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Commission Services
DG Internal Market
European Commission
Brussels
Belgium

Our ref: Mortgages Green Paper/KW

30 November 2005

Dear Sirs

Green Paper – Mortgage Credit in the EU

The Panel is grateful for this opportunity to comment on the Green Paper dealing with the mortgage market in the EU, outlining a potential case for intervention by the Commission in order to facilitate further integration of this complex market.

The Panel was fully supportive of the introduction of the regime covering the sale of mortgages in the UK. It believes this has been an important step in ensuring consumers are protected during what is often the most significant purchase they are likely to make. We are therefore encouraged that the Commission is seeking to ensure that other EU consumers benefit from mortgage regulation. That said, the Panel is concerned that any EU legislation in this area could result in additional cost to the UK mortgage industry, at a time when it has only recently absorbed significant costs associated with the new regime in the UK. As is usually the case, these costs are being passed on to UK consumers. However, the Panel is broadly supportive of any initiative which attempts to replicate the benefits enjoyed by UK consumers both in terms of the diversity and innovative nature of the UK market, and of the level of consumer protection available.

The Panel does not see the single market becoming a reality by means of consumers buying their homes with finance provided by a lender in another member state. The Panel understands that the housing market across the EU is very diverse – for example, home ownership in some member states is very low in comparison to others as a result of differences in social, political and cultural attitudes to home ownership. It therefore doubts there will be significant demand for cross-border sales of mortgage products. There may be some niche markets - second homes abroad for example - but the market will overwhelmingly from the consumer's perspective remain a national one.

The Panel believes the route to a more integrated EU market lies in harmonising funding arrangements allowing greater freedom for lenders, which will result in the creation of more diverse products becoming available across Europe. It also believes that a more consistent approach to valuations, early repayment charges, credit

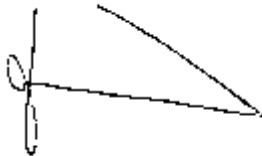
worthiness checks, and the relaxation of other legal constraints will play a much more significant role in promoting an integrated market. The Panel does not believe that consumer protection measures alone can achieve the stated aims of the Green paper. Indeed in isolation such measures are likely to have little effect. For example, the Panel fails to see how the introduction of a compulsory standardised information sheet can facilitate cross-border sales. Consumers need appropriate information at the right time in the mortgage buying process. But in view of the diversity of local arrangements the correct way to address this is to ensure each member state requires suitable pre-sale information which accurately reflects the local market and is not constrained by EU requirements which may not be appropriate in every case.

The Panel has considered the so-called 26th regime, but does not have sufficient information to be able to judge if this would be a suitable compromise solution. This perhaps warrants closer scrutiny as a potential workable solution to this issue.

The Panel believes that the right way to achieve the stated objective in the Green paper is to first address the restrictions in wholesale funding of mortgages and other legal constraints, which exist in some member states. Opening up such restricted markets to more innovative products will have an obvious and direct benefit for consumers. The Panel's answers to the questions posed in the Green Paper are attached as an annex to this letter.

The Panel welcomes this initiative by the Commission and looks forward to being involved in the continuing debate on this issue.

Yours faithfully

A handwritten signature in black ink, appearing to be 'John Howard', written in a cursive style.

John Howard
Chairman
Financial Services Consumer Panel

Specific response to questions posed

1. Should the Code of Conduct be replaced by binding legislation?

The Panel does not see the merits in simply translating the existing Code into binding legislation. It would rather see each individual member state being given the obligation to introduce robust consumer protection measures which address specific market failures in the local market.

2. What information should be given to consumers? A careful balance must be found between information deficiency and information overload.

The Panel is fully supportive of the new mortgage regime introduced in the UK in October 2004. That regime provides rules for financial promotions, pre-sale disclosure on initial contact outlining the level of service to be provided (e.g. advice or a non-advised sale, fees, policy on refunds etc); pre-application disclosure which requires key facts about the mortgage to be clearly outlined, including full details of costs and charges etc. It also covers post-sale information including after sale and on-going information requirements in annual statements. There are also rules covering information which must be given to consumer who are in arrears.

3. The Commission considers it fundamental that pre-contractual information is provided at a stage that enables the consumer to shop around and compare offers. Can such a common EU stage be identified, given the variations in Member States traditions and legislation?

The Panel believes that it should be possible to impose an obligation to provide *pre-application* key facts about a mortgage across Member States which allows for variations in processes.

4. Should an information provision regime apply only to lenders or to others such as brokers too? How can compliance with any such regime (binding/voluntary) be ensured?

The Panel understands that approximately 50% of all UK mortgage sales are affected through a broker. It is therefore appropriate that the same obligations for pre-sale disclosure are imposed on brokers to ensure the right level of consumer protection and to avoid any disproportionate impact on one sector of the market. The UK regime places the same obligations on brokers to become authorised by the regulator and this ensures that the regime can be properly enforced across the whole mortgage market. The Panel believes this is an effective and necessary model.

5. Should the provision of advice to the borrower be made compulsory or be a matter of choice?

The Panel does not believe consumers should be forced to accept advice – this should on the whole be a matter of choice.

6. Should conditions be applied to any advice actually provided, whether under a duty of choice (e.g. standards for the advice, sanctions for non-compliance, advance disclosure of fees, of the adviser's role and recording on durable medium)?

The Panel fully supports the UK regime in this area which imposes standards on suitability of advice. The UK regime imposes duties which include all the examples listed in the question.

7. Should early repayment be a legal right or a matter of choice? If it is to be a right, should it also be made possible for a consumer to waive this right? Under what conditions? Should this right be subject to compensation in the form of fees?

The Panel believes consumers should have a right to repay their mortgage early. In the UK consumers have an equitable right to redeem a mortgage and any attempt to impose a fetter on this right is prevented. The Panel is not in favour of consumers being able to waive this right as it believes some firms may put pressure on consumers to do so, with the result that this is not the consumer's free choice. That said, where the consumer has had the benefit of an introductory rate of interest, commonly below standard rates, then the Panel is in favour of lenders being able to charge a fee to compensate them for the consumer repaying before that special offer rate ends. Any fee charged should be restricted to compensating the lender and should not in any way be used as a penalty.

8. How should such fees (whether under a right or through contractual choice) be calculated? Should there be caps, as is the case in some Member States?

In view of the complex funding arrangements which exist in the UK – which, if replicated across the EU, many see as a good way of establishing a more integrated market – the Panel does not feel that it is possible to impose a calculation on firms. It would be more appropriate to impose a requirement that the resulting charge is fair. The Panel is not in favour of a cap on fees as fee capping does not automatically result in consumer benefit and may actually be consumer-detrimental to some groups.

9. How should the consumer be informed about early repayment? Is there scope for consumer education here?

The Panel feels the current UK practice of requiring examples of early repayment charges to appear in pre-application information is the best way of ensuring consumers are properly informed of the impact of early repayment. The Panel feels that consumer education can play a role here, but the product provider or broker selling the mortgage should be required to fully disclose if a fee will be payable on early repayment and illustrate what that fee might be.

10. What is the purpose of APR information? Information? Comparison? Both?

The Panel believes the APR is intended to provide consumers with the true cost of the credit taking account of interest and all other fees charged for taking out the mortgage. This is important from both an information and comparison perspective. The Panel is concerned that recent research in the UK suggests consumers do not fully understand what the APR is, and feels that in the absence of any other adequate costs comparison measure, further consumer education is needed here. Some commentators have advocated the use of the total cost for credit, but the Panel believes that this would need to be imposed across all consumer credit, not just the mortgage market, as consumers should be able to compare the costs of credit across a wide range of products.

11. Should there be an EU standard covering both the calculation method and the costs element?

The Panel understands that the UK mortgage regime uses the APR calculation laid down in the Consumer Credit Directive (87/102/EEC as amended by 90/88/EEC and 98/7/EC). It believes that for consumers to be able to make a meaningful comparison, the same calculation should be adopted. There should also be common standards for which costs and charges are to be included in the calculation.

12. If so, what kinds of cost elements should such an EU standard include?

The Panel believes that all costs which the consumer is obliged to pay to obtain the mortgage should be included in the APR calculation. This should include, but not be limited to all interest charges; valuation fees; any fee associated with taking a higher value mortgage; broker's fees; any legal fees for setting up the mortgage; compulsory life and payment protection insurance and sealing fees.

13. The Commission welcomes views on the merits of providing separately information on all costs not specified in the APR, and on the presentation of the effects of the APR on concrete terms such as the cost per month or the overall cost of the loan.

The Panel believes that any charge which the consumer must pay to obtain the mortgage must be included in the APR calculation. Therefore the number of charges which should be shown separately should not be great. In the event that there are other charges levied, then these must be shown along with other pre-application disclosure. The Panel does not believe that consumers necessarily need to have an explanation of the effects of the APR on say monthly costs. What is needed is a simple means of making a comparison across different products and providers, and a way of illustrating the true cost of the mortgage. Concrete terms should certainly be included within the pre-application information but this does not necessarily have to link to the APR.

14. What are the implications of usury rules for market integration (including any relationship with products such as equity release and mortgage insurance)?

The Panel believes that consumers should be protected against firms imposing excessive interest rates and charges. The UK mortgage regime prohibits firms from imposing such charges. In terms of the imposition of interest rate caps, the Panel does not feel this is the best means of protecting consumers. The Panel feels that where an interest rate cap is imposed, there will be a tendency for firms to gravitate towards charging the cap itself, as opposed to a free and open market – through robust competition – finding an appropriate level of charging. Also, interest rate caps would have to be set at a limit which allowed firms to charge higher interest rates for higher risk loans. Such a higher cap would be inappropriate and unhelpful for mainstream consumers. The Panel feels the regulator should be given powers to intervene when it is judged that a firm is abusing its position of trust with consumers by charging excessive amount through high interest rates or other charges. The Panel does not see this as a product specific issue.

15. Should this issue rather be examined in a broader, non-mortgage specific context?

The Panel believes that decisions on interest rates and charging generally, within the mortgage context, include complex issues around funding models which would therefore not lend themselves to be examined in a wider context.

16. The Commission welcomes views on the merits of the standardisation of mortgage contracts, e.g. via the 26th regime.

The Panel does not have enough information to be able to judge if the 26th regime would be one means of facilitating greater mortgage market integration, and would welcome the opportunity to learn more about this initiative.

17. Should the Commission consider imposing on Member States an obligation to ensure the existence of such alternative means of redress in the mortgage credit area?

The Panel views the existence of the Financial Ombudsman Service in the UK as an invaluable means of ensuring that consumers can seek redress from financial services firms in the event of a complaint, without having to turn to costly formal legal action. The Panel feels the Commission should explore this option further.

18. The Commission welcomes views on ways to reinforce the credibility of existing alternative redress systems, particularly in the mortgage credit area.

See the answer to question 17 above.

19. What are the merits of a single EU standard for both valuations processes and valuers? What are the merits of Commission action to ensure mutual recognition of national valuation standards?

The Panel believes that ensuring a standard approach to valuations will be one means of facilitating EU mortgage integration. If the ability to lend across borders is one objective for integration, then lenders must be in a position to be able to rely on information provided about the security they are taking for the loan itself. Where numerous valuation standards apply this will be very difficult, and so the Panel supports greater integration and the possibility of Commission intervention.

20. The Commission seeks views on the following gradual approach to encourage improvements in forced sales procedures: to first collect information on cost and duration of these procedures in all member States and their effectiveness in protecting the interest of all involved, then present it in a regularly up-dated 'scoreboard' and, should this prove ineffective in the long run, consider putting forward more robust measures.

The Panel believes the UK regime presents a robust approach to forced sales procedures. This includes a requirement to treat consumers in arrears fairly, requirements for on-going information about arrears, and repossessing a property only where all other reasonable attempts to resolve the position have failed. The Panel does not view a policy of providing a 'scoreboard' will have any positive impact on consumer protection. Consumers facing a forced sale are at their most vulnerable and the Panel believes this in itself would warrant a stronger approach.

21. The Commission seeks information on similar or other tax issues to the cross-border provision of mortgages, which are likely to infringe the freedoms provided for by EU law.

The Panel would support any action by the Commission to ensure that all product providers are treated equally in every Member State if they choose to offer a cross-

border mortgage service. However, it does not have any further information which would be of use to the Commission.

22. Before making further input, the Commission would welcome input on all these (mortgage collateral) issues.

The Panel believes that in order for lenders to be comfortable with providing cross-border services, some means of ensuring more consistency in both the manner of registering charges, and consistency of standards will be necessary. Therefore the Panel sees this as one area where Commission intervention may in fact produce beneficial results.

23. The Commission intends to create an ad hoc stakeholders working group to examine the need for and the nature of action on the funding aspects (primary and secondary) of mortgage credit. It is interested to assess to what extent a pan-European market on mortgage funding can be promoted by market led initiatives, e.g. on documentation standards and model definitions to be used in cross-border funding activities.

The UK mortgage market benefits from flexibility of funding mechanisms which facilitates innovation within a very competitive market. The Panel agrees with those who argue that replicating this model across Europe may be the biggest single factor in helping to integrate the market. It would therefore urge the Commission to consider the option of intervention in order to facilitate greater funding flexibility for lenders operating across the EU.

24. The Commission is interested to receive views on whether mortgage lending should necessarily be an activity which is restricted to credit institutions or whether and under which conditions such activity could be performed by institutions which do not take deposits or repayable sums, and therefore do not fall within the scope of the EU definition of a credit institution and therefore of all related prudential issues.

The Panel does not believe that mortgage lending should be restricted to credit institutions. The UK market is populated by firms of many different types including centralised lenders whose source of funding is through the wholesale markets. The diversity within the UK market ensures that it is highly competitive and that the needs of a variety of consumers groups, including those in niche markets, are met. The Panel understands that the threshold conditions for authorisation as a mortgage lender include prudential requirements relating to capital, which are not based on the category of lender the firm falls into. In opening up markets across Europe to a diverse group of lenders the Panel believes that what is important is that such lenders are adequately capitalised in order that the appropriate levels of protection for customers of such firms is in place.