

PARTIAL REGULATORY IMPACT ASSESSMENT (RIA)

Directive of the European Parliament and of the Council concerning unfair business-to-consumer commercial practices in the internal market

(The Unfair Commercial Practices Directive)

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A. Introduction

1. In October 2001, the European Commission launched a wide-ranging consultation on a Green Paper on EU Consumer Protection (the “Green Paper”).ⁱ The Green Paper made a number of proposals to harmonise and improve the current EU consumer protection regime, including the introduction of a framework directive containing a “general duty to trade fairly”, the development of codes of practice at the EU level, and improved enforcement co-operation.
2. The Commission published a Follow-up Communicationⁱⁱ (the “Follow-up”) on 11 June 2002, which stated that the Commission had received broad support for reform of the current regime and set out the Commission’s intention to propose a framework directive containing a “general duty [not] to trade [un] fairly”. The framework would also provide for the development of self- and co- regulation and the participation of stakeholders. The Commission set up an ‘expert group’ of national officials which discussed national fairness law and considered the basis of an EU framework directive.
3. On 18 June 2003, the Commission published a draft Directive concerning unfair business-to-consumer practices in the internal market (the “Unfair Commercial Practices Directive”). The draft framework Directive consisted of a self-standing general clause containing a prohibition on unfair commercial practices; the further elaboration of two categories of unfair commercial practices - misleading commercial practices (omissions as well as actions) and aggressive commercial practices - in each case with criteria to establish whether a practice is misleading or aggressive; and an annex containing a list of commercial practices that are to be considered unfair under all circumstances.
4. This regulatory impact assessment (RIA) is an assessment of the costs and benefits that might be associated with a framework directive. It is based on Commission consultation papers that provide a broad idea of the nature of any reform and the content of a future directive, but principally from the Commission’s draft Directive of 18 June 2003. Assessment of costs and benefits is based on previous consultation with business, consumer organisations and enforcement bodies. The RIA will be developed as the EU negotiations progress and will be used to inform the UK’s input into EU discussion.

ⁱ Green Paper on EU Consumer Protection, 2 October 2001 (COM(2001)531 final)
http://europa.eu.int/comm/consumers/policy/developments/fair_comm_pract/fair_comm_greenpap_en.pdf

ⁱⁱ Follow-up Communication to the Green Paper on EU Consumer Protection, 11 June 2002 (COM(2002) 289 final)
http://europa.eu.int/comm/consumers/policy/developments/fair_comm_pract/communication_en.pdf

B. Issues and Objectives

Issues:

5. In the Green Paper on EU Consumer Protection, the Commission identified the following problems:
 - Gaps in the coverage of existing EU Consumer Protection Directives - key areas such as marketing practices, practices linked to the contract, payment and after sales services are not covered;
 - The sector-specific approach, the long transposition period, and the time required to amend directives has meant that rules become quickly outdated and allow rogues to stay one step ahead of the law;
 - Gaps between Directives and the use of minimum clauses has allowed national legislation to play an ever greater role, creating a barrier to cross-border trade and shopping. Interaction between EU rules, national law, contract law, and private international law is difficult to understand, creating confusion for consumers and business.

6. On 11 April 2003, the DTI held a workshop to discuss the nature of consumer detriment from unfair commercial practices in the UK and the extent to which a “general duty to trade fairly” could help. Key problems discussed were: the use of high pressure selling techniques; the targeting of vulnerable consumers or consumers in a vulnerable position; inadequate or misleading information about products, services or prices; and inadequate responses to customer complaints. The workshop concluded that legislation in the area was often patchy and often difficult to enforce, and that a general duty to trade fairly could provide some useful tools for enforcement.

7. The UK does not currently have a “general duty not to trade unfairly” in its legal regime. This is in contrast to most other EU member states that are used to the application of such a general principle. The DTI has therefore commissioned a study by leading academics to consider how concepts of fair trading are currently used in English law and the potential impact of an explicit ‘general duty to trade fairly.’ The Report broadly concludes that while the Directive will have a considerable impact on English law, English courts already apply general principles of fair trading and that the application of general rules has not proven problematic for courts or business. The Report also highlights the potential for deregulation and rationalisation of the current regime.

Objective:

8. In the Explanatory Memorandum accompanying the draft Directive, the Commission sets out the broad objectives of the introduction of a framework directive. The Directive is intended to:
- Address internal market barriers by harmonising the requirements in an EU-wide framework of legal principles governing unfair business-to-consumer commercial practices;
 - Deliver a high level of consumer protection in order to promote consumer confidence, while minimising the burden on business; and
 - Achieve legal certainty whilst remaining as simple as possible and adaptable to market developments.

C. Risk Assessment of current problems

Consumer protection:

9. The National Consumer Council has presented an analysis of over 50 case studies of consumer detriment covering misleading practices, non-disclosure of important information and charges, exploitation and coercive selling, failure to deal with after sales problems.ⁱⁱⁱ The paper argues that a general duty would tackle gaps in the law and assist in covering future practices. The National Association of Citizens Advice Bureau has produced a report on the problems related to doorstep selling. The report is based on more than 1,500 evidence reports from 353 bureaux. The report argues that consumers are commonly subjected to unfair trading practices including high-pressure sales techniques and deception.^{iv}

10. On 11 April 2003, the DTI held a workshop attended by representatives from Trading Standards, Citizens Advice Bureaux (CAB), Office of Fair Trading (OFT) and National Consumer Council (NCC). The purpose of the workshop was to discuss in detail: the nature of consumer detriment from unfair commercial practices in the UK, including ascertaining where current legislation applies and why it may be difficult to enforce or be unenforceable; how a “general duty to trade fairly” could help to deal with practices that are not covered or difficult to enforce under current legislation; and what would need to be contained within the general duty in order to ensure that it works.

11. The workshop participants concluded that:
- There was often legislation in the area but that coverage was patchy and often difficult to enforce, particularly in respect of gathering sufficient evidence. Consumer awareness of their rights was also an issue.

ⁱⁱⁱ NCC “The case for a general duty – evidence to support the NCC’s campaign for a general duty not to trade unfairly”.

^{iv} NACAB Evidence Report “Door to Door: CAB clients’ experience of doorstep selling”, September 2002.

- A general duty to trade fairly could provide some useful tools for enforcement authorities, particularly in relation to misleading information, omissions of information and the use of high-pressure selling techniques: this would be more effective in some sectors than others. However, the difficulties of evidence gathering, enforcement and protecting the vulnerable may remain.

Barriers to cross border shopping:

12. The Commission has published an ex-ante assessment produced by GFA Management of the options presented in the Green Paper.^v The study uses consumer and business surveys to argue that there is significant potential for business-to-consumer cross border trade – nearly 40% of European companies targeting consumers would increase the proportion of their marketing and advertising budget to encourage cross border sales. A consumer survey undertaken as part of the study suggests that a potential 80 million European consumers would buy more cross border if they were confident about making purchases from shops in another EU country.

13. In a Eurobarometer survey on business experience of, and attitudes to, cross-border shopping, business reported that cross-border sales make up only a small percentage of sales to final consumers: 3% of Internet sales, 3.7% of telephone/mail order, 8% of door-to-door, 4.8% of sales to tourists in shops. Only 6.6% of advertising and marketing budgets are aimed at encouraging cross-border sales. Harmonisation of regulations on commercial practices, advertising and other consumer protection regulation was cited as the most efficient of the options in facilitating cross-border sales and/or advertising (68.2% of businesses).^{vi}

14. The proposal should also help to tackle the problem of rogue practices. For example, within the timeshare sector, the Organisation for Timeshare in Europe (the “OTE”), estimates that approximately 8-10% of sales are lost to rogue operators in Spain out of total revenue of €431million per annum.

^v GFA Management “Ex-ante Impact Assessment of the options outlined in the Green Paper on EU Consumer Protection” (B5-1000/02/000074).

http://europa.eu.int/comm/consumers/policy/developments/fair_comm_pract/gfa_report_en.pdf

^{vi} Standard Eurobarometer 57.2 - Flash Eurobarometer 128 Public opinion in Europe: Views on business-to-consumer cross-border trade, 14 November 2002

Opinion Studies conducted by: The European Opinion Research Group EEIG and Eos Gallup Europe

D. Options presented by the European Commission

15. Two options were identified in the Green Paper as potential routes for reform of the EU consumer protection regime. The Follow-up stated that the majority of respondents to the consultation on the Green Paper supported the second option. As a result, the Commission has stated its intention to make a proposal for a framework directive based on the “mixed approach”.

Option 1:

A “specific approach” based on the adoption of a series of further specific directives.

16. In its Green Paper, the Commission considered the possibility of achieving further harmonisation through the adoption of a series of further specific directives. The Green Paper suggested that the number of measures required would be difficult to estimate, but it was likely that directives covering advertising, marketing practices, payment and after sales service would be required, in addition to certain additional sector-specific directives. Existing directives would also need to be reviewed and reformed to keep them up to date. The Commission also stressed the importance of removing the ‘minimum clause’ in existing directives to encourage greater harmonisation of rules amongst member states. The minimum clause allows member states to retain or introduce higher levels of protection than those in the Directive.

Option 2:

A “mixed approach” of a comprehensive framework directive, supplemented by targeted directives where necessary.

17. The Green Paper presented the option of a new “mixed approach” consisting of an EU framework directive which would harmonise national fairness rules for business-consumer commercial practices. The Follow-up set out the Commission’s initial thoughts on a framework Directive in more detail.

18. In the draft Unfair Commercial Practices Directive, the general clause stipulates that a commercial practices is unfair if two core elements are met: the practice is contrary to the requirements of professional diligence; and it materially distorts or is likely to materially distort the economic behaviour with regard to the product of the average consumer to whom it is addressed or whom it reaches. The general clause is supplemented by two unfairness categories:

- A prohibition on misleading commercial practices. This may consist of misleading actions, i.e. deceiving the consumer in relation to an aspect of the product; or misleading omissions, i.e. failing to provide material information that the consumer needs to take an informed transactional decision.
- - A prohibition on aggressive commercial practices, i.e. the use of harassment, coercion or undue influence which leads to the average consumer’s freedom of choice or conduct with regard to the product being significantly impaired;

19. Attached to the framework Directive is an annex containing an exhaustive list of commercial practices which will in all circumstances be regarded as unfair.

Transposition

20. Transposition of the framework Directive in the UK may present an opportunity to deregulate some of the existing body of UK regulations. In particular, transposition of the Directive will require the amendment of conflicting domestic sectoral provisions which relate to unfair commercial practices. Domestic legislation which implements existing EU directives may remain, but other sectoral provisions that go beyond or conflict with the provisions of the framework Directive may need to be removed.

E. Quantifying and valuing the benefits and costs

Option 1: “specific approach”

Benefits

21. The Green Paper recognises that this is a familiar and tried-and-tested method that has led to the adoption of existing legislative provisions. It is easier to reach agreement on and adopt directives with limited scope. Moreover, specific targeted pieces of legislation offer clear rules for business and make it more likely that regulation will only apply where it is necessary.

Costs

22. The specific approach has been criticised on the basis that it takes a protracted period to adopt, review and amend directives. For instance, it took approximately 6 years of negotiations before the Sale of Goods Directive^{vii} was adopted. In addition, it has been claimed that the use of specific directives has created gaps that have enabled unscrupulous traders to stay ahead of the law.

23. A failure to introduce harmonisation might maintain costs to consumers and business seeking to shop or market across border. However, business response to the Green Paper claimed that regulation was only one factor affecting how consumers and business act across border – other factors were likely to include different languages, the desire to make purchases face-to-face, delivery time.

Question 1: Do you have any comments on this assessment? Do you have examples of particular costs or benefits of the specific approach?

Option 2: “mixed approach with general duty not to trade unfairly”

Benefits

24. The Green Paper and the Follow up set out a number of the potential benefits of a framework directive.

- **Better regulation.** The Commission intends for the framework to provide a more flexible and less prescriptive means of regulation. The comprehensive nature of such a clause should, in theory, reduce the need for further detailed consumer protection regulation. It might also provide a mechanism for simplification and reform of existing consumer protection Directives.

^{vii} 1999/44/EC

- Reducing internal market barriers. It is intended that the framework directive would make it easier for business to trade across border. Harmonised consumer protection rules and the elimination of the minimum clause in consumer protection directives should reduce regulatory barriers and reduce the legal cost of ensuring compliance with different regimes.
- Empowering consumers. The introduction of safety net legislation and clearer rules should increase the confidence of consumers to shop across border. This would enable consumers to get better deals and would open new markets for business.
- Strengthening the internal market. Empowered consumers, increased cross border marketing and shopping, and stronger action against rogue practices will drive competition within the internal market.
- Targeting rogues. If the general clause is used to tackle instances of bad practice currently not caught under existing law, there is a potential benefit for those companies who lose customers to companies engaged in rogue practices.

Question 2: Do you have any comments on this assessment of the potential benefits? How might these benefits affect your business or businesses in your sector? What are the most important benefits?

Question 3: What are the most important factors in maximising the benefits? e.g. how should existing legislation be simplified to create most benefits?

Compliance Costs

25. The following costs are based on the Commission's initial proposals for a framework Directive (Option 2). Figures are provided where possible and are based on costs provided through informal consultation with UK companies.

The General Clause

26. Compliance costs for the general clause are difficult to estimate because its nature is at this stage unclear. In the draft Unfair Commercial Practices Directive, the general clause stipulates that a commercial practices is unfair if two core elements are met: the practice is contrary to the requirements of professional diligence; and it materially distorts or is likely to materially distort the economic behaviour with regard to the product of the average consumer to whom it is addressed or whom it reaches.

27. A prime objective of any framework directive is to harmonise rules across the EU – thus creating consumer and business benefits. However, there is the risk, due to different legal traditions, that the general prohibition on unfair commercial practices will be interpreted differently across the Member States of the EU if it is defined too broadly. A freestanding general clause that is not confined to the unfairness categories

and the “blacklist” of unfair commercial practices has the potential for creating widely diverging national interpretations. This would lead to increased legal uncertainty and therefore increased compliance and ongoing legal costs. This is more likely to be the case should a framework directive contain a ‘minimum clause’, which allows member states to apply their own definition of fairness. This would lead to increased legal uncertainty and therefore increased compliance and ongoing legal costs.

28. However, there is also uncertainty about the impact and potential costs of “maximum harmonisation”. The scope of the Directive is very wide and the restrictions on how member states can regulate unfair practices are unclear. A potential problem lies with highly regulated sectors such as financial services, the utilities, and transport. Such sectors are subject to detailed rules which have the effect of regulating unfair commercial practices, in the form of conduct of business rules or licensing requirements. In such sectors, firms will have spent considerable sums of money implementing these provisions and the repeal of such rules might have cost implications. If detailed rules were replaced by general rules, there might also be uncertainty and additional compliance costs for such companies that are used to detailed provisions.

29. In an attempt to address issues of uncertainty, the OFT will consult and issue guidance on the application of the Directive in the UK prior to any new legislation coming into force. This should help counter any additional costs to business. However, as an illustrative example of potential legal costs, a trade association representing SME’s in the UK offers a free legal help line as part of its membership fee. However, for advice falling outside this service the trade association’s lawyers charge a reduced rate of £140 per hour. While most small businesses would usually do the majority of the ground work themselves, this is a significant potential cost if rules are uncertain.

Question 4: Do you have any comments on the assessment of costs and benefits associated with the general prohibition?

Question 5: Are you able to quantify what it might cost your business to change practice in this area?

Question 6: How could costs be minimised and benefits maximised?

Particular Categories of Unfair Commercial Practices

30. In addition to the general clause, there are two broad categories of unfairness – misleading actions and omissions and aggressive practices.

Misleading Actions

31. The draft Framework Directive expands on the requirements of the Misleading Advertising Directive. New requirements include requirements that a trader must not mislead about:

- after-sale customer assistance and complaint handling or the need for customer assistance and repair;
- the benefits or risks, claims about the product which the trader cannot substantiate, or the circumstances of the consumer including the rights and risks he may face;
- claims about any statement or symbol in relation to direct or indirect sponsorship or approval;
- the existence of a specific price advantage

32. There are also provisions relating to misleading actions about the company or brand. A trader must not mislead through: non-compliance with firm and verifiable commitments in a code of conduct to which the trader has agreed to be bound; or non-compliance with a commitment given to a public authority to cease an unfair commercial practice.

33. UK companies engaging in advertising or sales promotions must currently comply with the British Code of Advertising, Sales Promotions and Direct Marketing (“the Code”). The Code is created and enforced by the Committee of Advertising Practice and is endorsed and administered by the Advertising Standards Authority. This well established self-regulatory system is recognised by the OFT, the Government and the courts as one of the established means of consumer protection for non-broadcasting marketing. The system applies to all companies whether they take part in the creation of the code or not and is reinforced by the Control of Misleading Advertisements Regulations (1988).

34. As the provisions of the framework incorporate a number of requirements of the Misleading Advertising Directive and still allow for the use of self-regulatory systems, then the cost could be minimal. As the provisions do not create any positive requirements for how a company must trade to show it is not misleading, the costs should be minimal. There is even the possibility of reduced costs or new trade opportunities if there is harmonisation of such provisions across the EU.

35. There is scope for increased compliance costs if the UK’s self-regulatory system requires substantive structural change or if business needs to comply with new rules which cannot be implemented by the Code. This is more likely to be the case if the framework directive contained requirements for how codes should work (e.g. stakeholder involvement) or if it required code owners to obtain EU approval or for businesses to join EU codes. Increased costs are also more likely if the framework directive does not allow flexibility, which would hinder the ability of the Code to adapt to market circumstances and which might even restrict innovations in marketing and advertising.

Question 7: Do you have any comments on the costs and benefits associated with rules on misleading actions?

Question 8: How could costs be minimised and benefits maximised?

Misleading Omissions

36. The Directive prohibits commercial practices which omit or hide material information that the average consumer needs to make an informed decision. The Directive provides certain core information that must always be provided save where there is apparent from the context, including the traders name and the main characteristics of the product. Information requirements in specific EU Directives will also be considered material.

37. Businesses currently need to comply with a range of information requirements: many of these are the result of EU Directives. Information usually needs to be provided in advertisements, promotional literature, at any point of sale communication, and in any contract. Any new compliance cost will depend on the extent of the framework directive's additional information requirements and whether business is clear about which information requirements it must comply with. The Framework Directive does make clear that the sectoral directive would take priority. There is the potential for savings if the framework directive were to harmonise and / or replace existing information requirements.

38. The provision of information creates costs in terms of the amount of paper required and the amount of a brochure, contract or advertisement it takes up. Costs would be minimized if certain information were available "on request" and if provisions were made for different forms of media. For example, it is easier to provide more information in brochures but more burdensome to provide the same information in an in-store poster or a radio advertisement.

Question 9: Do you have any comments on the costs and benefits associated with rules on misleading omissions?

Question 10: How could costs be minimised and benefits maximised?

Aggressive commercial practices

39. The Directive contains specific provisions to tackle aggressive commercial practices which, through harassment, coercion or undue influence, significantly impair, or is likely to significantly impair, the average consumer's freedom of choice or conduct.

40. The Consumer Protection (Cancellation of Contracts Concluded Away from Business Premises) Regulations 1987 (as amended), which implemented the Doorstep

Selling Directive^{viii}, currently provides protection to consumers faced with salesmen away from a business premises or visiting them at home. However, it has been argued that this Directive does not cover many cases of pressure selling and does not provide sufficient tools to enforcement bodies. The National Association of Citizens Advice Bureau report provides 1,500 evidence reports demonstrating unfair trading practices in the sector.^{ix}

41. Direct and doorstep selling is significant sector in the UK and across the EU. In the UK, annual sales of consumer goods and services amount to £1.7 billion, with sales having doubled over the last 10 years. Around 480,000 men and women are engaged in the sector in the UK.^x Direct selling is a useful technique where products benefit from explanation or demonstration, where the product is novel, and where conventional advertising might not be appropriate.

42. To the extent that any framework directive tackled the small minority of unscrupulous companies engaging in bad practices, the compliance costs to legitimate business should be limited. In fact, there could be a saving to companies adopting high standards in their direct selling if it ensures that all companies act at the same level and drives out rogues. There could also be savings if the framework directive introduces harmonised consumer protection rules, particularly in respect of cooling off periods. Costs could also be minimised if companies are able to use a code of practice to ensure conformity with EU requirements.

43. There is the potential for increased costs if the framework directive sets new prescriptive procedures, sets certain requirements as to how a company should prove that they have not engaged in aggressive selling, or if the cooling off period is increased. There are also issues surrounding how vulnerable consumers are protected – if such consumers are targeted by the framework directive, care will need to be taken to ensure that this does not prevent companies from selling fairly to such consumers or leads to unnecessarily prescriptive requirements for other sectors e.g. e-commerce.

Question 11: Do you have any comments on the assessment of costs and benefits associated with rules on aggressive commercial practices?

Question 12: How could costs be minimised and benefits maximised?

^{viii}Council Directive 85/577/EEC to protect the consumer in respect of contracts negotiated away from business premises.

^{ix} NACAB Evidence Report “Door to Door: CAB clients’ experience of doorstep selling”, September 2002.

^x Figures provided by the Direct Selling Association.

Estimated Total Compliance Cost

44. It is difficult to estimate total compliance costs at present although business estimates of the potential costs associated with the four fairness categories would be helpful.

Other Costs

Government

45. A move from a sector specific approach to a framework directive has the potential to introduce savings for Government in respect of the time taken to negotiate and transpose EU Directives. However, any savings will be reduced if there is a need to take part in regular EU discussions on new ‘fairness categories’ or updating the list of unfair practices on a more frequent basis than can be justified by changes in market practice. The requirements of “maximum harmonisation” might also create increased costs in assessing whether provisions go above the required level; costs will be increased for highly regulated sectors such as financial services.

Enforcement bodies

46. There is a potential benefit for enforcement bodies if new tools are created that enable action against rogue traders and practices. However, any benefits will be reduced if rules are unclear and do not tackle the intended practice.

Business Sectors Affected

47. There is a potential impact on all sectors that are involved in business-to-consumer transactions. However, it is likely that the following sectors are likely to be most affected – retail, distance selling including e-commerce and mail order, doorstep selling, financial services, consumer credit, estate agency, transport, sales promotions, package travel, timeshare, education and training, and the holiday sector. Business sectors that provide services to other business will also be affected, namely the marketing, advertising and publishing sectors.

Question 13: Is this an accurate assessment of the business sectors likely to be affected by the proposals?

F. Consultation

Consultation

48. There have been three rounds of written consultation. The first was conducted on the basis of the Green Paper; the second in response to the Follow-up Communication and the third in relation to the draft Directive itself. Copies of the two documents and draft Directive were circulated widely amongst stakeholders (businesses and business organisations, consumer bodies and enforcement bodies). 35 formal responses were received by British stakeholders relating to the Green Paper; 21 formal responses were received in respect of the Follow-up Communication; 55 responses were received in respect of the consultation on the draft Directive.

49. For all three consultations, a meeting was arranged with a representative from the European Commission. Bilateral meetings with individual companies and organisations also took place. The Government will continue to consult throughout the negotiations on the Directive and to disseminate information about progress.

Consultation with small businesses

50. All sectors of small business are liable to be affected by the introduction of a framework directive. Stakeholders representing small business have been involved in consultation process.

51. The principal concerns expressed by small business were:

- that the framework Directive may impose an extra layer of unnecessary regulation as opposed to simplifying existing legislation;
- that there is need for more clarity about how a framework Directive would relate to existing directives, both in substance and with regard to the timing of implementation and reform. In particular, that there should not be a period of overlap in which businesses face a duplication of regulation;
- that codes of conduct should not be made legally binding as this would discourage businesses from signing up to codes and would go against the nature of self-regulation.

Particular issues raised by business

52. A number of issues have been expressed by business about the proposals:

- Concern that the Directive set clear and proportionate rules which provide legal certainty. Business believes that amendments to the definitions, especially “professional diligence” and “material diligence”, are necessary to achieve this;

- Concern that the relationship between the UCP Directive and EC directives should be clarified

- Concern that the Framework directive should complement market opening and the internal market. In this respect the internal market clause which provides for the application of home state control and mutual recognition is key.

- The benefits achieved through previous negotiations should be retained. In particular, the framework Directive should continue to be framed in terms of “unfairness” and should not be overly prescriptive or contain detailed rules on after-sales service and complaints handling that might create unnecessary burdens.

- The Directive should continue to be clearly focussed on unfair business-to-consumer practices and should not be extended to business-to-business practices.

- Business groups have welcomed the Commission’s suggestions that the introduction of any general duty could be accompanied by a simplification of existing directives. However, there is concern that this should take place when the framework Directive is introduced or that a firm commitment is provided of when it will happen.

- Concern that the Directive should apply to the “collective” interests of consumers and should not give rise to rights in private law.

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Department of Trade and Industry
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