



## **Coercive Selling on (tied) deposit accounts: Mortgage loans and fees related with maintenance of accounts**

### **FSUG opinion and recommendations**

#### **About FSUG**

The Financial Services Users Group (FSUG) is composed of 20 experts who represent the interests of consumers, retail investors, micro-enterprises and include individual experts in financial services from the consumer perspective. FSUG's tasks include: advising the European Commission in the preparation and implementation of legislation or policy initiatives affecting the users of financial services; proactively identifying key issues affecting users of financial services; advising and liaising with financial services user representatives and representative bodies at the EU and national level.

#### **Abstract**

The Directive 2005/29 EC of the European Parliament and of the Council of 11 May 2005, concerning unfair business-to-consumer commercial practices in the internal market (“Unfair Commercial Practices Directive”), particularly Article 9 (d), and the Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010 (MCD), namely but not limited to the Article 12(1), has not been enough to end those kinds of unfair commercial practices.

The MCD distinguishes tying and bundling of products, introducing a ban on tying practices. However, it also presents exemptions to this ban which have resulted in consumer detriment. Banks impose undue pressure on, or coerce, clients to buy products and/or services from the bank or any of its affiliates, as a condition for obtaining another product or service from the bank, where at least one of the products or services offered in the package is not available

separately (“tied package”), even when the products and/or services are functionally independent. Often, these “tied packages” contracts do not specify all the future prices, so that a long-term relationship is decided by short-term contracts. These practices include exploiting tied packages and/or use aggressive commercial practices. This results in onerous or disproportionate non-contractual barriers to the rights to terminate a contract or to switch to another product or another trader (coercion), maintaining customers “hostage” to a product or service that they do not want or need. In some cases, there is a possibility for creditors of terminating the contractual relationship regarding another product or service included in the package, creating *ex post* monopoly, for which firms compete *ex ante*.

## **Introduction**

Banks impose undue pressure on, or coerce, clients to buy products and/or services from the bank or any of its affiliates, as a condition for obtaining another product or service from the bank, where at least one of the products or services offered in the package is not available separately (“tied package”), even when the products and/or services are functionally independent. Often, these “tied packages” contracts do not specify all the future prices, so that a long-term relationship is decided by short-term contracts. These practices, where the banks exploit tied packages and/or use aggressive commercial practices, including onerous or disproportionate non-contractual barriers to the rights to terminate a contract or to switch to another product or another trader (coercion), in order to maintain “hostage” customers within a product or service that they do not want or need, threatening them with the termination of the contractual relationship regarding another product or service, included in the package, creates *ex post* monopoly, for which firms compete *ex ante*.

For example, banks often impose customers buying mortgages to contract a transaction bank account<sup>1</sup>. The customer can only give up on his transaction account in case of repayment of the mortgage. The issue becomes particularly relevant as there is no measure preventing banks to unilaterally decide changing (typically raising) running costs/fees of the transaction account. There are cases where the bank increased those costs more than 500%, in just a few years! However, banks do not allow customers to maintain a home loan without a basic transactional bank account, although these are functionally independent services.

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<sup>1</sup> Known as “current account”, “checking account” or “demand deposit account”.

This anti-competitive practice and conduct which restrict competition are likely to cause an increase in the price of each individual service/product offered in the package and the switching costs for the consumer as well.

Providers leverage the fact of customers being hostages of a tied package and/or using aggressive commercial practices like coercion, to unilaterally impose the price of the product or the service whose purchase depends on the acquisition of the main product or service.

This antitrust and restrictive practices as a huge impact in the real life of the financial consumers, in particular, but not exclusively, for the financial consumers who have revolving credits / open-end credits (*i.e.* credit card debt, lines of credit, *etc.*) or instalment loans / close-end credit (*i.e.* mortgage loan, car loan, appliance loan, *etc.*), which are a large part of the European financial consumers, since in these cases they face huge difficulties in switching payment/current accounts. Consumers are held hostages to these tied packages that combining slow-moving services/products with fast-moving services/products, because the providers (banks) create a contractual barrier that prevents the consumer to switch to another service/product or another trader or terminate a contract.

### **Cross selling**

Considering the description of “cross selling” proposed in ESMA’s Guidelines: “*offering of an investment service together with another service or product as part of a package or as a condition for the same agreement or package*” (ESMA, 2016)<sup>2</sup>.

Cross selling is a kind of bundling, so the description of bundle goes well for cross selling too.

### **Bundled Package**

Considering the description of “bundled package” proposed in ESMA’s Guidelines: “[a] *package of products and/or services where each of the products or services offered is available*

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<sup>2</sup> According to definition used in the ESMA’s Guidelines on cross-selling practices (ESMA, 2016. *Guidelines on cross-selling practices* [online]. [accessed 14-11-2018]. Available from World Wide Web: [https://www.esma.europa.eu/sites/default/files/library/2016-574\\_en\\_guidelines\\_on\\_cross-selling\\_practices.pdf](https://www.esma.europa.eu/sites/default/files/library/2016-574_en_guidelines_on_cross-selling_practices.pdf))

*separately and where the client retains the choice to purchase each component of the package separately from the firm” (ESMA, 2016)<sup>3</sup>.*

And in Article 4(27) of the Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014:

*“[b]undling practices’ means the offering or the selling of a credit agreement in a package with other distinct financial products or services where the credit agreement is also made available to the consumer separately but not necessarily on the same terms or conditions as when offered bundled with the ancillary services.”*

Bundling is a widely used practice, especially in telecoms and computer businesses. In general, we agree that a bundled package offers potential benefits for consumers, such as lower prices and lower risks (*i.e.* insurance linked to a loan) while, at the same time, it reduces risks for the provider, enabling them to offer a better deal for the customer, among other potential benefits.

In the case of bundled packages, we think that it is enough to empower the consumers with clear and simple information on price of the bundled package and on each of its components products or services, namely with a clear breakdown of all relevant known costs. This includes, as far as possible, all the future prices (for all services/products) or an estimation for future prices in case there is a possible change in them (so long as indexed to a relevant price index such as inflation). such as monitoring and administration fees; transactions costs and pre-payment penalties charges. This would allow the consumer to decide enter or not in a long-term relationship based on all the costs and conditions along the “life-cycle” of the contracts and not only considering the short-term conditions, allowing the consumer to make an informed decision.

In those cases where credit institutions change fees related to payment accounts associated to mortgages, there is a resulting change in the Annual Percentage Rate of charge (APR) as defined in the MCD (and the CCD). In fact, at the moment of choosing their mortgage contract consumers use the APR as an indicator for the cost. In doing so, consumers will tend to select the offer with the lowest APR for the scenario proposed. However, if there is allowance for an

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<sup>3</sup> *Ibid*, page 5.

unrestricted unilateral change of relevant costs associated to the mortgage, the corresponding APR will necessarily change, and in turn deteriorate its value as a significant indicator for choice. An offer with the best APR can become a bad choice very quickly, for example, by changing the maintenance costs of the underlying and forcedly required payment account.

### **Tied Package**

ESMA's Guidelines proposes the following description of "tied package": "*[a] package of products and/or services where at least one of the products or services offered in the package is not available separately to the customer from the firm*" (ESMA, 2016)<sup>4</sup>.

Article 4(26) of the Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 provides a similar definition: "*[t]ying practice means the offering or the selling of a credit agreement in a package with other distinct financial products or services where the credit agreement is not made available to the consumer separately.*"

But, unlike bundled packages, the tied package is a subtle form of bundling slow-moving services/products with fast-moving services/products and creating a contractual barrier that prevents the consumer to switch to another service/product or another trader or terminate a contract, because the consumer cannot obtain a clear and simple information on the price each product or service in the package, since at least one of the products is not available separately. The case of the MCD is crucial. By allowing exemptions to the ban on tying it has resulted in harmful practices that enforce consumers to take a payment account with the provider of the mortgage. In some MS, the transposition text has adapted the wording under Article 12.2 of that Directive, thus introducing the exemption as referring to a regular payment account, as opposed to the text that mentioned that such an exemption would be accepted with regards to "... open or maintain a payment or a savings account, where the only purpose of such an account is to accumulate capital to repay the credit, to service the credit, to pool resources to obtain the credit, or to provide additional security for the creditor in the event of default...".

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<sup>4</sup> *Ibid*, page 5

## **Coercive Selling**

Considering the description of “coercive selling” proposed in Directive 2005/29 EC:

*“any onerous or disproportionate non-contractual barriers imposed by the trader where a consumer wishes to exercise rights under the contract, including rights to terminate a contract or to switch to another product or another trader” (Directive 2005/29 EC)<sup>5</sup>.*

## **Recommendations**

Our recommendations are:

In general, Member States should introduce measures to prohibit tying practices, when the product or service and their components are functionally independent. The provider must be available to sell them separately, specify all prices, and provide an estimation for future prices in case they evolve over time (so long as indexed to a relevant price index such as inflation).

For example, banks sell actively home loans and a life insurance policy linked to home loans. Where those life insurance policies are created specifically to cover risks related to a particular home loan product, thus, cannot be available to be sold separately, we are dealing with a tied package. In those circumstances, banks must be available to sell a home loan without obligating the customer to buy them life insurance.

That is, tied packaging can only be allowed when one or more products that constitute it enable the consumer to reduce the risk of breach of contract of the relevant product or service established with the provider and, as a result of this decrease of the risk, there is an unquestionable reduction of the price of all the products that make up the package compared to the offer and prices available on the market for the same type of products.

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<sup>5</sup> Directive 2005/29 EC of the European Parliament and of the Council of 11 May 2005, concerning unfair business-to-consumer commercial practices in the internal market (“Unfair Commercial Practices Directive”), particularly Article 9 (d).

It is unacceptable that the lender may require the purchase of a product and/or service that does not reduce the borrower's risk towards the lender in contracting a certain product and hence reduce the cost (spread) of the loan for the borrower or permit its approval. This is the case of a payment account which is used solely for the purpose of repayment. Moreover, the established process for direct debits (especially SEPA) ensures the frictionless option to ensure payments of instalments irrespective of where (payment institution) the account is held.

Under no circumstances, be it a bundled package, should a provider be allowed to unilaterally change the contract terms of products or services sold, causing damages to the customer, and needs to specify all future prices of the package or an estimation for future prices in case there is a possible change in them (so long as indexed to a relevant price index such as inflation) and for each single product or service that are functional independent. The customer should be informed *ex ante*, with a clear breakdown of all relevant known present **and future costs**, such as monitoring and administration fees, transactions costs, and pre-payment penalties of the products or services contracted, and those conditions should not change over time.

The solution for the identified problems involves the following measures:

- a) Improve Article 12(2) of Directive 2014/17/EU, providing it with a wording that clarifies and remove the exemptions to the general rule prohibiting tying practices, particularly that such a ban may be withdrawn only in the cases set out in (a), (b) and (c). For bundling, this should be transparent with regards to the results in an effective and clear benefit for consumers, considering the offer and prices available on the market for the same type of products, in particular enabling the customer to reduce the risk of defaulting on the loan and, as a result of that reduction of the risk,.
- b) Improve Article 12(3) of Directive 2014/17/EU, providing it with a wording that clarifies and limits the exceptions to the general rule prohibiting tying practices.
- c) Improve Article 17 of the Directive 2014/17/EU to ensure that customer should be informed *ex ante*, with a clear breakdown of all relevant known present and future costs, such as monitoring and administration fees, transactions costs, and pre-payment penalties of the products or services contracted, and those conditions should not change over time, and in the case of the future prices of the package are

unquantifiable at the time of the celebration of the contract, the tied packaging must be prohibited.

- d) Improve Article 9 (d) of the Directive 2005/29 EC and articles 8 and 10 (1) of the Directive 2014/92/EU with the expressed spirit or purpose of the Article 24 Directive 2016/97/EU in order, *mutatis mutandis*, to prohibit the banks and investments firms from practicing coercive tied selling, more specifically, prohibit banks to coerce a client to have a bank account subject to monitoring and administration costs as a condition for buying another product (e.g. insurance, mortgage, funds, *etc.*). An alternative would be to exempt from costs bank accounts that are merely instrumentally used for the sole purpose of repaying a revolving credits / open-end credit (*i.e.* credit card debt, lines of credit, *etc.*) or instalment loans / close-end credit (*i.e.* mortgage loan, car loan, appliance loan, *etc.*)

Another way to introduce these measures could be by:

- e) Materialization of the original intention of the Joint Committee of the EBA, EIOPA and ESMA, to produce guidelines on cross-selling practices that would apply to banking, insurance and investment management, in order to prohibit banks from practicing coercive tied selling, more specifically prohibit banks from coercing a client to have an account in their bank as a condition for obtaining another product or service from the bank (included loans, mortgage, insurances, and investment products).
- f) Improve the Guidelines on Cross-Selling Practices under MiFID II in order to prohibit banks and investments firms from practicing coercive tied selling, more specifically prohibit banks/investments firms from coercing a client to have an account in their bank as a condition for obtaining another investment product or service from the bank/investment firm.