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Reykjavík, 24 April 2023

TO THE PRESIDENT AND MEMBERS OF THE EFTA COURT

WRITTEN OBSERVATIONS

submitted pursuant to Article 20 of the Statute of the EFTA Court and Article 90 of the Rules of Procedure of the EFTA Court by

THE GOVERNMENT OF ICELAND

Represented by

Ms. Inga Þórey Óskarsdóttir, Legal Advisor, Ministry for Foreign Affairs, and Mr. Eggert Páll Ólason, Specialist, Ministry of Finance and Economic Affairs, acting as Agent, in

Case E-1/23

Elva Dögg Sverrisdóttir and Ólafur Viggó Sigurðsson

v

Íslandsbanki hf.

In which the Reykjanes District Court requests the EFTA Court to give an advisory opinion pursuant to Article 34 of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice concerning the interpretation and application, in particular of Article 24, of 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 (hereinafter the “Mortgage Credit Directive” or the “MCD”), and, as appropriate, Article 10(2) of Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers (hereinafter the “Consumer Credit Directive” or the “CCD”), as further detailed in the request. The Government of Iceland has the honour of lodging the following written observations.

I. INTRODUCTION

1. With an application dated 1 February 2023, the Reykjanes District Court requested the EFTA Court to give an advisory opinion pursuant to Article 34 of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice (“SCA”), on a question in a case before it.
2. In the Court’s letter of 24 February 2023, the Government of Iceland was invited, pursuant to Article 35 of the Rules of Procedure, to lodge written observations within two months from the date of the notification, i.e. by Monday, 24 April 2023, cf. Article 90(1) of the Rules of Procedure.
3. The dispute between the parties concerns whether the provision on variable interest in a mortgage deed issued by the plaintiffs when they received a loan from the defendant should be declared invalid and whether the defendant was entitled to raise the borrowing rate applicable to the amount owed by the plaintiffs under the bond in three interest rate adjustments during 2021.
4. For further details on the factual background of the case, the Icelandic Government refers to the request for an advisory opinion.
5. The question posed to the court is:
Is it compatible with Directive 2014/17/EU (see, in particular, Article 24 thereof) and, as appropriate, with Article 10(2)(f) of Directive 2008/48/EC (cf. recital 19 of Directive 2014/17/EU), that the terms of a consumer property mortgage with variable interest rate state that adjustments of the borrowing rate will take account of factors including operating costs and other unforeseen costs?

II. OBSERVATIONS BY THE GOVERNMENT OF ICELAND

6. It is the position of the Government of Iceland that the Mortgage Credit Directive does not preclude the adjustment of the borrowing rates of mortgage credit agreements to take account of factors including operating costs and other unforeseen costs.
7. This position is, in part, informed by the choice of instrument by the European Union in adopting the Mortgage Credit Directive. Directives are acts addressed to Member States, setting requirements for contents of national law and entailing a national transposition

obligation. Subject to the degree of harmonisation required, directives entail a scope for Member States to decide on adapting the common rules to their national legislative frameworks. The decision of the European Union to adopt the MCD as a directive reflects the fact that mortgage markets differ significantly throughout the EEA, reflecting different national economic circumstances and resulting in diversity in products available across different areas of the Internal Market. This nature of the MCD was stressed by the European Commission when adopting the Proposal for the Directive:

Full harmonisation is not always necessary or appropriate: e.g., the structure of housing markets and mortgage markets differs throughout the EU, and the products and remuneration structures also vary. EU intervention needs to be detailed enough to be effective but high level enough to take into account the EU's diversity. A Directive offers a degree of flexibility in terms of the level of harmonisation. Such targeted provisions can accommodate the diversity that exists in the EU's mortgage markets.

8. The Government of Iceland stresses that this characteristic of the MCD is particularly significant in the wider context of the regulation of financial services and products in the Internal Market, which is to the largest extent done through regulations which are binding as such. Consequently, in the absence of a clear provision to regulate the products in the MCD, such as what variable rates are available to the market, it is clear that the Directive is not meant to limit the factors that can go into ascertaining variable interest rates. The Government of Iceland maintains that the MCD itself does not impose restrictions or prohibitions on changes to the borrowing rate. Rather it makes it clear that Member States can choose to impose such restrictions or prohibitions. Specifically, recital 67 of the MCD states that “Member States should be able to maintain or introduce restrictions or prohibitions on unilateral changes to the borrowing rate by the creditor.”

III. NATIONAL LAW

9. Iceland passed Act No 118/2016 on Consumer Property Mortgage to implement MCD as noted in Article 61. a. in the Act. The Act entered into force on 1 April 2017.
10. The Act defines borrowing rates in Article 4 (1) (21) as:

Interest, specified as a fixed or variable rate, which on an annual basis is applied to the loan amount.

11. Article 34 of the Act is titled “Loan with variable rates” and states in paragraph 1:

If a property mortgage agreement contains a provision stating that reference values, indexes or reference rates are to be used for deciding variable interest rates the creditor may only use reference values, indexes or reference rates that are clear, accessible, objective and verifiable, both by parties to the agreement and by the Consumer Agency (Neytendastofa). If a decision on the change of the interest rate is not based on a reference value, indexes or a reference interest rate, then the mortgage agreement shall state the conditions and procedure for the change of the interest rate.

12. Article 35 of the Act is titled “Information on the changes of borrowing rate” and states in paragraph 2:

The parties can however agree that, in a mortgage credit agreement, that the consumer shall be given information according to paragraph 1 at certain time intervals when the changes on borrowing rates are due to changes in reference exchange rate, reference rate or indexes and the benchmark is publicly disclosed in an appropriate manner, made available to the consumer by the lender and the consumer notified of it together with the amount of new regular payments.

13. Article 37 of the Act is titled “Payment before due date” and states in paragraph 5:

It is not permitted to demand a pre-payment fee:

...

3. If the credit has a variable interest rate.

14. Iceland passed Act No 121/1994 on Consumer Credit to implement CCD as noted in Article 35 in the Act. The Act entered into force on 1 November 2013.

15. Article 5 is titled “Definitions” and states in paragraph 1 (s):

Borrowing rate: Interest, specified as a fixed or variable rate, which is applied to the loan amount on an annual basis.

16. Article 7 is titled “Information before agreement is made” and states in paragraph 4 (f):

lending rates, conditions for their application and, if applicable, index or reference rates that may affect the initial lending rate, as well as the period, conditions and procedure for changing the borrowing rate; if different borrowing rates apply for different situations the aforementioned information about all of them shall be provided.

17. Article 12 is titled “Information that shall be stipulated in the credit agreement” and states in paragraph 2 (f):

lending rates, conditions for their application and, if applicable, index or reference rates that may affect the initial lending rate, as well as the period, conditions and procedure for changing the borrowing rate; if different borrowing rates apply for different situations the aforementioned information about all of them shall be provided.

18. Article 13 is titled “Information on borrowing rates” and states:

The consumer shall be informed of all changes in borrowing rates, on paper or other permanent media, before the change takes effect. The information shall state the amounts to be paid after the entry into force of the new borrowing interest rates and, if the number or frequency of payments changes, information about this. As a general rule, the consumer must be informed of changes 30 days in advance.

However, the contracting parties can agree that, in the loan agreement, the consumer shall be provided with information according to Paragraph 1, at certain intervals when changes in borrowing rates are caused by changes in reference exchange rates, reference interest rates or indexes and the new reference is publicly disclosed in an appropriate manner and made available to the borrower at the lender.

19. The Government of Iceland notes that the mortgage deed was issued by the plaintiffs before the MCD became part of EEA law. It could therefore be disputed whether the contractual terms at issue fall within the scope of EEA law. This issue has not been addressed in the question referred to the Court. However, it is for the EFTA Court to provide the national

court with all elements needed for the interpretation of EEA law that may be of assistance in adjudicating on the case pending before it.

IV. CONSIDERATION OF THE QUESTION REFERRED

20. There is a link between the Mortgage Credit Directive and the Consumer Credit Directive. The MCD refers to the CCD in recital 19, providing that certain essential definitions and key concepts in the MCD should be in line with those set out in the CCD. Member States should therefore ensure, in the transposition of the MCD, that there is consistency of application and interpretation in relation to those essential definitions and key concepts.
21. The Government of Iceland firstly remarks that credit agreements under the CCD have no limitations on variable interest rates. Variable interest rate credit agreements subject to the CCD are diverse and not subject to limitations *per se*.
22. The CCD allows for any type of variable rates subject to change for any reason, and the MCD does not change any definitions of variable interest rates. It follows that the MCD does not preclude any type of variable interest rate, as long as any indexes or reference rates used are clear, accessible, objective and verifiable by the parties to the credit agreement and the competent authorities, and the historical records of indexes for calculating the borrowing rates are maintained either by the providers of these indexes or the creditors. Recital 19 of the MCD makes it clear that terminology should be harmonized between the MCD and the CCD and for reasons of legal certainty the Union legal framework in the area of credit agreements relating to residential immovable property should be consistent with and complementary to other Union acts. The Government of Iceland stresses that no EEA act limits how variable rates are formulated, and the CCD does not contain any ban or limit on any type of variable interest rates.
23. Article 3 (j) of the CCD contains definitions of terms in the Directive and states that *borrowing rate means the interest rate expressed as a fixed or variable percentage applied on an annual basis to the amount of credit drawn down*. There is neither a limitation on how the borrowing rate is calculated or what can constitute a part of the borrowing rate nor an indication that there is a limit or a ban, partial or whole, on how a variable interest rate is calculated or formulated.

24. Article 10 *Information to be included in credit agreements* of the CCD states in paragraph 2 (f) that the Credit agreement shall specify in a clear and concise manner:

the borrowing rate, the conditions governing the application of that rate and, where available, any index or reference rate applicable to the initial borrowing rate, as well as the periods, conditions and procedures for changing the borrowing rate and, if different borrowing rates apply in different circumstances, the abovementioned information in respect of all the applicable rates;

25. Article 10 concerns documentation and information to be provided to the consumer. The Article has no direct bearing on the definition of “borrowing rate”. The Article specifically states that any index or reference rate applicable should be specified in a clear and concise manner. It does not ban or limit the variable rate to take other factors into consideration and change due to other factors. It is well established that the CCD allows for a variable interest rate that can change for any reason.

26. Article 11(1) of the CCD states that where applicable, the consumer shall be informed of any change in the borrowing rate before the change enters into force. Article 11(2) states that if the change is caused by a change in reference rate, the information can be given periodically. The Article clearly makes allowances for the rate to change for other reasons than a change in a reference rate.

27. The high level of consumer protection emphasised in the MCD and the CCD, is achieved through extensive mandatory information requirements and not by subject matter regulation, i.e. the consumer is protected by requiring creditors to provide them with clear and concise standardised information providing the consumer with real choice and enabling a competitive market in credit agreements.

28. The MCD has several references which indicate that there is no limitation on the use of variable interest rates, only that any indexes or reference rates used are to be clear, accessible, objective, and verifiable.

29. Article 24 “Variable rate credits” states:

Where the credit agreement is a variable rate credit, Member States shall ensure that:

- (a) any indexes or reference rates used to calculate the borrowing rate are clear, accessible, objective and verifiable by the parties to the credit agreement and the competent authorities; and
 - (b) historical records of indexes for calculating the borrowing rates are maintained either by the providers of these indexes or the creditors.
- 30. The wording of Article 24 does not contain a ban or limitation on what can be used to determine the variable rate. The phrasing “any indexes or reference rates used” cannot have any other meaning than to say that if indexes or reference rates are used, they must be clear, accessible, objective and verifiable. The words cannot be construed to mean that variable credit is limited to using indexes or reference rates.
- 31. For Article 24 to be construed to limit the factors that can be used to determine variable interest rates it would have to be formulated in such a manner, i.e. the phrasing would have to include clear text to that effect, such as, “Member States shall ensure that only indexes or reference rates are used to calculate the borrowing rate and that they are clear...”
- 32. Annex II to the MCD explains the European standardised information sheet (ESIS). The purpose of the ESIS is to provide customers with relevant information on the credit agreement, including information on interest rates. ESIS therefore contains detailed text on the calculations of interest rates, including variable interest rates.
- 33. Part B, Section 3, point (6) paragraph 2 of Annex II of the MCD states that “The formula used to revise the borrowing rate and its different components (e.g. reference rate, interest rate spread) shall be explained.” It is clear that the borrowing rate can be revised by *other means* than only a reference rate, or an interest rate spread, as indicated by the use of *e.g.* and not *i.e.*
- 34. Part B, Section 3, point (2) of Annex II of the MCD states “Where the borrowing rate is variable and based on a reference rate the creditor may indicate the borrowing rate by stating a reference rate and a percentage value of creditor’s spread.” The phrasing “variable *and* based on a reference rate” clearly indicates that the interest rate can be variable and based on other factors than a reference rate.
- 35. Additionally, the text in Part B, Section 6, point (4), of Annex II states how to calculate the borrowing rate in the future for variable interest credit. The relevant text states that the

information given should be: "...based on the highest value of any external reference rate used in calculating the borrowing rate where applicable, or the highest value of a benchmark rate specified by a competent authority or EBA where the creditor does not use an external reference rate." The Government of Iceland holds that this text clearly does not limit how variable interest is formulated. Furthermore, the text specifically allows for a variable interest rate which is not based on an external reference rate.

36. Article 27 (2) of the MCD states that when the change in the borrowing rate is correlated with a change in a reference rate, Member States may allow the parties to agree in the credit agreement, that information on a change in interest rate is to be given to the consumer periodically, if the new reference rate is made publicly available by appropriate means and the information concerning the new reference rate is kept available in the premises of the creditor and communicated personally to the consumer together with the amount of new periodic instalments. According to this provision variable interest rate can change for many reasons, but where the change in borrowing rate is correlated with a change in a reference rate the information may be given in the manner described in the provision.

V. SUMMARY

37. In light of the above, it is clear that the MCD does not preclude the adjustment of the borrowing rates of mortgage credit agreements to take account of factors including operating costs and other unforeseen costs. The definition of "borrowing rate" does not exclude such factors nor do the information requirements contained in the MCD and the CCD. Additionally, the MCD is a directive meant to take into account the diversity in products on the mortgage market. Recital 67 of the MCD specifically states that States should be able to maintain or introduce restrictions or prohibitions on unilateral changes to the borrowing rate by the creditor. Therefore, it is clear that the MCD itself does not impose restrictions or prohibitions on changes to the borrowing rate. As there is no text in the Directive calling for any limitations or a ban on the factors that can be used to determine variable interest rates, the Court cannot apply such a ban or limitation.

VI. ANSWER TO THE QUESTION REFERRED

38. The Icelandic Government respectfully submits that the EFTA Court answer the question from the national court as follows:

Directive 2014/17/EU does not preclude that the terms of a consumer property mortgage with variable interest rate state that adjustments of the borrowing rate will take account of factors including operating costs and other unforeseen costs.

For the Government of Iceland,

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