6th of February 2015

Final EMF Comments on EBA Consultation Papers on Draft Guidelines on Creditworthiness Assessment and on Arrears & Foreclosure

The European Mortgage Federation[1] (EMF) welcomes the opportunity to comment on the EBA's draft Guidelines on creditworthiness assessment and on arrears and foreclosure:

- *General remark*

The aim of the draft Guidelines is to provide greater detail on how credit institutions should give effect to Articles 18, 20(1) and 28 of the Mortgage Credit Directive (MCD) and, in this way, "ensure that these high-level provisions will be implemented and supervised consistently across the 28 EU Member States"[2] and "thus contribute to the EBA's objective of achieving a convergence of supervisory practices"[3]. The EMF would like to recall that, on the basis of extensive consultation, discussion and negotiation during the legislative process on the MCD, the EU Institutions took the decision to take a largely minimum harmonisation approach to the Directive and to adopt high-level, principles in relation to the assessment of creditworthiness and arrears and foreclosure. The Co-legislators recognised the need to provide Member States with the necessary flexibility in order to take account of the specificities of their national markets. Prescriptive EU-wide legal obligations – either at the time or at a later date - would not only constrain long-standing national practices, but also potentially result in increased litigation. It is vital that this deliberate flexibility is maintained and respected during the transposition and implementation process.

The EMF would like to take this opportunity to underline that the flexibility and discretion provided for in the MCD does not equate to vagueness. The EMF would therefore caution against the use of vague notions in the draft guidelines, which could be a source of legal uncertainty and unnecessarily divergent local interpretations, and rather encourage a focus on objectivity.

As a further general remark, the EMF would like to underline the importance of striking the right balance between gathering relevant information on the financial situation of the candidate borrower without violating data protection legislation and ensuring that the candidate borrower is responsible and accountable for the information he/she provides, and, ultimately, for the final decision regarding which credit best suits his/her needs. In this respect, the principle of "responsible borrowing" is an extremely important one which should be promoted as much as possible through these Guidelines (see response to question 2 below).

I. Draft Guidelines on Creditworthiness Assessment

Question 1: Do you agree with the proposed Guidelines? If not, outline why you disagree and how the Guidelines could be improved. Please respond separately for each of the seven Guidelines.

[1]Established in 1967, the European Mortgage Federation (EMF) is the voice of the European mortgage industry, representing the interests of mortgage lenders and covered bond issuers at European level. The volume of outstanding mortgage loans in the EU amounted to €6.7 trillion at the end of 2013. As of November 2014, the EMF has 20 members across 15 EU Member States as well as a number of observer members in the EU and the Russian Federation. The European Mortgage Federation - European Covered Bond Council (EMF-ECBC) is registered in the European Institutions' Transparency Register under ID Number 24967486965-09.
[2]EBA Consultation Paper on Draft Guidelines on Creditworthiness Assessment, page 6.
[3]As above.

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Draft Guideline 1.1:

- The assessment of the candidate borrower's creditworthiness is carried out at the moment of the granting of the credit based on his/her circumstances at that time and not on the basis of the evolution of the borrower's financial circumstances throughout the lifetime of the loan, which are very difficult for the creditor to predict. Unless the borrower provides information about variability of his/her income, a creditor cannot feasibly verify this over the lifetime of the loan.
- If the requirement to collect income history is retained, the collection of data from borrowers should be limited to a certain period of time in order to secure proof of employment and the level of the income. The collection of life-time income data would be onerous for both parties.

Draft Guidelines 1.2 & 1.3:

- As a general remark, the EMF believes that provided the lender complies with the requirements of draft guideline 1.1, there is no reason why there should be additional, specific requirements for self-employed individuals or those with a seasonal income.
- As specific comments on the contents of 1.2 and 1.3, the EMF is concerned about the introduction of notions aimed at guaranteeing the quality of the information provided by the consumer, specifically the independence of sources (1.2) and third party verification (1.3). For example, would the receipt of a pay slip or a tax declaration from the consumer fulfil the third party verification requirement? Or is the intention that a creditor consults a candidate borrower's employer or the tax authority? These notions would be difficult to apply and justify operationally, would give rise to undesirable discussions with the third party and the consumers, particularly where the consumer already has a bank account/relationship with the lender and could actually prove to be an obstacle to the granting of mortgages to certain categories of consumers. The EMF therefore advocates the removal of this reference.

Draft Guideline 2.1: The more precise term "conclusion of the credit agreement" should replace "mortgage approval".

Draft Guideline 3.1:

- This requirement does not appear to take account of the general and the personalised information requirements in the MCD, the latter in the form of the ESIS, and appears to impose additional disclosure requirements, the added value of which is not clear. It should also be noted that the assessment of whether documentation is well presented or not is very subjective.
- Furthermore, the EMF is concerned that this draft guideline appears to shift the responsibility for misrepresentation of information by the candidate borrower from the borrower to the creditor.

Draft Guideline 4.1:

- The drafting of this guideline implies that in the event of payment difficulties or over-indebtedness of the borrower it would be concluded that the creditworthiness assessment had not been appropriately carried out by the creditor, that this was therefore the cause of the hardship and that the lender is liable. In the MCD, the lender should only assess the "probability" for the customer to fulfil his/her obligations. To ensure consistency with the MCD, the following wording should be deleted "without causing the consumer undue hardship and over-indebtedness".

Draft Guideline 4.2: The EMF understands this draft guideline as requiring the creditor to keep its credit policy up-to-date, rather than as a requirement on the creditor to continuously review the creditworthiness of the borrower. Confirmation of this understanding would be welcomed.

Draft Guideline 4.3: It is not possible to take into account all directly relevant taxes and insurances, since not all of this information is necessarily known to the creditor at the moment of the creditworthiness assessment.

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Draft Guideline 5.1:

- Unlike for a candidate borrower's existing financial obligations, creditors do not have access to information which would enable them to substantiate the "living expenses of the consumer", making it difficult to fulfil this requirement;
- If this draft Guideline were to be retained, it should allow creditors to make use of a standard amount to determine reasonable living expenses.

Draft Guideline 6.1: As indicated above, the Industry is very cautious about requirements on creditors to make allowances for future scenarios because of the obvious limitations to doing this. For this reason, the Industry believes that any such requirements should be limited to the stress-testing of mortgage payments.

Draft Guideline 7.1:

- The risk profile of a loan typically depends on the individual circumstances of a borrower; a loan that might pose a higher risk for one borrower because of their circumstances may not for another because of a different set of circumstances. What is important is complete and comprehensive information and adequate explanations to the candidate borrower of the features of different loans. It should be recalled that specific loan types with particular features, such as foreign currency loans and variable interest rate loans, are extensively addressed in the MCD and it is our view that no further action is required in this respect.
- The EMF would welcome clarification from the EBA on the extent to which this requirement is intended to be a conduct or prudential consideration of the borrower's risk profile. If the latter is intended, the EMF questions whether this is actually needed in addition to CRD IV.

Question 2: Are there any additional requirements that you would suggest adding to the Guidelines? If so, outline the reason(s) for each proposed additional requirement.

Following on from points made above, the EMF believes that it is important to include in the draft guidelines requirements relating to 'responsible borrowing', which would oblige borrowers to provide the lender with complete and correct information on their financial situation and personal circumstances in the context of the credit application process.

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II. Draft Guidelines on Arrears & Foreclosure

Question 1: Do you agree with the proposed Guidelines? If not, outline why you disagree and how the Guidelines could be improved. Please respond separately for each of the five Guidelines.

Draft Guideline 2.2:

- The EMF understands that the motivation behind the privacy requirement is to ensure that where meetings are held with borrowers that those meetings are held in private; however, as drafted, the EMF is concerned that this draft guideline could be misinterpreted as a requirement for a lender to conduct meetings with all of its borrowers in relation to their payment difficulties, which is not practicable.
- Furthermore, there is a risk that the reference to data protection legislation could be misconstrued as consent always being necessary, even, for example, in the case of an intermediary communicating payment default information to credit bureaus. The latter is information which is needed to safeguard financial stability and for which consent is not necessary. It should be clarified that the reference to consent relates to personal information such as the causes of default.
- As an additional consideration here, in some Member States, mortgage lenders operate on the internet and do not have branches, meaning that it is impossible to fill a physical meeting requirement. We would therefore suggest that "meetings" be replaced by "dialogue".

Draft Guideline 2.3: The exact aim and meaning of this requirement is not clear.

Draft Guidelines 3.1-3.4:

- These draft guidelines appear to impose new obligations at both a procedural and information level that are not contained within the MCD and do not appear to reflect the aim of Article 28 of the Directive.
- As an example of this, 3.1 covers borrowers' pre-arrears and 3.4(b) imposes a new information disclosure requirement on creditors, in addition to the already extensive information requirements under the MCD. This information could be provided by the public instances themselves via the internet.

Draft Guideline 4.1:

- The EMF would like to underline that the majority of cases where borrowers face difficulties in repaying their loans are solved amicably based on lender forbearance. However, this draft guideline appears to oblige creditors to accord concessions to consumers in arrears/past due. There are a number of concerns in this respect. Firstly, this could result in borrowers purposely not paying their instalments in the knowledge that they will receive concessions. Secondly, this could have a significant impact on risk-weighted assets, thus increasing the costs of mortgage loans and the risk of credit crunch phenomena. In the event of financial difficulty, there should be an obligation on borrowers to provide detailed financial information, which the lender can assess to ensure that the mortgage is sustainable. Where it is not deemed to be sustainable, the lender should be retain the right to decide not to offer forbearance and proceed to a different solution i.e. voluntary sale, enforcement etc., while the borrower may enter an insolvency arrangement or bankruptcy as a last resort.
- Furthermore, the requirement on a creditor to offer total or partial refinancing of a credit agreement could present a risk of action being taken against the lender on grounds of a kind of "abusive assistance" (this notion exists in France, for example, in commercial collective actions) in the event that the borrower is still unable to meet his/repayments.
- The EMF would therefore propose the following redraft of the Guideline:

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4.1 The creditor ***is encouraged to*** ~~should~~ take into account the individual circumstances of the consumer, the consumer's interests and rights and his/her ability to repay when deciding on ***if, and if so,*** which steps/forbearance measures to take. Forbearance measures ***can*** consist of concessions towards a consumer facing, or about to face, difficulties in meeting his/ her financial commitments. Concessions to the consumer ***could*** include:

Draft Guideline 5: The requirement on the lender to justify the reasons for the options offered to the borrower would introduce a subjective element to the explanation to be provided and furthermore present a risk that the reasons will be contested in court. It would furthermore place a significant administrative burden on the lender.

Question 2: Are there any additional requirements that you would suggest adding to the Guidelines? If so, outline the reason(s) for each proposed additional requirement.

A requirement setting out the borrower's obligation to co-operate with the lender should be included. Where a borrower does not co-operate, for example by ignoring correspondence (indicating that he/she might be unwilling rather than unable to meet repayments), then the protections under the Directive would not apply to the non-cooperating borrower and the lender should be permitted to proceed to the next stage in the process.

Also, it is important that any guidelines covering "non-primary dwelling" type residential mortgage borrowers i.e. buy-to-let borrowers, as a result of the national discretion in the MCD to include buy to let properties within the scope being applied, are formulated so that they do not either: (a) give rise to legal uncertainty or (b) unnecessarily extend mortgage resolution processes beyond the category of family homes, where contrary to buy-to-let which is a 'discretionary' type of ownership, the focus is keeping a roof over a family's head.

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