement supervision as banks and SKOKs. Banks and SKOKs are in a situation where there is a greater risk involving these entities as they, opposite to loan institutions, are allowed by law to accumulate financial resources of individuals as well as business entities, store customer deposits and to grant credit or cash loans and to expose such resources to risk.

In addition, the consequences of introducing the draft provisions for the financial market – completely unmentioned by the project's promoters – should be pointed out. As a result of lowering the limit of maximum non-interest costs, many loan institutions in Poland will not be economically viable. However, what is important, along with the decrease in the supply of services offered by these institutions, it is not envisaged to introduce mechanisms resulting in a decrease in the supply of such services. What is more, the result of the measures proposed will improve the business situation of the largest banks, including those owned by the State Treasury, and SKOKs, which in the future may lead to significant competitive distortions.

The limitation of obligations related to the verification of borrowers' statements in relation to banks and SKOKs in the long term (when the currently draft provisions will come into force) should also be assessed in terms of the possibility of recognizing such action as unlawful public aid within the meaning of European Union law.

Considering the above-mentioned circumstances, the Bill contains measures that contravene European Union law.

On behalf of the Submitter,

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