THE CONSTITUTIONAL COURT
OF THE REPUBLIC OF LATVIA

JUDGEMENT
on Behalf of the Republic of Latvia
in Riga on 12 February 2020
in case No. 2019-05-01

The Constitutional Court of the Republic of Latvia, comprised of: chairperson of the court hearing Ineta Ziemele, Justices Sanita Osipova, Aldis Laviņš, Gunārs Kusiņš, Daiga Rezevska, Jānis Neimanis, and Artūrs Kučs,

having regard to constitutional complaints submitted by limited liability company "ONDO" and Ltd. "ExpressCredit",

on the basis of Article 85 of the *Satversme* of the Republic of Latvia and Para 1 of Section 16, Para 11 of Section 17 (1), Section 19^2 and Section 28^1 of the Constitutional Court Law,

at the court hearing of 14 January 2020 examined in written procedure the case

"On Compliance of Section 1 (1) of the Law of 4 October 2018 "Amendments to the Consumer Rights Protection Law" with Article 1 and Article 105 of the *Satversme* of the Republic of Latvia".

The Facts

1. On 18 March 1999, the *Saeima* adopted the Consumer Rights Protection Law, which entered into force on 15 April 1999.

1.1. By the law of 28 May 2015 "Amendments to the Consumer Rights Protection Law", which entered into force on 1 January 2016, the *Saeima* added to Article 8 of the Consumer Rights Protection Law Parts 2^2 and 2^3, worded as follows:

"(2^2) The costs of a consumer credit agreement shall be commensurate and corresponding to fair transaction practice. The total costs of the credit to a consumer shall be calculated in accordance with the procedures laid down in the laws and regulations regarding consumer credit.

(2^3) Such total cost of the credit to a consumer shall be considered as not corresponding to the requirements referred to in Paragraph 2^2 of this Section which exceed 0.55 per cent of the credit amount per day from the first to the seventh day (including) of using the credit, 0.25 per cent of the credit amount per day from the eight to the fourteenth day (including) of using the credit, and 0.2. per cent of the credit amount per day starting with the fifteenth day of using the credit. In agreements, pursuant to which credit shall be repaid on demand or the term of using the credit exceeds 30 days, such total costs of the credit to a consumer shall be considered as not corresponding to the requirements referred to in Paragraph 2^2 of this Section which exceed 0.25 per cent of the credit amount per day. Restriction of the total costs of the credit to a consumer shall not be applied to such consumer credit agreements upon the conclusion of which an item is to be deposited as security in the creditor's safe-keeping and according to which the liability of the consumer is limited only to that pledged item."

1.2. By Section 1 (1) of the law of 4 October 2018 "Amendments to the Consumer Rights Protection Law" (hereafter – Amendments to the Consumer Rights Protection Law), Section 8 (2^3) of the Consumer Rights Protection Law was expressed as follows:

"Such total cost of the credit to a consumer shall be considered as not corresponding to the requirements referred to in Paragraph 2^2 of this Section which exceed 0.07 per cent of the credit amount per day. Restriction of the total costs of the credit to a consumer shall not be applied to such consumer credit agreements upon the conclusion of which an item is to be deposited as security in the creditor's safe-keeping and according to which the liability of the consumer is limited only to that pledged item" (hereafter – the contested regulation).

Pursuant to Section 3 of the Amendments to the Consumer Rights Protection Law, the contested regulation entered into force on 1 July 2019.

2. Two cases regarding the compliance of the contested regulation with Article 1 and Article 105 of the *Satversme* of the Republic of Latvia (hereafter – the *Satversme*) were initiated at the Constitutional Court.

To facilitate more comprehensive and speedier adjudication of both cases, pursuant to Section 22 (6) of the Constitutional Court Law, they were joined in one case. The joined case No. 2019-05-01 was given the title "On Compliance of Section 1 (1) of the law of 4 October 2018 "Amendments to the Consumer Rights Protection Law" with Article 1 and Article 105 of the *Satversme* of the Republic of Latvia".

3. The applicants – limited liability company "ONDO" and Ltd. "ExpressCredit" (hereafter also – the Applicants) – hold that the contested regulation is incompatible with Article 1 and Article 105 of the *Satversme*.

The applicants are capital companies, which, on the basis of special licences issued for the indefinite period of time by the Consumer Rights Protection Centre, provide consumer credit services. Limited liability company "ONDO" notes that its commercial activities are linked to issuing credits in small amount, i.e., in the amount from EUR 5 to EUR 425, for purchasing goods or services for the period from one day to thirty days. Whereas Ltd. "ExpressCredit" notes that approximately 91 per cent of its unique clients have been issued credits up to the amount of EUR 800 for the period of six months.

It is maintained that the contested regulation does not prohibit the Applicants from engaging in commercial activities in the area of consumer credit. However, it imposes significant restrictions on the total costs of the credit for a consumer and, thus, decreases the possibility for the Applicant to receive due payment for the use of capital for the issued loans, which is said to be the only source of income for the Applicants. The Applicants will not be able to engage in commercial activities in the area of their choice, i.e., issuing short-term loans to consumers, because of the application of the contested regulation. Allegedly, a person's right to engage freely in commercial activities, in particular, if this right has been acquired on the basis of a licence, falls within the scope of Article 105 of the *Satversme*. Hence, the contested regulation is said to restrict the Applicants' right to property, set out in Article 105 of the *Satversme*.

3.1. Allegedly, the restriction on fundamental rights, included in the contested regulation, has not been established by a law adopted in due procedure. The legislator had not had at its disposal appropriate analysis and substantiation regarding the interest rate, its impact on market operators and consumers prior to

adopting it. In the course of adopting the contested regulation, several competent authorities of the state and non-governmental organisations had objected against the intended restriction on interest rate up to 0.07 per cent per day, pointing to the absence of due analysis and the possible negative impact of the contested regulation on the state budget and the accessibility of short-term loans to consumers. However, these objections and offered proposals had not been taken account and had been dismissed without any substantiation.

The initial impact assessment report regarding the draft law (hereafter – annotation) allows concluding that the contested regulation had been adopted because, pursuant to the data of 2017 provided by the Consumer Rights Protection Centre, in some areas of lending, the amount of late term repayments of loans had been large. However, this information, allegedly, is not true because approximately 70 per cent of loans are repaid without extending the term. Likewise, the statements made in the annotations to the draft law that the contested regulation would decrease the burden of debts to consumers and, thus, also shadow economy and emigration of inhabitants, are not substantiated by any concrete data.

Ltd. "ExpressCredit" also doubts whether the wording of the contested regulation is sufficiently clear since the methodology for calculating the total costs of the credit for a consumer per day for loans with a schedule for repayment is not clear. The methodology for calculating the total costs of the credit per day has been explained by the Consumer Rights Protection Centre; however, it should be defined in the law. Moreover, the contested regulation is said to be so unclear that it is not understandable, whether the total costs of the credit have been limited to 0.07 per cent of the total amount of credit per each day of using the credit or on average throughout the total period of using the credit.

3.2. The limited liability company "ONDO" notes that the aim of the restriction on fundamental rights, included in the contested regulation, is to protect consumer rights and facilitate the influx of additional revenue into the state budget. Thus, the contested regulation serves for such purposes as the protection of other persons' rights and public welfare. Ltd. "ExpressCredit", in turn, is of the opinion: although the restriction on fundamental rights might have a legitimate aim, i.e., protection of other persons' rights, the legislator, in adopting the contested regulation, has not appropriately substantiated the existence of such an aim.

The chosen measure is said to be inappropriate for reaching the legitimate aim of the restriction on fundamental rights because, as the result of applying the contested regulation, short-term loans would effectively disappear from the market. A person wishing to borrow a small amount would be forced to take a

longer-term loan and thus, the total costs of the credit would increase. Moreover, with short-term loans disappearing from the market, the number of merchants operating in the market would decrease significantly, as would the turn-over of those individual merchants who would continue their operations. This would leave a negative impact on the state budget.

Other measures, restricting the merchants' rights and interests to a lesser extent, are said to be available for reaching the legitimate aims of the restriction on fundamental rights; these had not been examined by the legislator. For example, it is possible to ensure appropriate assessment of a consumer's creditworthiness. Already now, the Consumer Rights Protection Centre has been granted extensive rights to supervise operations of entities providing crediting services. Likewise, the legislator could have retained the restrictions on the total cost of credit, established previously, and adopt additional regulation that would encourage consumers to borrow more responsibly. Moreover, the legislator could have defined such interest rate that would ensure decreasing of the total costs of the credit but, at the same time, would restrict the Applicants' rights to a lesser extent, e.g., to set the restriction on the annual interest rate in the amount of 60 per cent of the total costs of the credit. In the course of adopting the contested regulation, the responsible committee of the *Saeima* had supported the proposal by the Bank of Latvia regarding decreasing the interest rate. Although the limited liability company "ONDO" does not support this alternative proposal either, it, in difference to the contested regulation, had been elaborated by experts, *inter alia*, analysing the market situation in Latvia and in the neighbouring countries.

The benefit that society gains from restricting the Applicants' right to property is said to not outweigh the damage inflicted on their rights and lawful interests. As the result of applying the contested regulation, no more than 10 per cent of active inhabitants will have access to consumer credit. Moreover, with short-term loans disappearing from the market, the risk that illegal crediting could expand and could have a negative impact on competition should be taken into account. Therefore, the proportionality principle had not been complied with.

3.3. The legislator had set limits to the total costs of the credit already before – by the law of 28 May 2015 "Amendments to the Consumer Rights Protection Law". The Applicants had expected that, thus, the State had introduced into the respective sector clear rules for engaging in commercial activities. If at the time when the Applicants were issued licences for engaging in commercial activities the contested regulation had been in force, they would have planned their activities differently. The transitional period, set by the legislator, in turn, is said to be

disproportionally short, because it is possible to reorient commercial activities so as not so suffer significant loses within eight and a half months. Moreover, in adopting the contested regulation, the legislator has envisaged no compensatory mechanism with respect to the Applicants. Thus, the principle of legitimate expectations had been violated.

3.4. After familiarising themselves with materials in the case, the Applicants note that they do not uphold the *Saeima's* reasoning that the contested regulation does not restrict their right to property, envisaged in the first sentence of Article 105 of the *Satversme*. Although the contested regulation has been in force only for a short period, the financial indicators and estimates show that the Applicants will not be able to engage in long-term commercial activities due to the restriction included in it.

The Applicants underscore that the restriction on fundamental rights, included in the contested regulation, has not been established by a law adopted in due procedure. Namely, before its adoption, appropriate analysis of the situation had not been conducted to clarify why the desirable aim was not reached by the previous valid regulation, neither research of the most appropriate solution or assessment of the impact caused by the contested regulation had been conducted. If it is applied in the long-term, the accessibility of credit resources in economy will significantly deteriorate because credits will become more expensive and the competition between non-banking creditors will decrease. In the course of adopting the contested regulation, allegedly, it had not been analysed at all why exactly 0.07 per cent of the credit amount per day should be considered as being an appropriate rate. In 2017, prior to the adoption of the contested regulation, the Ministry of Economics had proposed to set out that the total costs of the credit for a consumer that exceed 0.1 per cent of the credit amount per day should be deemed as being inappropriate. However, prior to adopting the contested regulation, the legislator did not duly assess alternative measures, moreover, did not consider also whether, pursuant to the legal acts of the European Union, the European Commission had to be notified about the Amendments to the Consumer Rights Protection Law, which introduced the contested regulation.

Ltd. "ExpressCredit" states its considerations also as to why the contested regulation should not be considered as being sufficiently clear. I.e., in adopting the contested regulation, the legislator had not taken into account that there were several types of credit repayment, *inter alia*, the annuity method. In applying the contested regulation, it is impossible to determine correctly the total costs of the credit per day regarding the loans for the repayment of which this method is used.

In the course of adopting the contested regulation, the Consumer Rights Protection Centre also had pointed to this, proposing to set restrictions on the annual interest rate because the formula for calculating it had been clearly defined in regulatory enactments.

4. The institution, which issued the contested act, – **the *Saeima*** – states in its written reply that the contested regulation complies with Article 1 and Article 105 of the *Satversme*.

4.1. Article 105 of the *Satversme*, allegedly, does not envisage legal protection for a person's possibilities to gain profit because such abstract possibility cannot be regarded as an object of the right to property. Likewise, the principle of legitimate expectations does not prohibit the legislator from limiting a person's right to property in accordance with public interests, *inter alia*, by amending legal regulation.

The contested regulation does not envisage annulment or suspension of the licence issued to the Applicants, it only establishes restrictions on the total costs of particular service, i.e., lending, covered by the consumer. The possible abstract decrease of the Applicants' profit caused by the application of the contested regulation cannot be regarded as a restriction on the right to property. Limiting the total costs of the credit to 0.007 per cent of the credit amount per day *per se* cannot be regarded as such that would be disproportionally low or such that would prohibit a person from gaining fruits from their property. Hence, it is maintained that the contested regulation does not restrict the Applicants' right to property that follows from Article 105 of the *Satversme*.

4.2. Even if the contested regulation restricts a person's fundamental rights, set out in Article 105 of the *Satversme*, it had been established by a law adopted in due procedure. The legislator had heard and examined objections made by representatives of the sector at several sittings of the responsible committee. Likewise, alternatives to the contested regulation had been very extensively discussed at the sittings of the responsible committee. Members of the responsible committee, in supporting the proposal made by the working group of the Ministry of Finance and the Bank of Latvia, accepted regulation that envisaged recognising as disproportional and inappropriate such total costs of the credit that, expressed as the annual interest rate, at the moment of concluding the consumer credit agreement, exceed three times the annual weighed interest rate for consumer credits in EUR of six months. However, Members of the *Saeima* did not support

this proposal, being of the opinion that the contested regulation was a more suitable measure for protecting consumer rights.

The legitimate aim of the restriction on human rights is said to be the protection of other persons', i.e., the consumer's, rights. Namely, in adopting the contested regulation, the legislator's aim had been to prevent the practice where the costs of the issued credit for a consumer, in particular, for a socially more vulnerable person who experienced financial difficulties, were so disproportionally high that could be considered as being incompatible with fair transaction practice and could even be equalled to usury. Likewise, the restriction is said to promote responsible borrowing since the possibility for a person to assume quickly and without due considerations debt commitments, which they cannot afford, is decreased. Influencing consumers' behaviour by restricting the accessibility of a certain product or service is an admissible practice within the legal system.

4.3. The measure chosen by the legislator ensures that neither the payments of credit interest nor the commission in total or separately can be set in the amount that would create disproportional costs for the consumer. This is said to protect both those consumers who have made a well-considered choice to take a loan and also those consumers who perhaps have received the loan without due assessment of their financial possibilities and needs. The cases when loans are issued to persons who are unable to repay them are said to be far from infrequent. The fact that that the application of the contested regulation might lead to decrease in the offer of short-term credits is said to be compatible with consumers' interests. Such loans are not to be used to satisfy persons' needs for daily commodities, as well as for paying bills or purchasing medicines. Such use might lead to the cycle of repeated loans, which only increases persons' debt obligations in the long term.

Alternative measures had been examined sufficiently in the course of adopting the contested regulation; however, the legislator had considered that they would not allow reaching the legitimate aim of the restriction in equal quality. Likewise, a more effective verification of a consumer's credit worthiness cannot be considered as being an alternative measure. The obligation of the creditor has been imposed the obligation to assess a consumer's ability to repay the loan before concluding the credit agreement in the Consumer Rights Protection Law for a long time already. However, in many cases, this obligation is not performed effectively, therefore the legislator has the right and the obligation to introduce also other measures that would ensure due protection of public interests.

The legislator is said to have a broad margin of appreciation in protecting the interests of a more vulnerable societal group. The restriction, included in the contested regulation, does not prohibit the Applicants from engaging in commercial activities in a sector of their choice. Moreover, the legislator has established a sufficiently long transitional period that allows the Applicants and other creditors to duly plan their activities in compliance with the contested regulation.

5. The summoned person – **the Ministry of Finance** – notes: to conduct comprehensive research related to the proposed amendments to legal acts regulating consumer credit, as well as to prepare concrete proposals, by the Order of the Prime Minister of 1 August 2018 No. 20 "On Working Group", a working group was established (hereafter – the Working Group). The Working Group was headed by the Minister for Finance, and representatives of the Ministry of Economics, the Ministry of Justice, the Finance and Capital Marker Commission, the Consumer Rights Protection Centre, the Bank of Latvia, the Cross-sectoral Coordination Centre, the Finance Latvia Association and the Alternative Financial Services Association of Latvia had been included in its.

The majority of institutions represented in the working Group had supported the decrease of the total costs of the credit for a consumer and asked to define a united rate. The Working Group had analysed also information on regulation in other countries. According to the assessment prepared by the Bank of Latvia, prior to the adoption of the contested regulation, the maximum total costs of the credit for a consumer in Latvia had been the highest in the Baltics. Such rates are appropriate for loans that are issued for a short term and constitute less that one per cent of the total portfolio of issued credits within economy.

In promoting responsible crediting and ensuring accessibility of appropriate financial resources, *inter alia*, diversity of the range of financial instruments and providers of services, proportionality of costs of the crediting services, as well as competition between providers of the respective services, decreasing the maximum rate of the total costs of the credit had been justified. To ensure competitiveness of the Latvian financial sector and prevent expansion of shadow economy, it had been recommended in the Working Group's report to define an unchanging maximum rate of the total costs of the credit depending on the term for using the credit and not lower than the actual rates of financial instruments extensively used in the financial sector, as well as to equal it to the lower rate of total costs of the credit established in the other Baltic States.

The Working Group's report, as well as the material on the credit rates of consumer credit, prepared by the Bank of Latvia, had been submitted to the responsible committee. However, it should be taken into account that the state institutions and the association "Latvian Alternative Financial Services Association" did not reach a consensus regarding restrictions on the total costs of the credit for loans issued for up to 30 days

6. The summoned person – **the Ministry of Economics** – notes that stricter limiting of the total costs of the credit for a consumer is justified and necessary. However, the restriction should be such that would ensure balance between the interests of consumers and creditors.

The Working Group had concluded that the annual interest rate should be used for restricting the total costs of the credit. It is said to be the only interest rate that reflects precisely the expensiveness of credits and has a methodology for calculating it established in regulatory enactments. The methodology for calculating this rate allows applying the annuity method to the repayment of loans issued for a longer period or to envisage a schedule for repaying the loan. Because of this, an alternative proposal had been submitted to the responsible committee, providing that such total costs of the credit for a consumer, which, expressed as the annual interest rate, at the moment of concluding the consumer credit agreement exceeded more than three times the average weighed annual interest rate of credits in EUR issued to residents' households of six months, as being incompatible. However, the legislator had dismissed this proposal.

Allegedly, the contested regulation will have an impact on those creditors who are offering crediting services with relatively high interest rates, short terms of re-payment and demand repayment of the credit in a single payment. Possibly, as the result of applying the contested regulation, such loans will no longer be offered because they will become economically unprofitable. Loans with longer terms of repayment and for a larger amount will be offered instead. Whether merchants will be forced to discontinue their operations is said to depend on the abilities of each creditor to adjust to changes in the market and opportunities for making profit.

7. The summoned person – **the Consumer Rights Protection Centre** – notes that the impact of the contested regulation on the credit sector should be assessed as being similar to the one caused by the restrictions on the total costs of the credit per day, defined by the law of 28 May 2015 "Amendments to the

Consumer Rights Protection Law". At that time, the introduction of restrictions also had caused concern among creditors regarding unprofitability of commercial activities and possible discontinuation of operations; however, this had not happened. Moreover, it can be predicted that, with decreasing offer of short-term loans, the number of persons who might assume the respective commitments without due considerations would also decrease.

7.1. The payments that constitute the total costs of the credit for a consumer have been defined in the Consumer Rights Protection Law. These are all costs, including interest, commission, fees and any other payments, which must be paid by the consumer in relation to the credit agreement and which are known to the creditor (except costs of a sworn notary). The total costs of the credit include also costs for additional services in relation to the credit agreement, including insurance premiums, if conclusion of an additional services contract is a mandatory precondition in order to receive credit or in order to receive it on the terms and conditions offered.

The contested regulation is said to limit the total costs of the credit per day. However, regulatory enactments do not define how to calculate the total costs of the credit per day. Since the total costs of the credit are calculated and indicated in agreements for the entire term of crediting, in calculating the costs of the credit per day, mathematically, the indicator of the costs determined for the entire term of credit agreement should be divided by the number of days constituting this term. However, it is easy to make these calculations if the loan is repaid in a single payment. Whereas in cases where the credit repayment is not made as single payment, allegedly, it is impossible to make correct calculations to verify whether the restriction, included in the contested regulation, is complied with. Moreover, the contested regulation is said to create a situation where the expensiveness of the credit is influenced by the term of the credit agreement. I.e., the maximum admissible annual interest rate is said to be lower for short-term credits compared to long-term credits. Thus, the restriction, included in the contested regulation, does not ensure equivalent restriction of costs for all types of credit agreements. Moreover, it is not economically justified because the costs of short-term crediting will always be higher.

Already after adoption of the contested regulation, the Consumer Rights Protection Centre had pointed out to the legislator the shortcomings in the application of this regulation and had called for amendments to law and using the annual interest rate for restring the total costs of the credit, for the calculation of which a clear procedure has been defined in regulatory enactments and which

reflected the expensiveness of credit most precisely. The legislator, however, dismissed this proposal.

7.2. Application of the contested regulation, most probably, will mean that it will no longer be profitable for creditors to issue loans in small amounts for a term up to 30 days. It is alleged that there is a risk that, in such a case, those creditors who continue to offer short-term crediting services, might introduce measures to decrease the costs of the crediting, i.e., minimise the procedure for assessing consumers' ability to repay the credit, and the quality of this process, as well as to invest comparatively smaller resources for introducing a qualitative internal control system and customer due diligence. Several creditors might discontinue their operations, even they would reorient their activities to offer only long-term credits. This might impact competition in the market.

Accessibility of consumer credit is said to be essential for the development of the entire economy. When the licencing of non-bank creditors was introduced, also the criterion for assessing consumers' creditworthiness was introduced, and it is said to be the most important criterion of responsible lending. The total costs of the credit for a consumer may be restricted; however, the respective restrictions should not jeopardise the nature of the particular crediting service. For example, issuing of short-term credit is said to be such crediting service that is characterised by high costs and short terms, thus, this type of credit is classified as high-costs short-term credit, the access to which is quick and simple. It should be taken into account that, from the perspective of financial literacy, and most vulnerable to such credits are consumers with low, irregular income or with negative credit history.

8. The summoned person – **the Ombudsman** – holds that the contested regulation does not restrict the Applicants' rights, established in Article 1 and Article 105 of the *Satversme*.

8.1. The rights to engage in a certain type of commercial activities, obtained by the Applicants, are said to fall within the scope of the first sentence of Article 105 of the *Satversme*. However, the contested regulation, substantially, does not prohibit them for continuing crediting consumers on the basis of a licence. This is proven by the fact that, following the adoption of the contested regulation, the Applicants continue offering their services to consumers. Most probably, the application of the contested regulation will result in decreasing profits for the Applicants; however, Article 105 of the *Satversme* does not protect the right to profit.

8.2. Assuming that the contested regulation restricts the Applicants' right to property, the Ombudsmen, nevertheless, upholds the statement made in the *Saeima*'s written reply that the restriction on fundamental rights has been established by law, it has a legitimate aim, and it is proportional to the legitimate aim.

The legislator has heard and examined proposals made by representatives of the sector at several sittings of the responsible committee of the *Saeima*. In comparison with the former valid regulation, the contested regulation is said to decrease substantially the total costs of the credit for a consumer and, thus, prevents disproportionally high payment for credit. Issuing of such short-term loans to persons with low income and young people should not be supported. The legislator had introduced diverse measures for consumer protection before; however, these had not been sufficient. Namely, the amount of short-term loans had only continued to increase and, likewise, the amount of those loans, for which the term of repayment had been prolonged three and more times. Hence, the benefit that society gains from the contested regulation outweighs the damage inflicted upon the grantor for credit.

The content of the contested regulation had been known to the Applicants since June 2018; hence, their legitimate expectations had received sufficient protection.

9. The summoned person – **the Bank of Latvia** – notes that it upholds the reasoning included in the written reply by the *Saeima* that the contested regulation had been adopted in due procedure.

The Bank of Latvia had participated in the Working Group, which had been established in relation to the proposed amendments to the legal acts regulating consumer crediting. Materials, prepared by the Working Group, had been presented to the responsible committee of the *Saeima*. Moreover, at the time of drafting the contested regulation, also the Bank of Latvia had expressed its opinion publicly and informed society, justifying why the total costs of the credit should be decreased.

In adopting the contested regulation, the legislator had chosen to restrict the total costs of the credit more substantially than had been recommended by the Bank of Latvia; however, alternatives measures had been examined in the course of adopting this regulation. It is not expected that, as the result of applying the contested regulation, the accessibility of credit resources in economy would

substantially decrease, however, it can be predicted that the contested regulation will promote more responsible crediting.

10. The summoned person – association "Latvian Alternative Financial Services Association" – subscribes to the Applicants' opinion that the contested regulation is incompatible with Article 1 and Article 105 of the *Satversme*.

A short-term loan, essentially, is neither worse nor better than a long-term loan or other types of loans and financial products. These are said to be different products that meet different needs of consumers. Because of their nature, they are linked to different costs and risks, which both the creditor and the consumer should take into account. Various studies and facts indicate that short-term loans are necessary and their inaccessibility could cause greater harm to consumers than their accessibility. The legislator should ensure that such legal regulation is adopted that would ensure not only that consumers would be protected, to the extent possible, from malicious actions by creditors and other risks, but also that the market of short-term loans would be able to exist and thus, this service, required by consumers, would be accessible.

Following adoption of the contested regulation, many creditors are altering their products, increasing both the amounts and the terms of loans. Therefore, those consumers who need resources for satisfying their short-term needs are forced to borrow amounts that are larger than their need or for longer terms than necessary and, thus, pay to creditors more than before the contested regulation was adopted. After it entered into force, some creditors have discontinued their operations or are planning to do so.

Although the contested regulation is said to be sufficiently clear and comprehensible to professionals of the sector and the Consumer Rights Protection Centre, it is not certain, whether the legislator itself clearly understands what exactly it has envisaged. In the course of adopting the contested regulation, it had been explained that, pursuant to it, no interest rate of a loan would exceed 25 per cent annually. However, the annual interest rate is not calculated by multiplying the days in a year with the interest rate of 0.007, defined in the contested regulation. It is calculated in accordance with the formula defined in the Cabinet Regulation of 25 October 2016 No. 691 "Regulations regarding Consumer Credit". Hence, the calculation of the annual interest rate is said to depend on several factors, *inter alia*, the term and amount of loan. Calculations prove that the annual interest rate is higher for loans with shorter terms compared to loans with longer terms. Likewise, the annual interest rate is lower for loans of larger amount compared to

smaller loans, even if the terms for repayment are the same. However, this is not logical because short-term loans, objectively, cost more for the creditor. To be able to cover the costs related to reviewing loans also in the future, creditors are forced to offer to consumers credit products for longer terms and in larger amounts, which are more expensive for consumers and, thus, less favourable.

The legislator, in defining the objectives for drafting the contested regulation, had relied on false data and statements. 0.07 per cent, included in the contested regulation, is said to be a number that appeared without calculations, substantiation, and analysis. Validity of the contested regulation, possible consequences of its application and impact on creditors, consumers and economy in general had not been examined. Neither the changes that had occurred in the market following the previous amendments to the Consumer Rights Protection Law, by which the total costs of the credit for a consumer were restricted, had been analysed. Contrary to the legislator's assertions, after 1 January 2016, the number of distance consumer credits, issued for the term of 30 days, had rapidly decreased. Likewise, the doubts expressed by competent authorities and experts regarding the quality of the contested regulation had been disregarded. Thus, in adopting the contested regulation, the legislator, perhaps, has complied with the formal rules for its adoption; however, the principle of good legislation had been violated.

11. The summoned person – association "Latvian Association of Borrowers" – holds that the contested regulation complies with Article 1 and Article 105 of the *Satversme*. The restriction on fundamental rights, included in it, is said to be proportional, and the principle of legitimate expectations has not been violated either. Moreover, Article 105 of the *Satversme* does not protect a person's possibility to gain profit because such abstract possibility is not the object of the right to property.

In the course of adopting the contested regulation, association "Latvian Association of Borrowers" had supported it. The disproportional total costs of the credits have resulted in the inability of several thousand of borrowers to repay the loan in time. The restriction, included in the contested regulation, will prohibit creditors from using property contrary to public interests.

12. The summoned person – *Mg. iur.* Zanda Dāvida, PhD student at the Faculty of Law, the University of Latvia, – notes that the necessity to ensure high-level of consumer rights protection is particularly underscored in the European Union law. This necessity is linked to the sensitive nature, public

importance of this area, as well as insufficient protection of borrowers in the circumstances of the free market regulation

In the conditions of globalisation and digitisation of society, as well as abundance of information and various services, the importance of consumer rights protection only increases. If consumer rights protection is not sufficient and effective not only the historically classical consumer rights can be jeopardised but also the national security, social and economic values of society may be negatively impacted. Legal acts of the European Union do not establish special requirements with respect to short-term consumer credits. Thus, the Member States have the discretion to adopt the most appropriate regulation, by assessing the needs of society and merchants, social and economic situation of the state, its traditions and history, as well as the consumer's profile and anticipated behaviour.

It should be taken into account that a consumer is in a disadvantageous situation, compared to the merchant, in particular, with respect to information, and therefore it should be considered that a consumer is economically weaker and with less legal experience than the merchant. However, the legislator may decrease this inequality by intervening. Moreover, in the framework of the modern "society of credits", the issue of poverty and the need to provide special protection to consumers with low income has become relevant.

The legislator's reasoned choice of a particular type of consumer rights protection is said to be a political decision, which does not always coincide with the stakeholder's understanding of the most appropriate solution. It is important to conduct empirical and economic research in the course of drafting the regulation on consumer rights protection. However, it should be taken into account that such studies are expensive and time-consuming. In cases of doubt regarding the middle point in the balance of protected values or where circumstances force the legislator to resolve a problematic situation swiftly, consumers' interests take the priority. Moreover, the adopted regulation should not foster the development of "society of credits". In adopting the contested regulation, the legislator has abided by these principles and the contested regulation complies with Article 1 and Article 105 of the *Satversme*.

13. The summoned person – Associate Professor of BA School of Business and Finance *Dr. iur.* Jānis Grasis – holds that the contested regulation complies with Article 1 and Article 105 of the *Satversme*.

The contested regulation does not envisage annulling or suspending the licence issued to the Applicants. It only defines restrictions on the total costs of the

crediting service covered by a consumer. Hence, the contested regulation does not prohibit the Applicant from engaging in commercial activities on the basis of the licence issued to them.

In reviewing the constitutionality of the contested regulation, it should be taken into account that Latvia's residents have very small savings, i.e., for approximately two-thirds of society their savings are not sufficient to allow considering their financial situation as being stable. Likewise, in accordance with the data provided by the State Revenue Service on the undeclared salaries or the so-called "salaries in envelopes", in 2018, approximately 19 per cent of those employed have received such. Allegedly, persons who receive salaries regularly and legally, actually, do not need short-term loans because, in case of need, they can use products offered by commercial banks. Moreover, the level of financial literacy is very low in Latvia.

The legislator's aim, in adopting the contested regulation, had been to protect the consumers with low income and not particularly high financial literacy. The benefit for society is said to outweigh the damage caused for the creditors. The contested regulation has been adopted in the procedure set out in the *Satversme* and the Rules of Procedure of the *Saeima*, has been promulgated and is publicly accessible in accordance with the requirements defined in regulatory enactments. The restriction on fundamental rights, included in it, is said to be sufficiently clear. In the course of adopting the contested regulation, association "Latvian Alternative Financial Services Association", the Latvian Chamber of Commerce and Industry, the Association of Latvian Commercial Banks, as well as other stakeholders have been heard. The fact that the opinion of these persons was not taken into account cannot serve as the grounds for recognising the contested regulation as being incompatible with the *Satversme*.

In adopting the contested regulation, the legislator had envisaged a sufficiently long transitional period for the Applicants and other grantors or credit to plan appropriately their operations in compliance with the new regulation. The right of some creditors to financially viable business that brings profit fast, for the sake of which people, who have encountered financial hardship, should sacrifice themselves, cannot be more important than the State's obligation to protect consumers and create a sustainable crediting environment. There are no grounds to consider that the application of the contested regulation would cause any substantial negative consequences for the entire economy.

14. The summoned person – ***Dr. iur.*** **Vadims Mantrovs, Docent of the Department of Civil Law, the Faculty of Law, the University of Latvia** – holds that the contested regulation complies with Article 1 and Article 105 of the *Satversme*.

In the area of crediting services, it is important to ensure consumer protection of a particularly high level. Also in Latvia, the legislator, trying to protect consumers and their financial interests as much as possible, in recent years, has consistently made the requirements set for the provision of crediting services more stringent. The contested regulation is one of the measures for consumer rights protection.

In difference to the previous valid regulation, it no longer envisages differential restrictions on the total costs of the credit for a consumer, depending on the term of credit, but defines a united restriction. Moreover, the contested regulation significantly decreases the maximum amount of daily interest rate in the total costs of the credit for a consumer. This restriction is said to be linked to the adverse situation regarding fulfilment of consumer credit agreements and high interest rates. Moreover, it should be taken into account that the legislator, by adopting the contested regulation, has not totally denied access to crediting services but has defined restrictions on the total costs of the credit to be covered by a consumer per day. This does not prohibit the Applicants and other creditors from engaging in commercial activities in the area of consumer credit.

In adopting the contested regulation, the legislator has not envisaged either the highest or the lowest restriction on the total costs of the credit per day, compared to other European states. Although the criteria that the legislator has followed, in choosing the particular amount of per cent, are not indicated in the annotation to the draft law, this alone cannot be the grounds for recognising the contested norm as being incompatible with the *Satversme*. Latvia, like any other European state, may choose the most appropriate model for restricting the total costs of the credit to ensure the consumer rights protection on a particularly high level. The restriction, established by the contested regulation, is justified also from the perspective of the return of capital. The principle of legitimate expectations does not guarantee to the Applicants that the legislator, in view of the need for particularly strong protection of the consumer, would not decrease the amount of interest rate for the total costs of the credit per day.

The Findings

15. The contested regulation expresses Para 2^3 of Section 8 of the Consumer Rights Protection Law in a new wording, providing that such total costs of the credit to a consumer are considered as not corresponding to the requirements referred to in Paragraph 2^2 of Section 8 of this Law which exceed 0.07 per cent of the credit amount per day. Restrictions of the total costs of the credit to a consumer are not to be applied to such consumer credit agreements upon the conclusion of which an item is to be deposited as security in the creditor's safe-keeping and according to which the liability of the consumer is limited only to that pledged item. Section 3 of the Amendments to the Consumer Rights Protection Law provides that the contested regulation enters into force on 1 July 2019.

The present case was initiated before the contested regulation entered into force. At the time of reviewing the case, it had come into force.

Thus, the Constitutional Court will review the constitutionality of Para 2^3 of Section 8 of the Consumer Rights Protection Law (hereafter – the contested norm).

16. The Applicants request reviewing the compatibility of the contested norm with Article 1 and Article 105 of the *Satversme*, being of the opinion that it restricts their right to property and violates the principle of legitimate expectations.

If the compliance of a contested norm with several legal norms of higher legal force is challenged then the Constitutional Court, taking into account merits of the case, must define the most effective approach to this compliance review (*see, for example, Judgement of 18 October 2018 by the Constitutional Court in Case No. 2017-35-03, Para 8*).

16.1. Article 105 of the *Satversme* provides: "Everyone has the right to own property. Property shall not be used contrary to the interests of the public. Property rights may be restricted only in accordance with law. Expropriation of property for public purposes shall be allowed only in exceptional cases on the basis of a specific law and in return for fair compensation."

When the compliance of a legal norm with the entire Article 105 of the *Satversme* is contested but the contested norm does not provide for expropriation of property for public purposes, the compliance of this norm with only the first three sentences of Article 105 of the *Satversme* must be reviewed (*see, for example, Judgement of 7 July 2014 by the Constitutional Court in Case No. 2013-17-01, Para 18, and Judgement of 13 October 2015 in Case No. 2014-36-01, Para 15.1.*).

Since the present case does not pertain to expropriation of property for public purposes, the contested norm should be reviewed in the scope of the first, second and third sentence of Article 105 of the *Satversme*.

16.2. Article 1 of the *Satversme* provides that Latvia is an independent democratic republic.

The Constitutional Court has recognised that the principle of legitimate expectations, derived from the basic norm of a democratic state governed by the rule of law, falls with the scope of Article 1 of the *Satversme*, this principle protects only such rights with respect to exercising of which a person could develop lawful, valid and reasonable expectations, which is the core of this general legal principle. The State, in turn, is obliged to abide by this principle in its activities.

The principle of legitimate expectations is linked to the principle of legal security and ensures the stability required by it, prohibiting inconsistent actions by the State. The foundation of this principle is that an individual may expect that the State would act lawfully and consistently, whereas the State must protect the trust it has been granted. Existence of the principle of legitimate expectations, as one of the general legal principles, is linked not only to trusting the state power but also to the possibilities for the addressees of legal norms to exercise their discretion.

The principle of legitimate expectations protects the rights that a person once has acquired, i.e., a person may expect that the rights that have been obtained in accordance with a valid legal act will be retained and exercised within a certain period. However, the principle of legitimate expectations does not exclude the possibility that the rights, once acquired by an individual, might be amended in a legal way. Namely, this principle does not give the grounds for expecting that the legal situation, once established, will never change. It is also essential that, in such a case, the legislator defines a "lenient" transitional period (*see Judgement of 8 March 2017 by the Constitutional Court in Case No. 2016-07-01, Para 16.2.*).

In the present case, the principle of legitimate expectations is closely linked to the possible restriction on the right to property. Namely, the Applicants had expected that since the legislator had set out concrete rules for commercial activity, i.e., consumer crediting, they, abiding by these rules, would be able to engage in this activity. Thus, in examining the possible restriction on a person's right to property, the principle of legitimate expectations also should be taken into account.

Hence, the compliance of the contested norm with the principle of legitimate expectations should be reviewed in conjunction with the possible restriction on the right to property.

17. The Applicants note that because of the restriction established by the contested norm they would no longer be able to issue credits in small amounts for a period up to 30 days and, thus, it prohibits the Applicants from engaging in commercial activities on the basis of a licence.

Whereas the *Saeima* and several persons summoned in the case, *inter alia*, the Ombudsman and J. Grasis, hold that the contested norm does not prohibit the Applicants from providing consumer credit on the basis of a licence also in the future. Namely, it does not envisage annulment or suspension of the issued licences but only imposes limits on the total costs of the credit. The special licences that have been issued allow the Applicants to continue issuing to consumers credits in small amounts. The possible abstract decrease of the Applicants' profits, in turn, cannot be considered to be a restriction on the right to property.

To examine the compliance of the contested norm with the right to property, enshrined in Article 105 of the *Satversme*, and the principle of legitimate expectations, it must be established, first and foremost, whether this norm restricts the respective right.

17.1. Article 105 of the *Satversme* envisages a comprehensive guarantee for rights of financial nature. "The right to property" is to be understood as all rights of financial nature that the eligible person may use for their own benefit and may handle as they would wish to (*see, Judgement of 30 March 2011 by the Constitutional Court in Case No. 2010-60-01, Para 17.1., and Judgement of 7 June 2012 in Case No. 2011-19-01, Para 9.1.*). It comprises the owner's right to use their property for gaining maximum economic benefit (*see Judgement of 26 April 2007 by the Constitutional Court in Case No. 2006-38-03, Para 11, and Judgement of 12 November 2008in Case No. 2008-05-03, Para 7*). The Constitutional Court has recognised that a person's right to engage in commercial activities on the basis of a licence falls within the scope of the right to property (*see, for example, Decision of 20 April 2010 by the Constitutional Court on Terminating Legal Proceedings in Case No. 2009-100-03, Para 8.2., and Judgement of 12 December 2014 in Case No. 2013-21-03, Para 10.1.*).

It follows from the case materials that, pursuant to the Cabinet Regulation of 29 March 2011 No. 245 "Regulations Regarding the Special Permit (Licence) for the Provision of Consumer Credit Services" (hereafter – Regulation No. 245), the Applicants had been issued special permits (licences) for the provision of consumer credit services for an indefinite period (*see Case Materials, Vol. 1, pp. 40–44, Datubāze. Kapitālsabiedrības, kuras saņēmušas speciālo atļauju*

(licenci) patērētāju kreditēšanas pakalpojumu sniegšanai. Available: www.ptac.gov.lv).

Thus, the Applicant's right, acquired on the basis of a licence, to engage in a certain type of commercial activity falls within the scope of Article 105 of the *Satversme*.

17.2. The Constitutional Court has recognised that interference into commercial activities, conducted on the basis of a licence, cannot be deemed to be a restriction on the right to property. In such a case, the restriction should be manifested as such concrete negative impact that had occurred as the result of applying the contested norm (*compare, see, Judgement of 15 November 2016 by the Constitutional Court in Case No. 2015-25-01, Para 10.2.*).

Article 105 of the *Satversme* should be specified and applied in conjunction with Article 1 of the First Protocol to the European Convention for the Protection of Human Rights and Fundamental Freedoms (hereafter – the Convention) (*see, for example, Judgement of 26 April 2007 by the Constitutional Court in Case No. 2006-38-03, Para 10, and Judgement of 7 June 2012 in Case No. 2011-19-01, Para 9.1.*). Thus, with respect to the content of Article 105 of the *Satversme*, the Constitutional Court takes into account the case law of the European Court of Human Rights regarding application of Article 1 of the First Protocol to the Convention.

The European Court of Human Rights has noted that even if the licence issued to a person has not been revoked but the person's commercial activities are hindered in a way that, essentially, the licence issued to the person becomes meaningless, then Article 1 of the First Protocol to the Convention is applicable (*see Judgement of 7 June 2012 by the Grand Chamber of the European Court of Human Rights in Case "Centro Europa 7 S.R.L. and di Stefano v. Italy", Application No. 38433/09,Para 177–178, and Judgement of 8 November 2018 in Case "O'Sullivan McCarthy Mussel Development Ltd v. Ireland", Application No. 44460/16, Para 88*). Moreover, in establishing whether, in the particular case, the right to property has been restricted, the principle of legitimate expectations could be relevant (*see, for example, Judgement of 20 November 1995 by the European Court of Human Rights in Case "Pressos Compania Naviera S.A. and Others v. Belgium", Application No. 17849/91, Para 31*).

Hence, to ascertain the existence of a restriction, the Constitutional Court must, first and foremost, establish, whether the contested norm hinders the Applicant in engaging in commercial activities on the basis of a licence. Following that, the Constitutional Court, in reviewing the proportionality of the restriction,

must establish whether the restriction included in the contested norm hindered the commercial activities of the creditors in such a way that, essentially, rendered the licences issued to them meaningless.

17.3. Pursuant to Para 9 of Section 1 of the Consumer Rights Protection Law, the total costs of the credit to a consumer are all costs, including interest, commission, fees and other payments, which must be paid by the consumer in relation to the credit agreement and which are known to the creditor (except costs of a sworn notary). Thus, the total costs of the credit are all those payments, which the creditor may demand from a consumer in relation to a credit agreement.

Until 1 January 2016 when the law of 28 May 2015 "Amendments to the Consumer Rights Protection Law" entered into force, restriction on the total costs of the credit for a consumer had not been established. By these amendments, the legislator envisaged that such total cost of the credit to a consumer were considered as disproportional and incompatible with fair transaction practices which exceeded 0.55 per cent of the credit amount per day from the first to the seventh day (including) of using the credit, 0.25 per cent of the credit amount per day from the eight to the fourteenth day (including) of using the credit, and 0.2. per cent of the credit amount per day starting with the fifteenth day of using the credit. Whereas in agreements, pursuant to which credit had to be repaid on demand or the term of using the credit exceeds 30 days, such total costs of the credit to a consumer had to be considered as incompatible, which exceeded 0.25 per cent of the credit amount per day. In planning their commercial activities in the area of crediting, the Applicants had taken into consideration that, in determining the total costs of the credit for a consumer, they had to apply the said restrictions.

By the contested norm, the legislator has envisaged a uniform restriction on the total costs of the credit for a consumer irrespectively of the term of the credit agreement, providing that such total costs of the credit for a consumer that exceed 0.07 per cent of the amount of credit per day are to be considered as being disproportional and incompatible with fair transaction practice. Thus, compared to the previous valid regulation, the legislator has decreased the maximum admissible amount of those payments that the creditor may demand from the consumer in relation to the credit agreement.

The Applicants note that the admissible total costs of the credit for a consumer had been significantly decreased by the contested norm and, thus, the Applicants' ability to continue providing crediting services to consumers on the basis of a licence are jeopardised. Namely, the Applicants' income, gained from

consumers in connections with credit agreements, no longer would be able to cover the costs incurred by the creditor in connection with issuing of the credit.

The Applicants have noted that, by decreasing the admissible total costs of the credit for a consumer, their commercial activity, which they engage in on the basis of a licence, is being hindered. The Constitutional Court concludes that the contested norm restricts the Applicants' right to engage in commercial activities on the basis of a licence, since it sets out more disadvantageous conditions for the creditor than before, which the Applicants' from now on have to take into account in planning their commercial activities in the area of consumer credit.

Thus, the contested norm restricts the Applicants' rights, envisaged in the first, second and third sentence of Article 105 of the *Satversme*.

18. In ascertaining, whether the restriction on the right to property is justifiable, the Constitutional Court must examine:

1) whether the restriction on fundamental rights has been established by law;

2) whether the restriction has a legitimate aim;

3) whether the restriction is proportional to its legitimate aim (*see, for example, Judgement of 8 June 2007 by the Constitutional Court in Case No. 2007-01-01, Para 22*).

19. To assess, whether the restriction on fundamental rights had been established by a law adopted in due procedure, it must be verified:

1) whether the procedure, set out in regulatory enactments, had been abided by in adopting the law;

2) whether the law has been promulgated and is accessible in compliance with the requirements set out in regulatory enactments;

3) whether the law has been worded with sufficient clarity, allowing a person to understand the content of the rights and obligations following from it and to foresee the consequences of its application (*see, for example, Judgement of 8 April 2015 by the Constitutional Court in Case No. 2014-34-01, Para 14*).

The wording of the contested norm was included in the draft law, submitted by eight Members of the 12th convocation of the *Saeima*, No. 1290/Lp12 "Amendments to the Consumer Rights Protection Law". In the course of examining it, the Economic, Agricultural, Environment and Regional Policy Committee of the *Saeima* (hereafter – Responsible Committee) decided to prepare its own alternative draft law No. 1305/Lp12 "Amendments to the Consumer Rights Protection Law" (hereafter – draft law No. 1305/Lp12) and the contested norm

also was included in it. The *Saeima* reviewed draft law No. 1305/Lp12 in three readings. The restriction on fundamental rights, included in the contested norm, has been established by the law "Amendments to the Consumer Rights Protection Law", adopted by the *Saeima* on 4 October 2018 and promulgated on 16 October 2018 in the official journal "Latvijas Vēstnesis", No. 2018/204.6.

19.1. The Applicants are of the opinion that, perhaps, the procedure for adopting the contested norm complied with the formal requirements, set out in regulatory enactments; however, it is contended that the legislator did not comply with the principle of good legislation. Namely, prior to adopting the contested norm, the legislator did not have at its disposal adequate analysis and justification regarding the selected interest rate, as well as its impact on market operators and consumers. Likewise, it is alleged that, in the course of adopting the contested norm, the opinion of some other representatives of the sector regarding its possible incompatibility with Article 105 of the *Satversme* had not been taken into account, also, possible alternatives had not been examined. The annotation to draft law No. 1305/Lp12 is said to be incompatible with Article 85 of the Rules of Procedure of the *Saeima*. Namely, it does not include substantiation of the need for this law and how it could impact the development of society and economy, the state budget and the system of legal norms that is in force. The quality of the contested norm has been influenced also by the haste, in which it had been adopted. Moreover, the legislator had not considered, whether the amendments to the Consumer Rights Protection Law, which included the contested norm, were to be notified to the European Commission in accordance with legal acts of the European Union.

19.1.1. The Constitutional Court has recognised that the legislative process not only should comply with the formal requirements set out in regulatory enactments but also should facilitate persons' trust in the State and law (*see Judgement of 12 April 2018 by the Constitutional Court in Case No. 2017-17-01, Para 21.3.*).

Pursuant to the principle of good legislation, the legislator must review the compliance of the legal norms envisaged in the draft law with legal norms of higher legal force, *inter alia*, the *Satversme*, provisions of international and European Union law, and must align the legal norms included in the draft law with the already existing legal norms in accordance with the principle of rational legislator. Likewise, the envisaged legal regulation must be duly justified by explanatory research, if necessary. The legislator also must consider the risk estimates made by sectoral experts and introduce measures timely prevention of these risks (*see*

Judgement of 6 March 2019 by the Constitutional Court in Case No. 2018-11-01 , Para 18.1,).

It follows from materials in the case that representatives of ministries, the Legal Bureau of the *Saeima*, as well as representatives of the sector had participated in the sittings of the Responsible Committee where the contested norms were discussed. The minutes and audio recordings of the Responsible Committee's sittings show that, in the course of adopting the contested norm, also the objections and proposals made by representatives of the sector were repeatedly heard. Namely, the Ministry of Economics, the Chamber of Commerce and Industry, the Association of Commercial Banks, the Competition Council, the Consumer Rights Protection Centre, association "Latvian Alternative Financial Services Association" and other institutions expressed their opinion regarding the intended regulation at the Responsible Committee's sittings. Likewise, the Members of the *Saeima*, who had submitted proposals regarding the wording of the contested norm, expressed their opinion (*see Case Materials, Vol. 1, pp. 94–158; Vol. 2, pp. 1–154; Vol. 3, pp. 1–21*).

The draft law was discussed also by the Working Group, the report "Proposals regarding Improving Normative Regulation in the Area of Consumer Credit", prepared by it, was submitted to the Responsible Committee. It includes, *inter alia*, analysis of the regulation in other countries aimed at decreasing the total costs of the credit for a consumer and the conclusion that, prior to the adoption of the contested norm, the total costs of the credit for a consumer in Latvia were the highest in the Baltics and that decreasing of its maximum rate was justified. The criteria that should be taken into account, in determining the respective restrictions, were indicated in the report, likewise, the risks that could be caused by excessive decreasing of the rate were pointed out to the legislator (*see, Case Materials, Vol. 2, pp. 115–127*).

Thus, the Constitutional Court ascertained that the legislator had ensured participation of stakeholders and that opinions were heard in the course of examining draft law No. 1305/Lp12. The fact that the legislator has not taken into account all objections that were made and proposals that were submitted cannot be the grounds for recognising that the principle of good legislation had not been complied with (*see, for example, Judgement of 25 March 2015 by the Constitutional Court in Case No. 2014-11-0103, Para 18.1.*). The Constitutional Court underscored that the principle of good legislation does not guarantee a particular outcome, desirable for one person or a group of persons; however, compliance with it provides assurance that the particular issue has been

democratically discussed; i.e., various opinions have been expressed and analysed, and, in the case where various rights and lawful interests collide, the balance has been sought by respecting the values included in the *Satversme* and the general legal principles (*compare, see Judgement of 23 April 2019 by the Constitutional Court in Case No. 2018-12-01, Para 24.1.*). Thus, as regards the participation of stakeholders and hearing of opinions in the course of adopting draft law No. 1305/Lp12, the principle of good legislation has not been violated.

The Constitutional Court has recognised that extensive feasibility studies in the course of drafting and adopting a legal norm, *inter alia*, seeking advice of scholars and experts of the sector, could have a positive impact on the quality of the legal norm (*see Judgement of 12 May 2016 by the Constitutional Court in Case No. 2015-14-0103, Para 21*). Examining the substantiation of the necessity to adopt the contested norm, the Constitutional Court concludes: the process of drafting the contested norm in general proves that the legislator had become aware of the particular situation in the area of consumer credit and the practice in other countries, as well as examined various possibilities for decreasing the total costs of the credit for a consumer. Hence, in this respect, the principle of good legislation had been complied with.

19.1.2. The annotation to draft law No. 1305/Lp12 indicates why the law is necessary, what impact the law might have on the development of society and economy, the state budget and the valid system of legal norms, which international commitments of Latvia the draft law complies with, what consultations have been held in preparing it and how enforcement of the law will be ensured (*see Annotation to Draft Law No. 1305/Lp12*).

Annotation to a draft law is one of the sources providing information regarding the need for the legal act, its application and impact on various areas. It is of informative significance, i.e., it reveals the motivation of the party submitting the draft law. The substantiation included in the annotation allows society to gain an impression of the considerations that had been the grounds for adopting the legal norm and helps to convince society that, in the course of adopting legal norms, the need to restrict fundamental rights, guaranteed in the *Satversme*, had been carefully weighed. The Applicants' considerations regarding the annotation's incompatibility with the requirements set in the Rules of Procedure of the *Saeima* are linked to, in their opinion, insufficient substantiation of the need to adopt the contested norm. However, the amount of detail of the substantiation included in the annotation *per se* cannot be a criterion for identifying a violation of the principle of good governance.

19.1.3. After the case was transferred for review, the limited liability company "ONDO" has submitted to the Constitutional Court its opinion, noting additionally that the legislator had not considered whether the respective draft law, which included the contested norm, should have been notified to the European Commission, pursuant to the requirements of the Directive 2015/1535 of the European Parliament and of the Council of 9 September 2015 laying down a procedure for the provision of information in the field of technical regulations and of rules on Information Society services (hereafter – the Directive).

The Directive imposes upon public institutions an obligation to inform the European Commission about adopting any draft technical regulations on products and Information Society services before these regulations are included in the national legal acts. The aim of the Directive is to ensure that Member States are informed of the technical regulations envisaged by any other Member State (*see the sixth recital of the Directive*).

Pursuant to sub-para "b" of Article 1 of the Directive, the Directive is applied only to such services, which are normally provided for remuneration, at a distance, by electronic means and at the individual request of a recipient of services. Whereas "technical regulations", in the meaning of the Directive, are rules on services, including the relevant administrative provisions, the observance of which is compulsory, *de jure* or *de facto*, in the case of marketing, provision of a service, establishment of a service operator or use in a Member State or a major part thereof, as well laws, regulations or administrative provisions of Member States, except those provided for in Article 7, prohibiting the manufacture, importing, marketing or use of a product or prohibiting the provision or use of a service, or establishment as a service provider. It follows from the Directive that a Member State has the duty to inform the European Commission if the particular regulation, in accordance with the criteria included in the Directive, is to be recognised as being "draft technical regulation".

Latvia, like Finland, Lithuania and Estonia, in adopting regulation similar to the contested norm, establishing by it restrictions on the costs of a consumer crediting agreement, has not informed the European Commission about it (*see: Eiropas Savienības dalībvalstu paziņoto tehnisko noteikumu informācijas sistēmas datu bāze, Available: ec.europa.eu*). Para 4 of Article 1 of the Directive provides that it does not apply to rules relating to matters which are covered by the Union legislation in the field of financial services, as listed in Annex II to this Directive; moreover, it is noted that this lost is non-exhaustive. These are, for example, investment services, insurance and reinsurance operations, banking services,

operations relating to pension funds, services relating to dealings in futures or options. It is noted in the Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market that credit also is a financial service (*see 18th recital of this Directive*).

19.1.4. Participants in the case have not objected to the procedure, in which the contested norm was promulgated, and neither does the Constitutional Court doubt that the contested norm has been promulgated in the procedure set out in the *Satversme* and the Rules of Procedure of the *Saeima* and is accessible in accordance with the requirements defined in regulatory enactments.

19.2. Ltd. "ExpressCredit" notes that the wording of the contested norm is not sufficiently clear because a methodology for calculating the total costs of the credit per day has not been defined. The legislator has not taken into account that there are several types of credit repayment. These influence the calculation of the total costs of the credit per day. It is alleged that it is impossible to calculate correctly the total costs of the credit per day for credits with the annuity method of repayment. The Consumer Rights Protection Centre also has drawn the Constitutional Court's attention to the fact that the way, in which the total costs of the credit per day should be calculated, has not been defined in regulatory enactments. To calculate these, the total costs of the credit, which are calculated and indicated in agreements for the whole term of crediting, should be divided by the number of days included in the crediting term. However, this leads to a situation, where the maximum admissible annual interest rate is lower for those credits, which are issued for a shorter term, than for those issued for a longer term (*see Case Materials, Vol. 3, p. 81–85*).

The Constitutional Court has already recognised that the legal norms adopted by the legislator should be predictable and clear, as well as sufficiently stable to allow a person not only to make short-term decisions but also make one's long-term future plans (*see, for example, Judgement of 25 October 2004 by the Constitutional Court in Case No. 2004-03-01, Para 9.2.*). The Constitutional Court has recognised the predictability of the consequences of a legal norm as an essential criterion that proves that it has been worded clearly; i.e., the norm should be worded in a way that would allow a person to predict clearly the scope and meaning of its application. Another aspect that should be taken into account in assessing, whether the legal norm is sufficiently clear, is how much effort and time of the legal norm's addressee is required to become aware of their rights and obligations that follow from the new regulation (*see, for example, Judgement of*

30 March 2011 by the Constitutional Court in Case No. 2010-60-01, Para 15.2., and Judgement of 19 October 2017 in Case No. 2016-14-01, Para 25.3.).

19.2.1. The Consumer Right s Protection Law provides explanation of what, in the meaning of this Law, is to be considered a consumer credit agreement and which persons are allowed to provide crediting services to consumers, likewise, the purpose and scope of application of this Law are indicated. Para 9 of Section 1 of this Law defines exactly which costs constitute the total costs of the credit for a consumer. The legislator's aim to restrict the total costs of the credit for the consumer to 0.007 per cent of the amount of credit per day clearly follows from the contested norm. This applies to all consumer crediting agreements, except those upon the conclusion of which an item is to be deposited as security in the creditor's safe-keeping and according to which the liability of the consumer is limited only to that pledged item.

The Constitutional Court has recognised that the *Saeima*, in exercising its right to legislate, enjoys discretion, insofar the general legal principles and other provisions of the *Satversme* are not violated (*compare, see Judgement of 19 October 2017 by the Constitutional Court in Case No. 2016-14-01, Para 25.2.*). This applies also to issues related to legislative technique (*compare, see Judgement of 19 June 2010 by the Constitutional Court in Case No. 2010-02-01, Para 9.4.2., and Judgement of 20 May 2011 in Case No. 2010-70-01, Para 16.1.*). Since a legal norm, as to its juridical nature, is an abstract prescript on conduct, it does not follow from the quality requirements set for a legal norm in the *Satversme* that each legal norm should be worded as an absolutely precise instruction. The legislator has the right to formulate legal norms with various levels of detail, creating both general and special regulation.

The legislator has included in the contested norm a general principle, which must be complied with in determining the total costs of the credit for a consumer and which is clear in typical cases. The fact that, in some cases, when in connection with the type of credit repayment additional actions must be taken in calculating the total costs of the credit per day, *per se* does not mean that the contested norm would be unclear.

19.2.2. It clearly follows from the contested norm that the total costs of the credit for a consumer may not exceed 0.07 per cent of the amount of credit per day. Whether the total costs of the credit for a consumer comply with this maximum admissible amount should be verified in each particular case, primarily, by the creditor. The association "The Alternative Financial Services Association of

Latvia" notes that the contested norm and nuances of its application are sufficiently clear for professionals of the sector (*see Case Materials Vol. 3, p. 93*).

A person might need knowledge in the field of finance to apply the contested norm correctly and calculate the maximum admissible total costs of the credit for a consumer per day. However, a legal norm may be sufficiently clear and predictable even if a person needs appropriate assistance to understand the scope of this norm (*see Judgement of 21 February 2019 by the Constitutional Court in Case No. 2018-10-0103, Para 18.1.*). Thus, if a person is unable to clarify the content of the regulation included in the contested norm, they may clarify it with the assistance of experts of the respective field and lawyers. Moreover, pursuant to Para 20 and Para 21 of the Cabinet Regulation of 25 October 2016 No. 691 "Regulations Regarding Consumer Credit", the area of consumer credit as such envisages the creditor's obligation to explain to a consumer, in an understandable and simple way, the nature of the service offered so that they would be able to make decision on entering into an agreement on the basis of true and complete information.

19.2.3. The Constitutional Court concludes that the contested norm has been worded with sufficient clarity to allow a person to understand the content of the rights and obligations following from it and predict the consequences of its application. Whereas the fact that, in applying the contested norm to credits that have been issued for a longer term, the maximum admissible annual interest rate is higher than the one for short-terms credits, *per se* does not mean that the contested norm is unclear. This circumstance should be taken into account in examining, whether the restriction on fundamental rights included in the contested norm substantially complies with the *Satversme*.

In view of the above, the Constitutional Court concludes that the contested norm had been adopted in compliance with the procedure set out in regulatory enactments and that the process of its adoption complies also with the principle of good legislation.

Thus, the restriction on fundamental rights that follows from the contested norm has been established by law.

20. Every restriction on fundamental rights should be based on circumstances and arguments that necessitate it, i.e., the restriction is established for important interests – a legitimate aim (*see, for example, Judgement of 22 December 2005 by the Constitutional Court in Case No. 2005-19-01, Para 9*).

If a restriction on rights has been established then, in legal proceedings before the Constitutional Court, the institution, which issued the contested act, has been imposed the obligation to present and substantiate the legitimate aim of this restriction, in the present case it is the *Saeima* (*see, for example, Judgement of 1 November 2012 by the Constitutional Court in Case No. 2012-06-01, Para 12, and Judgement of 11 December 2014 in Case No. 2014-05-01, Para 18*).

The *Saeima* notes that the aim of the restriction, included in the contested norm, is to prevent the practice where the costs of a loan for a consumer, in particular, for a socially more vulnerable person who experiences financial difficulties, the costs of the issued credit are so disproportionally high that could be regarded as being incompatible with fair transaction practice or even equalled to usury. Moreover, the contested norm indirectly promotes responsible borrowing by decreasing the possibilities for a person to assume hastily and without due consideration debt commitments, which these persons, actually, cannot afford. Thus, the legitimate aim of the restriction on fundamental rights is protection of the rights of other persons, i.e., consumers, set out in Article 116 of the *Satversme*.

20.1. It follows from the annotation to draft law No. 1305/Lp12 that the contested norm had been adopted because various measures, introduced before, aimed at decreasing the total costs of the credit for a consumer, had not been sufficiently effective. Namely, according to the data provided by the Consumer Rights Protection Centre in 2017, in some areas of crediting (distance credits, mortgages) the amount of late credit repayments continues to be high (above 20 per cent of the credit portfolio) and the number of extended distance credits increases every year (in 2016 – 61 per cent but in 2017 – 64 per cent). The aim of the draft law is to ensure proportional total costs of the credit for a consumer (*see annotation to draft law No. 1305/Lp12*).

In examining draft law No. 1290/Lp12 "Amendments to the Consumer Rights Protection Law", which later was included in draft law No. 1305/Lp12, at the sitting of the Responsible Committee on 19 June 2018, D. Brūklītis, the representative of the Ministry of Economics, characterising the situation in the consumer credit market, admitted that the number of credits issued in the area of non-bank credit had increased every year, distance credits continued to have the largest amount of late repayments; moreover, the general trend to extend the term for repayment was very pronounced; i.e., borrowing without assessing the possibility of repaying in time (*see audio recording of the sitting of the Economic, Agricultural, Environmental and Regional Policy Committee on 19 June 2018, Case Materials, Vol. 5*). Likewise, the Consumer Rights Protection Centre, in its

report of 2019 on the operations of the non-banking consumer credit market in 2018, notes that until 31 December 2018, the credit repayment terms had been extended three and more times for 45 per cent of distance credits (*see: Patērētāju tiesību aizsardzības centrs. Pārskats par nebanku patērētāju kreditēšanas tirgus darbību 2018. gadā, 2019, 22. lp.*). The Organisation for Economic Co-operation and Development notes in its report of 2019 on short-term consumer credits that, in Latvia, only 65 per cent of all short-term loans are repaid on time (*see: OECD (2019). Short-term consumer credit: provision, regulatory coverage The Organisation for and policy responses, p. 27*).

These data prove that, within the framework of legal regulation that was in force before the contested norm was adopted, numerous consumers had difficulties in repaying the issued credit within the set term.

20.2. Section 2 of the Consumer Rights Protection Law defines the purpose of this Law – to ensure that consumers are able to exercise and protect their lawful rights, as well as to protect the collective interests of consumers.

The Constitutional Court has already recognised that a consumer is the subject of special legal relations and enjoys special protection. A creditor, in turn, is such a participant of legal relations who, in financial terms, is incomparably more powerful than the consumer. A restriction of a creditor's fiscal interests with the aim to protect the rights and interests of a consumer as a weaker market player complies with the nature and purpose of consumer rights protection (*see Judgement of 8 April 2011 by the Constitutional Court in Case No. 2010-49-03, Para 12.3.*).

The importance of consumer rights protection has been recognised also in the European Union law. Article 38 of the Charter of Fundamental Rights of the European Union provides that Union policies must ensure a high level of consumer protection. As noted by summoned person Z. Dāvida, such special protection has been established only in the areas of consumer rights and environmental law. This is said to related to the sensitive nature, public significance and insufficient protection in the conditions of free market regulation in these areas. Moreover, in the present day contemporary "credit society", the importance of consumer rights protection continues to increase, in particular, of consumers with low income (*see Case Materials, Vol. 5, pp. 36–37*). It is noted also in legal literature that in circumstances of abundance of various goods and services, the need to ensure consumer rights protection has increased. Likewise, some consumer groups are foregrounded who due to economic, social and other circumstances might require

special protection (*see: Benöhr I. EU Consumer Law and Human Rights. Oxford: Oxford University, 2013, p. 78*).

20.3. Short-term credits, if appropriately regulated and used by knowledgeable and informed consumers, may satisfy certain consumer needs effectively. However, short-term credits, consumer credits with particularly high costs, due to their specificity, may cause additional risks for a consumer, *inter alia*, lead them into a cycle of repeated loans and higher costs compared to choosing another financial product. These risks, in particular, affect consumers with low or irregular income and also with low financial literacy, young or, quite on the contrary, people (*see: OECD (2019). Short-term consumer credit: provision, regulatory coverage and policy responses, pp. 6, 26–27, 30*).

The results of a survey of inhabitants, organised by the Consumer Rights Protection Centre, reveal that people with low income take loans from non-banking creditors most frequently (*see: Patērētāju tiesību aizsardzības centrs. Latvijas iedzīvotāju viedoklis par finanšu uzkrājumiem, kā arī banku un nebanku kredītu devējiem, 2019, 12. lp.*). Pursuant to the study conducted by the University of Latvia, 39 per cent of respondents had difficulties in repaying the issued loan but 25 per cent had experienced such difficulties repeatedly. The most typical way of solving such problems is extending the term for repaying the credit, moreover, often it is done sever time (*see: Ansonska E., Austers I., Bērziņš G., Priede J. The Use of Distance Payday Loans in Latvia. Psychological Aspects of Consumer Behaviour. Riga: University of Latvia, 2017, pp. 39, 41–42*). Whereas the Finance and Capital Market Commission has concluded in a study conducted in 2018: although the financial literacy of Latvia's inhabitants has increased, nevertheless, for part of inhabitants, the credit burden has become even greater than before, and expensive short-term solutions are used in situations like these (*see: Finanšu pratības indekss. Available: www.klientuskola.lv*).

The aim of the restriction on fundamental rights, included in the contested norm, is, taking into account the existing economic situation in the state, protection of consumer rights by defining what total costs of the credit should be considered as being disproportional and incompatible with fair transaction practice. This regulation is aimed at ensuring that the costs of a loan issued by a creditor are such that a consumer, in particular, a person with low income, would be able to repay the loan. Hence, the restriction included in the contested norm, is one of the measures to be used for the protection of other persons', i.e., consumers', rights and lawful interests. Stability, welfare and financial sustainability of Latvian

households are important for the entire national economy. Hence, the restriction also serves the aim of protecting public welfare.

Hence, the legitimate aims of the restriction on fundamental rights, included in the contested norm, are as follows – protection the right of other persons and protection of public welfare.

21. Upon identifying the legitimate aim of the restriction on fundamental rights, compliance of this restriction with the principle of proportionality must be examined and, thus, it must be ascertained:

1) whether the measures used by the legislator are suitable for reaching the legitimate aim; i.e., whether it is possible to reach the legitimate aim of the restriction by the contested norm;

2) whether such action is necessary; i.e., whether the aim cannot be reached by other measures, less restrictive on a person's rights;

3) whether the legislator's actions are appropriate; i.e., whether the benefit gained by society outweighs the damage inflicted upon a person's rights.

If it is recognised that the restriction, established by the legal norm, is incompatible with even one of these criteria then the restriction is incompatible with the proportionality criterion and is unlawful (*see, for example, Judgement of 6 June 2018 by the Constitutional Court in Case No. 2017-21-01, Para 17*).

22. In examining, whether the selected measures are suitable for reaching the legitimate aims, the Constitutional Court verifies, whether the legitimate aims can be reached by the selected measures. Thus, the Constitutional Court must ascertain, whether the contested norm, i.e., decreasing of the admissible total costs of the credit for a consumer per day, allows protecting consumer rights and welfare of entire society.

The restriction on fundamental rights, included in the contested norms, ensures that the total costs of the credit for a consumer will not exceed 0.007 per cent of the amount of credit per day. The Constitutional Court holds that limiting the total costs of the credit is one of the ways, in which a consumer may be protected against disproportionally high payments for credit.

The Applicants note that the contested norm is only seemingly suitable for reaching the legitimate aims of the restriction on fundamental rights. Application of this norm is said to lead to a situation where the maximum admissible annual interest rate of credits issued for a longer term is higher than the one for short-term credits. As the result of applying the contested norm, loans with short terms of

repayment would no longer be accessible to consumers because issuing of such credits would no longer be economically profitable for creditors. Hence, a person would be forced to borrow larger amounts of credit for a longer period and, thus, the costs relating to concluding a crediting agreement will, accordingly, increase for a consumer, likewise, illegal crediting will increase. Also the summoned person, association "The Alternative Financial Services Association of Latvia", referring to numerous studies, points out that inaccessibility of short-term credits could inflict greater damage upon a creditor compared to their accessibility (*see Case Materials, Vol. 3, pp. 88–92*).

The *Saeima*, in turn, notes in its written reply that satisfying daily needs by short-term loans may lead to the cycle of repeated loans, which, in the long term, only increases a person's debt commitments and has a negative impact upon a person, their mental and physical health. Therefore, the fact that the application of the contested norm might result in diminished offer of short-term credits complies with consumers' interests. Influencing consumer behaviour by decreasing accessibility of a certain product or service in the market is said to be a suitable measure for consumer rights protection. The summoned persons – the Bank of Latvia and J. Grasis – do not foresee that the contested norm could significantly worsen the accessibility of credit resources within economy and have a negative impact on consumers (*see Case Materials, Vol.*3*, pp. 40–41, and Vol. 5, p. 65*).

Association "The Alternative Financial Services Association of Latvia" has pointed to several studies, which, in its opinion and judging by the experience of other countries, provides evidence of the negative impact by the contested norm on a consumer. I.e., as the result of applying the contested norm, with the decreasing offer of short-term loans in the market, a consumer would be forced to borrow larger amounts for a longer period and, thus, the costs related to taking out a loan would only increase; moreover, illegal crediting might increase (*see, Case Materials, Vol. 3, pp. 88–92*). However, as noted in the study by the Organisation of Economic Co-operation and Development, if the accessibility of short-term credits is limited, consumers, possibly, instead of choosing other types of loans with longer terms of repayment, borrow, for example, form their friends or family members. Moreover, no proof was found in this study that consumers, in case a short-term loan is not accessible, turn to illegal lenders (*see: OECD (2019). Short-term consumer credit: provision, regulatory coverage and policy responses, pp. 38–39*).

Special regulation has not been set in the legal acts of the European Union regarding the need to limit the total costs of the credit for a consumer. Likewise,

the summoned persons Z. Dāvida and V. Mantrovs point out that this matter is not harmonised in the European Union, and each Member State, depending on its special circumstances, regulates it differently (*see, Case Materials, Vol. 5, pp. 36, 68–69*). The Constitutional Court notes that, in the current social and economic situation of the State of Latvia, the restriction included in the contested regulation is one of the measures that might ensure that a consumer is protected against high payments for the credit and, thus, promote the stability, welfare and financial sustainability of a household. Thus, the contested norm is a suitable measure for protecting consumer rights and also for promoting welfare of the entire society.

Hence, the measures chosen by the legislator is suitable for reaching the legitimate aims.

23. In examining, whether the chosen measures are necessary for reaching the legitimate aims, the Constitutional Court verifies, whether the legitimate aims cannot be reached by other measures, less restrictive upon an individual's rights and equally effective.

The Constitutional Court already has recognised that a more lenient measure cannot be any other measure but only such that allows reaching the legitimate aim at least in the same quality (*see, for example, Judgement of 7 October 2010 by the Constitutional Court in Case No. 2010-01-01, Para 14*). The Court has the jurisdiction to verify, whether alternative measures, which would restrict persons' fundamental rights to a lesser extent, exist (*see, for example, Judgement of 24 November 2017 by the Constitutional Court in Case No. 2017-07-01, Para 19*).

23.1. The Applicants note that such regulation that would ensure appropriate assessment of consumers' creditworthiness before entering into an agreement, would be an alternative measure. Moreover, a system for supervising operations of providers of crediting services already has been set up and exists, it is maintained by the Consumer Rights Protection Centre.

The *Saeima*, however, points out that it is impossible to reach the legitimate aim of the restriction on fundamental rights in the same quality by the measure indicated by the Applicants. The creditors' obligation to assess the creditworthiness of a consumer has been established in legal acts already now; however, this measure has not ensured sufficiently effective protection of consumer rights.

The creditor's obligation to assess the creditworthiness of the consumer before the conclusion of the credit agreement is included in Article 8 of the Directive 2008/48/EC of the European Parliament and of the Council of

23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC. Latvia has included the requirements set out in this Directive in the Consumer Rights Protection Law, envisaging in several of its norms the creditor's obligation to assess the consumer's ability to repay the credit before the conclusion of the consumer credit agreement (*see Parts 4^1, 4^2, 4^7 of Section 8 and Para 2 of Section 8 (5) of the Consumer Rights Protection Law*). The aim of this assessment is to ensure that only such credit agreements are concluded with a consumer, where the commitments envisaged therein, most probably, would be met by the consumer. However, the results of inspections, conducted by the Consumer Rights Protection Centre, show that a consumer's ability to repay credit is not always duly assessed. Namely, in conducting supervisory activities in 2017 and 2018, to verify how creditors ensure that consumers' solvency is assessed before the decision on issuing credit is made, it was found that in 55 cases of 152, a consumer was issued credit, which they, most probably, would not be able to repay from their income (*see: Patērētāju tiesību aizsardzības centra veiktajā finanšu pakalpojumu uzraudzības projektā konstatētais. Available: http://www.ptac.gov.lv*). 16 creditors, whose credit portfolio had the largest share of late repayments, were inspected, and it was proven that the due assessment of a consumer's creditworthiness was not always properly conducted. This was admitted also by D. Brūklītis, the representative of the Ministry of Economics, at the sitting of the Responsible Committee on 19 June 2018 (*see audio recording of the Economic, Agricultural, Environmental and Regional Policy Committee on 19 June 2018, Case Materials, Vol. 5*).

The considerations, mentioned in the applications, regarding the need to improve the process of assessing consumers' creditworthiness are linked to possibilities of improving the application of valid normative regulation. However, the Constitutional Court has recognised that the possible improvements in applying legal norms cannot be assessed as an alternative measure for reaching the legitimate aim (*see Judgement of 21 December 2015 by the Constitutional Court in Case No. 2015-03-01, Para 27.1.*).

23.2. In Applicants opinion, recognising such restriction on the interest rate for the total costs of the credit per day, which would ensure consumer rights protection but restrict the Applicants' right to engage in commercial activities to a lesser extent, could be another alternative measure. At the sitting of the Responsible Committee, the Bank of Latvia had offered a solution that would restrict the Applicants' rights to a lesser extent; the legislator; however, had dismissed it without justification. The legal regulation that had been in force before

the contested norm or such that would set the restriction on the annual interest rate as 60 per cent of the credit amount could be an alternative. Likewise, it could be provided that the total costs of the credit for a consumer may not exceed 0.1 per cent of the amount of credit per day.

The Rules of Procedure of the *Saeima* entrusts a considerable part of preparatory work in elaborating a draft law, prior to reviewing it at the *Saeima*'s sittings, to the Committees of the *Saeima*, and the Responsible Committee ensures that the draft law is fully prepared for reviewing at the *Saeima*'s sitting (*see Judgement of 19 December 2010 by the Constitutional Court in Case No. 2011-03-01, Para 18*).

It follows from materials in the case that alternative wordings of the contested norm had been discussed at the sittings of the Responsible Committee on 18 and 25 September 2018. It follows from the minutes and audio recordings of these sittings that deputies had submitted several proposals to define another interest rate for the total costs of the credit per day. Likewise, on the basis of the solution offered by the Bank of Latvia and the Working Group, the Responsible Committee had prepared a proposal to set out that such total costs of the credit for a consumer, which, expressed as annual interest rate, at the moment of concluding consumer credit agreement, would exceed more than three times the annual weighed interest rate of six months for consumer credits in EURO for residents' households, as being incompatible. As had been noted by the representative of the Bank of Latvia at the sitting of the Responsible Committee, a similar formula had been used to set restrictions on the total costs of the credit for a consumer also in Estonia. Pursuant to this calculation, the total costs of the credit for a consumer could not exceed approximately 0.13 per cent of the amount of credit per day. Although this proposal was supported at the sitting of the Responsible Committee, the *Saeima* dismissed it at its sitting of 4 October 2018. Likewise, the arguments by the Consumer Rights Protection Centre regarding the need to establish restrictions not by using total costs of the credit but the annual interest rate were heard at the sitting of the Responsible Committee on 18 September 2018 (*see audio recording of the Economic, Agricultural, Environmental and Regional Policy Committee on 19 June 2018, Case Materials, Vol. 3).*

The legislator has assessed whether, in the particular case, alternative measures exist that would infringe upon the creditor's fundamental rights, enshrined in the *Satversme*, to a lesser extent, and, following this assessment, has chosen the solution that also in the future the restriction must be defined not by using the annual interest rate but the total costs of the credit for a consumer per

day. Moreover, the legislator has concluded that, in view of the current situation in the area of consumer credit and the need to protect consumer rights and lawful interests, as well as public welfare, the total costs of the credit for a consumer should be limited to 0.007 per cent of the amount of credit per day and that there are no alternative measures. The Constitutional Court points out that the legislator, in choosing one of the potentially suitable measures for reaching the legitimate aim, has the right to assess and to decide. If the legislator, by exercising its discretion, has decided that the most suitable solution would be imposing restrictions on the total costs of the credit for a consumer, then another, alternative interest rate cannot be recognised as being a more lenient measure, unless the measure chosen by the legislator is contrary to the general legal principles and other norms of the *Satversme*.

Thus, there are no other, more lenient measures allowing to reach the legitimate aim of the restriction on fundamental rights at least in the same quality.

24. In assessing the compliance of the restriction on fundamental rights with the legitimate aim, it must be verified whether the adverse consequences caused to a person by restricting their fundamental rights do not outweigh the benefit that society in general gains from this restriction. Namely, the interests that need to be balanced in the case need to be identified, as well as which of these interests and rights should be given priority (*see Judgement of 7 October 2010 by the Constitutional Court in Case No. 2010-01-01, Para 15*).

In the present case, the legislator's task, in envisaging more adverse conditions for creditors that they will have to take into account in the future, in planning their commercial activities in the area of consumer credit, is to balance a person's right to engage in commercial activities in the area of one's choice with the restriction on rights and lawful interests that comply with the legitimate aims of the restriction on fundamental rights, *inter alia*, the need to ensure consumer rights protection.

Hence, the Constitutional Court must verify, whether a fair balance between these various rights and lawful interests has been achieved by the contested norm.

24.1. The Constitutional Court has repeatedly noted that the legislator has the duty to consider periodically, whether the particular legal regulation continues to be effective, suitable and necessary, as well as the possible ways to improve it (*see, for example, Judgement of 11 November 2005 by the Constitutional Court in Case*

No. 2005-08-01, Para 9.5., and Judgement of 2 June 2008 in Case No. 2007-22-01, Para 18.3.).

The Constitutional Court already has concluded that the legal regulation in force before the contested norm entered into effect permitted a situation, in which numerous consumers had difficulties in repaying the loan within the set term. Therefore, the legislator was obliged to take measures that would ensure fair treatment of a consumer and would prevent situations where the creditor, by using their economic advantages, could gain disproportional financial benefit at the consumer's expense. Regulation that would allow that the creditor compensates the costs and risks related to the conclusion of a consumer credit agreement at the expense of the creditor –the economically week party of the agreement would be contrary to the substance and purpose of the Consumer Rights Protection Law. The State must ensure effective consumer rights protection. Consumer rights protection is a value of a democratic state governed by the rule of law, and it is important also from the vantage point of sustainable development of society.

24.2. As established above, the legislator, by decreasing the total costs of the credit for a consumer, has aspired to protect a consumer against high payments for credit. The Constitutional Court underscores that the principle of legitimate expectations allows and, in certain cases, even demands amending the existing legal regulation. Otherwise, the State would be unable to respond duly to the changing circumstances in life. In amending legal regulation, the legislator must take into account also the rights, with the respect to retaining and exercising of which legitimate expectations might have developed (*compare, see Judgement of 27 October 2010 by the Constitutional Court in Case No. 2010-12-03, Para 11*). The principle of legitimate expectations protects only such rights regarding the exercise of which a person could developed legitimate, justified and reasonable expectations (*see Judgement of 21 October 2016 by the Constitutional Court in Case No. 2016-03-01, Para 13*).

Creditors' right, obtained on the basis of a licence, to engage in commercial activities in the area of consumer crediting, falls within the scope of Article 105 of the *Satversme* (*see Para 17.1. of this Judgement*). However, this right should be separated from creditors' interest in gaining profit. Article 105 of the *Satversme* does not envisage legal protection for a person's right to gain profit because such abstract possibility cannot be regarded as the object of the right to property (*see Judgement of 3 November 2011 by the Constitutional Court in Case No. 2011-05-01, Para 15.2.*). Thus, the licence issued to a creditor for an unlimited term may create legitimate expectations in need of protection regarding the possibility to

continue commercial activities in the area of consumer credit. However, a merchant cannot develop legitimate expectations requiring protection that the legal regulation of the particular sector will not be amended in a way that could have negative impact on their economic activities, decreasing the possibilities to gain the intended amount of profit.

In the present case, it is essential, whether the legislator, in amending legal regulation, has established lenient transition to the new legal regulation. The Constitutional Court has recognised that the requirement, which follows from the principle of legitimate expectations, to ensure as lenient as possible transition to the new regulation is significant because a person, to whom the new regulation will be applied, must be given the possibility to prepare for it adequately. Such lenient transition can be ensured, for example, by postponing for a certain time the entering into force of the new regulation in the transitional provisions (*see Judgement of 16 December 2005 by the Constitutional Court in Case No. 2005-12-0103, Para 24*). The contested norm was adopted on 4 October 2018 but, in accordance with Section 3 of the Amendments to the Consumer Rights Protection Law, it entered into force only on 1 July 2019. Thus, creditors had approximately nine months to adapt their commercial practice to the new regulation and ensure that the total costs of the credit for a consumer fall within the limits defined in the contested norm. This period is sufficient for recognising that lenient transition, compatible with the principle of legitimate expectations, to the new legal regulation has been ensured.

24.3. In assessing, whether the contested norms has ensured fair balance between the rights of consumers and creditors, the Constitutional Court must establish, whether, dure to restrictions, included in the contested norm, creditors' commercial activities were hindered to the extent that, substantially, licences issued to them were rendered meaningless.

The Applicants and association "The Alternative Financial Services Association of Latvia" have noted that the contested norm makes creditors' commercial activities economically unprofitable, namely, creditors no longer would be able to engage in commercial activities in the area of their choice, i.e., to issue short-term credits to consumers. Already now, because of the contested norm, several commercial companies have changed the products they offer or discontinued their operations.

The Ministry of Economics notes that the contested norm could have a negative impact on some creditors whose commercial activities are directly linked to issuing short-term credits. Whether these commercial companies will continue

their operations is said to depend on their ability to adjust to changes in the market. The Consumer Rights Protection Centre, in turn, believes that, as the result of applying the contested norm, those commercial companies whose area of commercial activities is issuing short-term loans, possibly, will discontinue their operations; however, in general, the impact of the contested norm upon the area of credit should be assessed as being similar to the one caused by the restrictions on the total costs of the credit for a consumer established before. Also at that time, creditors had expressed concern that, possibly, they would have to discontinue their commercial activities; however, these concerns had not been confirmed (*see Case Materials, Vol. 3, p. 86, and Vol. 4, p. 73).*

Pursuant to Section 8 (1^1) of the Consumer Rights Protection Law and Para 2 of Regulation No. 245, capital companies who have received a special licence for providing consumer crediting services, issued by the Consumer Rights Protection Centre, are allowed to provide crediting services to a consumer. During the period of the validity of this licence, creditors are obliged to submit twice per year – by 1 March and 1 September - to the Consumer Rights Protection Centre information about services they have provided, to ensure, thus, that operations of providers of credit services are supervised (*see Para 28 of Regulation No. 245*).

The Applicants continue providing consumer crediting services on the basis of the licences issued to them also after the contested norm has entered into force. It follows from the Consumer Rights Protection Law and Regulation No. 245 that the licence grants to creditors the right to provide to a consumer all types of crediting services. The contested norm does not envisage annulment of the licences issued to creditors and *per se* does not prohibit creditors from providing consumer crediting services. Hence, the Constitutional Court has no grounds for arriving at the conclusion that, by the respective restriction, creditors' commercial activities would be hindered in way that would, substantially, render the licences issued to them meaningless.

24.4. The Constitutional Court concludes that the benefit that society gains from the restriction, included in the contested norm, in circumstances where there was a necessity to decrease the total costs of the credit for a consumer to protect consumer rights, outweighs the adverse consequences caused for creditors due to restriction of their fundamental rights. Moreover, the legislator has found a balance between society's interests and creditors' legitimate expectations by postponing, in the transitional provisions, entering into force of the new regulation for a certain period.

Hence, the restriction complies with the proportionality principle and, thus, the contested norm complies with Article 1 and Article 105 of the *Satversme*.

The Substantive Part

On the basis of Sections 30–32 of the Constitutional Court Law, the Constitutional Court

held:

to recognise Section 8 (2^3) of the Consumer Rights Protection Law as being compatible with Article 1 and Article 105 of the *Satversme* of the Republic of Latvia.

The Judgement is final and not subject to appeal.

The Judgement enters into force on the day it is published.

Chairperson of the court hearing I. Ziemele