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ACTAS
Policy options for Portugal in the field of over-indebtedness

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Introduction

Unfortunately we did not have a Portuguese National Report when we published our broad interdisciplinary study in the field of over-indebtedness of consumers in Europe (Nick Huls and others 1994). When we conducted our research in 1993, over-indebtedness apparently was not yet a problem in your country. The Conference in Coimbra indicated that this may be different in the near future, so this is a splendid opportunity to bridge the gap.

Portugal seems to be in the take off phase of becoming a credit society, with more characteristics of other European societies. Although it became very clear that Portugal has a strong national legal culture in this field, it was also considered that this country may learn from developments abroad. So, this paper is meant to offer the Portuguese policymakers some background for finding their own solutions. Sometimes it can be an advantage of lagging behind a little bit: you may profit from mistakes that other countries have made and you may pick and choose from the menu of options that exist abroad. This is what historians call «a premium of being backward».

In this paper I offer the findings of our work as a source of inspiration for the development of national Portuguese law and policy making as it is conceived by your Government. Europe is important for Portugal, because of the Second Banking Directive and fiscal policies, which have a strong impact on the development of your welfare state and the working of your local credit market. In our book we have made a Draft-proposal for a Directive, along the lines of the Safe Product Directive, but this has not lead to any initiatives at the European level, so far. The Member states still have a broad authority to regulate in this field.

My impression from the Conference was that the problem of over-indebtedness has not yet led to huge societal problems in your country. My suggestions would be, however, not to wait too long in taking new initiatives. It has some advantages to develop a new system in quiet times. Experience shows that bankruptcy laws which were conceived in hectic circumstances, often are very one sided.

In the following I give an overview of our main findings.

1. The emergence of the credit society

The use of consumer credit in Europe started to grow in the 1960’s. Over the past decades it developed rapidly in all European countries. Credit has become a feature of most of the member states. On the demand side of the economy, credit has become part of the way of life of millions of consumers in the Community. Broad parts of the population buy their homes on mortgage credit, finance their cars with a personal loan or a revolving credit agreement and use their credit cards to shop around. One can also see a democratisation of credit. On the one hand the taking out of a personal loan is no longer necessarily a sign of despair by the poor, on the other hand, the use of credit cards nowadays is no longer a restricted privilege of the well to do. The use of credit has become a normal feature of all industrialised modern societies.

On the supply side one sees that the granting of credit is a lucrative financial service which is offered by all big financial institutions on a massive scale. For the manufacturing industry, credit is an indispensable marketing tool; many products today simply can not be sold if no credit facilities are available. It is necessary for the vitality of many industries that consumer credit is widely available.

The increased use and availability of credit has many positive consequences. Most importantly, credit fuels economic growth. In modern society the use of widely available consumer credit is no longer seen as a sin, but as a contribution to the economy.

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Because of these benevolent effects, it is not surprising that governments help stimulate the use of consumer credit, by regulating the provision of credit and by offering different types of tax incentive.

The most important form of consumer credit today is the mortgage. The provision of mortgages is an essential part of a policy that stimulates home ownership. To have one's own home is of great importance to many people. Mortgage credit has grown rapidly in recent decades, it accounts for the major part of the total credit held by consumers in Europe.

The second important form is non-mortgage consumer credit. A pattern in the provision of consumer credit can be distinguished. In the 1930s, finance companies in Europe started lending money which had a direct relationship with the purchase of consumer goods. Over the past thirty years or so, this relationship has diminished in importance since the big financial institutions entered the consumer credit market in a major way and introduced personal loans and, later, revolving credit. These forms of credit have little if any direct relationship with the sale of a particular good or service. Recently, there has been a reversal of this trend. New forms of credit arise that are again closely related to sale transactions. With new technologies it has become easier for retailers to sell their own products with the help of their own credit facilities. Many new forms of credit (e.g. bank credit cards, shop credit cards and debit cards) have been established and are being used more frequently.

Numerous factors put pressure on the modern consumer to incur liabilities which can lead to debts for reasons that the individual can exert influence on in only a limited way. Credit has become part of modern life-style, which fewer and fewer people can avoid or retreat from.

The European citizen today invests in his home; and handles personal financial management through the use of credit, insurance and numerous other financial services. He is becoming more entrepreneurial, more mobile and more willing to take risks. This readiness to take risk expresses itself, among other things, in the expansion of the use of consumer credit in Europe.

Over-indebtedness: a societal problem

Most experts agree that the primary cause of over-indebtedness is credit. Its rise has coincided with the rise in consumer debt. The data show that everywhere in Europe, over-indebtedness is today found more frequently than several years ago. For various reasons, many consumers are not able to pay back their debts. Such financial entrapment is not restricted to specific social or economic groups, but can happen to almost any user of credit.

Four different groups of overcommitted debtors can be distinguished. The first group is the group that runs into temporary misfortune (i.e. unemployment, divorce, illness, and so on). A second group consists of people that unconsciously become overcommitted. This group makes use of the widely available forms of credit, without realising that they might not be able to repay in the future. The third group are the «poor» who have to take credit in order to attain a reasonable standard of living. The fourth group is the smallest and covers both people that wilfully overcommit themselves financially and people that attempt to defraud their creditors.

The solutions suggested below — which focus on the European dimension — are mostly appropriate for those overindebted consumers that belong to the first and second groups. The third group will benefit only to a limited extent from the changes proposed, and the fourth group will not benefit at all.

Over-indebtedness in most European countries is associated with failure and bankruptcy. The term bankruptcy has stigmatic connotations as it puts the blame on the debtor. Bankruptcy is degrading and can reduce one’s self-esteem which is reinforced by the disapproval of others. Until recently, defaulting debtors could be, and sometimes were imprisoned. Because of the stigma the term bankruptcy bears, the new approach that is suggested for Europe below will not be called «bankruptcy», but «debt settlement» instead.