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ECJ: Method of calculating compensation for early repayment of loan

In a request for a preliminary ruling from the District Court of Ravensburg (Landgericht Ravensburg) the European Court of Justice was asked for an interpretation of Directive 2014/17/EU on the creditor's right to receive compensation for premature repayment of a loan. The ECJ held that it must be ensured that the calculation by the creditor of its loss of profit from the premature termination, considering the flat rate return on the sum repaid early is fair and objective, and that it does not exceed the creditor's financial loss.

Statutory provisions:

Section 502 (1) German Civil Code (BGB): In the case of early repayment, the lender may require suitable compensation for early repayment of the loan to cover the damage directly related to early repayment if the borrower at the time of repayment owes interest at a fixed borrowing rate. In the case of general-purpose consumer credit agreements, sentence 1 applies only if the fixed borrowing rate was agreed already at conclusion of the loan agreement.

Article 16 (2) Directive 2008/48/EC states that in the event of early repayment of credit the creditor shall be entitled to fair and objectively justified compensation (i. e. either 1% or 0.5% of the amount of credit repaid early) for possible costs directly linked to early repayment (...).

Article 25 Directive 2014/17 (which amended Directive 2008/48) and entitled 'Early repayment', provides that (1) "Member States ensure the consumer's right to discharge fully or partially his obligations under a credit agreement prior to the expiry of that agreement. In such cases, the consumer shall be entitled to a reduction in the total cost of the credit to the consumer, such reduction consisting of the interest and the costs for the remaining duration of the contract. (...) (3) Member States may provide that the creditor is entitled to fair and objective compensation, where justified, for possible costs directly linked to the early repayment but shall not impose a sanction on the consumer."

Background:

On 11 January 2019, the plaintiffs in the main proceedings (MW and CY) concluded a real estate consumer credit agreement with VR Bank Ravensburg-Weingarten eG (hereinafter: VR Bank) for the purpose of acquiring a condominium. In the loan agreement, the borrowing rate of the loan was fixed until 30 January 2029. The loan agreement further stipulated that VR Bank was entitled to compensation for the resulting loss in the event of early repayment. On 19 May 2020, MW and CY sold the property and terminated the loan agreement on 30 June 2020. VR Bank demanded compensation from MW and CY for the early repayment. The plaintiffs claimed that VR Bank was not entitled to the early repayment penalty because the loan agreement did not contain sufficient information on the calculation of the compensation.

The referring court enquires, i. a., whether the compensation of the creditor for costs linked to the early repayment of the loan, as provided for in Article 25(3) of Directive 2014/17, also covers the creditor's loss of profit. The referring court also wished to know the requirements under EU law for the purpose of calculating that loss of profit, in particular also the loss of the remaining contractual interest that would have been payable during the remaining term of the loan.

ECJ decision:

The ECJ held that - in the event of early repayment of a consumer credit relating to residential immovable property – the **compensation may take into account the creditor's loss of profit** borne directly by the creditor as a result of that early repayment and, in particular, the financial loss suffered, **also in connection with the remaining contractual interest** that will no longer be received, provided that the compensation is

fair and objective, that no penalty is imposed on the consumer and that the compensation does not exceed that financial loss.

The ECJ also stated that Article 25(3) of Directive 2014/17 must be interpreted as meaning that **Member States must ensure** that the calculation by the creditor of its loss of profit, **taking into account the flat-rate return on the sum repaid early**, is fair and objective, that it does not exceed the creditor's financial loss and that no penalty is imposed on the consumer. Directive 2014/17 does not require such a calculation to be linked to the manner in which the creditor actually uses the amount repaid to him.

Article 16 (4) (b) of Directive 2008/48 states that Member States may only provide for the right of the creditor **to exceptionally claim compensation in excess of the maximum limit** (as described above under „statutory provisions“) if it can be proven that the loss suffered from early repayment exceeds the maximum limit for compensation determined under Article 16 (2). For the ECJ this shows that interest which will no longer be received following early repayment may be compensated and that the EU legislature regarded **the financial loss of the creditor in the form of interest** as being capable of being included in the potential costs that it incurs because of that repayment.

Finally, the ECJ notes that the objectives of Directive 2014/17 are not limited to ensuring a high level of consumer protection, but also include the creation of an efficient and competitive internal market in credit agreements relating to residential immovable property. Therefore, the national legislature may, given the possibility left to it to determine the permissible cost elements, include as one of the heads of compensation the loss of profit sustained by the creditor where it considers it necessary to further the objectives in its own residential property market. A scheme which does not allow creditors to be compensated for the loss of the remaining contractual interest that would have been paid on the loan may impel them to implement strategies with a potentially undesirable impact on the objectives of Directive 2014/17, such as limiting the range of credit products on offer or charging higher interest to consumers across the board.

Reference:

ECJ, judgment of 14 March 2024 (**C?536/22**) *VR Bank Ravensburg-Weingarten*.

Keywords

compensation payment, early repayment, loan