

Responsible and Informed Lending and Consumer Protection in the Case of Consumer Loans from Non- Bank Credit Providers

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bank lenders prevent irresponsible lending?*

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Summary of audit results

One in four consumer loan repayments is not made on time.

Financial policy under the jurisdiction of **the Ministry of Finance** includes, among others:

- Financial supervision and financial stability
- Promoting financial literacy
- Sustainable development of financial services.

According to the principle of responsible lending, the lender must ensure the borrower's ability to repay the loan by gathering information about the borrower's financial behaviour and assessing their ability to pay.

The obligation to comply with the principle of responsible lending applies equally to lending banks, lessors, and non-bank credit institutions.

Since 2016, credit providers must have an activity licence issued by the Financial Supervision Authority.

The Ministry of Finance should intensify efforts to create effective and discouraging obstacles, which could prevent over-borrowing from non-bank lenders due to impulsive and reckless decisions and too easy access to credit. Although the ministry acknowledges that people often face difficulties, when repaying non-bank consumer loans, the policymaking and supervision in restraining both borrowers and non-bank lenders have been relatively inadequate.

There are gaps in the supervision and consumer protection of non-bank lenders.

- The Financial Supervision Authority has various tools for supervising non-bank lenders, but they mostly use precept. Only a few misdemeanour proceedings which are more forceful have been initiated.
- The Consumer Protection and Technical Regulatory Authority (CPTA) has not checked for years whether non-bank lenders provide the required information to loan applicants before signing the contract.
- Companies that buy debts from creditors are not subject to supervision, resulting in not being equally protected of the borrower's interests and rights as compared to when taking out the loan.

The Ministry of Finance has encountered difficulties in leading the implementation of proposals that positively impact lending responsibility. The execution of plans proposed in the strategy documents, such as the credit information register, has been delayed since 2016. The extension of the statute of limitations for misdemeanours and the increase of penalty rates took five years.

The interests and rights of borrowers and debtors are less protected than those of creditors and debt collectors, as decisions made by the Consumer Disputes Committee are non-binding. In expedited order-for-payment procedures, courts are not required to verify the legal basis for

debt collection if no objections are raised by the debtor. Debt buying occurs without state oversight.

For your information

The Ministry of Finance plans¹ to bring debt collection companies under the supervision of the Financial Supervision Authority, while transposing the directive on credit servicers and credit purchasers.

Improving the financial literacy of adults, especially those in financially vulnerable situations, requires targeted efforts. The Ministry of Finance has not yet analysed the extent of possible damage from over-borrowing, there is a lack of important data therefore the design of necessary measures is hindered. A behavioural science approach has not been utilised to guide consumers. Different target groups should be considered, determining the level of detail and methods to ensure that information impacts their behaviour. Debt counselling services are not widely accessible.

For your information

An amendment to the law, effective from November 2023², provides the Financial Supervision Authority with the opportunity to impose significantly higher fines and alleviate procedural bottlenecks, including extending the statute of limitations for misdemeanours by half.

Although the Financial Supervision Authority supervises non-bank lenders, its impact is limited. The authority monitors the credit market's development and conducts risk-based inspections. After the detection of violations, primarily a precept is issued. The likelihood of initiating misdemeanour proceedings against lenders for their violations has been minimal. Furthermore, the fines imposed are relatively small.

For your information

In 2023, the CPTRA plans to test compliance with the principle of responsible lending through control transactions.

The CPTRA needs to assess the risks related to insufficient pre-contractual consumer information more extensively and conduct appropriate checks. As credit consumers themselves make few complaints about credit providers to the CPTRA, the latter lacked a comprehensive overview of consumer problems until the autumn of 2022, when a series of articles covering debtors' issues appeared in the media³.

For your information

The Ministry of Economic Affairs and Communications plans to reorganise the work of the Consumer Disputes Committee, including making the committee's decisions binding.

The supervision of the CPTRA and the Financial Supervision Authority over consumer credit advertising primarily relies on complaints. The capability to monitor online advertising is limited, and there is no digital tool for this purpose. Therefore, it is uncertain whether the advertisements displayed to consumers on social media and elsewhere on the web meet the requirements. As financial services advertising is supervised by both the Financial Supervision Authority and the CPTRA, information exchange and extensive cooperation should be encouraged.

There were errors in the data on the volume of non-performing loans collected by the Financial Supervision Authority, and issues with data accessibility in the CPTRA's information system were noticed. The information collected by the Financial Supervision Authority until 31st March 2022, regarding the volume of non-performing loans, was inaccurate. Due to the merger of the CPTRA's document management systems, data on previous supervision procedures are unavailable.

¹ Directive (EU) 2021/2167 of the European Parliament and of the Council of 24th November 2021 on credit servicers and credit purchasers and amending Directives 2008/48/EC and 2014/17/EU. The deadline for transposing the directive is 29th December 2023.

² „Act on Amending the Auditors Activities Act, the Financial Crisis Prevention and Resolution Act, and Other Acts“ adopted by the Riigikogu on 22nd February 2023.

³ The article series „The Power of Debt,“ analysing the systemic errors of the Estonian loan market, was published in Eesti Päevaleht, Eesti Ekspress, Maaleht, and Delfi in September 2022.

Recommendations of the National Audit Office

The Ministry of Finance, as responsible of financial policy and the coordinator of financial literacy, should:

- Ensure that the regulatory environment and supervisors' tools prevent irresponsible lending and ensure the protection of consumers' rights and interests. In collaboration with other ministries, actions should be taken to prevent over-lending and improve the protection of consumers in vulnerable conditions.
- Include measures for adults in the strategy action plan for financial literacy to raise awareness of borrowing and debt risks, guide financial behaviour, and support the Ministry of Social Affairs and local governments in providing debt counselling services.

The supervisory authorities, the Financial Supervision Authority and the CPTRA, should implement all procedural options available to ensure compliance with the principle of responsible lending and consumers protection.

The Ministry of Finance and the Ministry of Justice should analyse whether the changes related to misdemeanour procedures enable effective, proportionate, and dissuasive punishments to be imposed during supervision after these changes come into force⁴. If necessary, further work should be carried out to find a solution.

The Ministry of Finance and the Ministry of Economic Affairs and Communications should create an opportunity to resolve disputes between consumers of credit products and creditors or debt collection companies through out-of-court proceedings, ensuring that decisions are binding. This would reduce the burden on the judicial system.

Response from the Minister of Finance: The minister agreed that although significant progress has been made and work is in process, there is still room for improving the regulatory environment, promoting financial literacy, and developing advisory services.

Response from the Chairman of the Management Board of the Financial Supervision Authority: The chairman noted that the authority applies procedural options effectively and proportionately based on the circumstances of each supervision case. However, a system of administrative fines and procedures would be better suited for the financial supervision of professional market participants.

Response from the Deputy Secretary General for Business and Consumer Environment at the Ministry of Economic Affairs and Communications: The Ministry is in the process of changing the work organization of the Consumer Disputes Commission, including making the decisions legally binding.

Response from the Minister of Justice: While the Ministry of Finance's involvement in the analysis is crucial, it is the Ministry of Justice that bears the responsibility for changing the regulation of the offense

⁴ Article 23 of the Consumer Credit Directive.

procedure. To resolve consumer disputes, the Ministry of Justice would prefer a conciliation procedure according to the Conciliation Act.

Response from the Director General of the CPTRA: The authority will consider the National Audit Office's recommendation when developing the work plan. The CPTRA will continue to utilise all available procedural options to ensure compliance with the principle of responsible lending and consumers protection.