

Responsible Lending and Borrowing

Sharon Bowles, 3 September 2009

This is a many sided question but at its core it has to meet criteria of:

1. Fairness in the treatment of consumers
2. Prudentially sound lending

In the context of prudentially sound lending we can subdivide into that which is systemically relevant and that which is locally contained.

We all know that the current financial crisis has a substantial part of its origin in unsound lending. It may have taken sub-prime lending on a US scale, coupled with structured finance, to start a global crisis but we have certainly had housing bubbles at the heart of more local, national crises. So we should not dismiss systemic risk at the national level.

Almost immediately I have started to talk about mortgages, and this is surely a category on its own that, probably uniquely, has the scale to be systemic. It is also fixed in location and due to hugely differing land and property values, even within individual member states, does not have anything like a standard or competing price within a single market.

Add on to that the complexities of laws that surround land and property ownership, from conveyance to repossession, and it is not surprising to find little appetite for harmonisation of everything involved in purchase or cross border mortgages. Indeed also being a member of the legal affairs committee, I can say I have experience of the kinds of difficulties that we would face on that front.

I also recall attending meetings around the subject when the ECON Committee was preparing its mortgages report in the last Parliament and the lasting impression that I got from industry was 'more trouble than it is worth'.

However, there is attention being given to prudential regulation of financial institutions, and I think that is where big items like responsible lending for mortgages belongs.

It may be worth pointing out that we live in an upside-down world. There is no regulation that is as tough as frightened markets and banks having to recapitalise. Also, I have now been receiving concerns expressed that governments are encouraging irresponsible lending by pressurising banks to lend in circumstances that the banks would not wish to on a risk basis.

There are other lower credit items than mortgages, and they fall under the consumer credit directive. I will leave more comment on that to IMCO chair Malcolm Harbour this afternoon. Broadly I am inclined to say myself, let's see how that works out before doing more actual legislation. Certainly experience with the consumer credit directive after it comes into force and proper impact assessments would seem to be necessary for better regulation principles. However, that does not mean the information gathering process should not start – as is now being done.

Coming back again to my committee – and it may please you to know that Malcolm and I have discussed and are clear on our respective competences so there are not committee wars here – we have conduct of business rules and overlap with MiFID.

One area that is attracting my attention is the link between prudential regulation and conduct of business.

In the special committee of enquiry into the demise of Equitable Life, there were issues around inadequate information and indeed miss-selling, and one of the recommendations was for prudential regulation and conduct of business to be more joined up at the supervisory level. It does seem to me that the financial crisis, issues around over-lending and self certification (self-deception as the Commissioner called it) that have had to be tightened up, at least in the country I know best, serve to reinforce this point.

Therefore as we set about our improvements to the supervisory system to create a European layer, or however it end up, we do need to make sure that we do not in that process create bigger spaces between prudential and conduct of business regulation through which individuals can fall. There is not point in having many rules, poorly applied: far better to have simple rules, strongly supervised.

Some of those potential gaps may perhaps be avoided by investigation of ways to ensure better assessment of creditworthiness, by programs of financial education and by elimination of conflicts of interest in attaching bonus payments to sales volumes. Part of the solution may also be ensuring that staff are properly qualified, and that expertise exists both in selling and supervising. But somewhere it must all join up - and this means supervisors communicating, and at times taking a walk down the High Street to see what is in the shop window.

With regard to intermediaries, the European Parliament adopted a resolution on 5 June 2008 on Retail Financial Services in the Single Market, calling for a framework for intermediaries (I prefer to call them agents and brokers – that is something that the general public we wish to educate may relate more to). We asked that those offering services cross border should follow the principle of same business, same risk, same rules. That is a good principle, but its effectiveness can really only derive from good supervision, not a one size, tick box approach. Same business does not mean called the same thing, it means having the same mix of business type and risk. But I am now getting a bit back on IMCO ground because credit intermediaries features in the Consumer Credit Directive.

Then we come to treating consumers fairly.

I agree with the Commissioner that it is not transparent and it is not fair to deluge purchasers with excessive terms and conditions. What I have previously in other contexts called legal spam.

The ECON Committee has previously suggested there could be a harmonised system of consumer information. This would in fact be possible in some ways even for mortgages so I am pleased to hear that initiative. This was put forward in the committee's opinion to IMCO for their report on 'Protecting the consumer: improving consumer education and awareness' in September 2008.

Another point that the committee has previously made is for non-discriminatory cross-border access to credit data and fraud data for credit institutions and credit data agencies.

Looking at some of the questions, again I find overlap with where we are already taking action on prudential regulation. So the point of taking stock before piling on more proposals is relevant. Of course consultations such as this are part of 'taking stock', but cannot be the end of it.

Looking at loan-to-value – that is featuring in prudential considerations. But it has limitations as a blanket measure for credit. When it comes to mortgages there are land values and other local circumstances that can be relevant – some areas will always be more 'sound' than others and the wallet of purchasers more stretched. In my own constituency there are many high value houses owned by high earners – but they have less spare cash than those in some other places. I do not believe we can or should impose rules that do not take account of social and local circumstances.

If we look at purchase of other assets there are all kinds of different depreciation rates - or appreciation in some cases. So there needs to be an approach that fits cars and white goods which will be different to home improvements.

To conclude, I wish to make the point that there are dangers in presenting regulation in such a way that the consumer can take the attitude that 'all is safe because there are rules'. That runs counter to personal responsibility, which has to be at the heart of financial education and awareness. It also makes it easier for fraudsters. So we should install not blind trust but 'suspicious trust'.

At the same time, more and more people are becoming mobile within Europe, and are constantly being caught out by 'expecting' things to be the same as back home. My own postbag as an MEP is witness to that.