

GREEN PAPER – MORTGAGE CREDIT IN THE EU

Response by Cheltenham & Gloucester plc

Cheltenham & Gloucester plc (C&G) is a wholly owned subsidiary of Lloyds TSB Group plc and is one of the largest home mortgage providers in the UK. The Group holds approximately 9% of the outstanding balances in the UK home mortgage market. This reply is submitted by C&G on behalf of the Lloyds TSB Group and we welcome both the consultative approach adopted by the European Commission to this area and also the opportunity to comment.

Overall comments

We agree with paragraph 14 of the Green Paper, namely that the integration of the EU mortgage markets will involve dealing with four distinct but inter-related areas, namely consumer protection, legal issues, collateral issues and funding.

We also strongly support Commissioner McCreevy in as much as we suggest that intervention in the form of regulation should not be seen as inevitable. Indeed we would suggest regulation should only be introduced if a clear and unequivocal need has been established after a full cost benefit analysis has been carried out and all alternatives explored.

Looking across different mortgage markets in Europe today, it is clear there is a wide variety and diversity; we believe it is in the interest of consumers that any integration should retain this diversity rather than forcing standardisation across European member states. There is always a danger that a prescriptive regulatory regime would stifle innovation and cause product convergence.

So far as the London Economic report is concerned, we share the doubts expressed by the Council of Mortgage Lenders in its own response and in particular the comment that there appears to be no link between the measures suggested in the report and the benefits obtainable. We also consider that this report under-estimates the cost of implementing the regulatory regime in the UK.

We do, however, support the desire to encourage cross border activity although we consider there are a number of cultural barriers as well as legal and other barriers to be overcome.

The comments and proposals in the Green Paper apply equally to mortgages to finance the purchase of the property over which the security is created and to second or subsequent mortgages securing other types of loan.

The latter category of mortgages are for quite different purposes, usually of significantly lower amounts and for shorter periods than purchase money mortgages. We suggest, therefore, that a study needs to be undertaken as to whether these two types of loan should be treated in exactly the same way.

Finally, we do not believe that creating a uniform consumer protection regime across all member states would necessarily overcome the current cultural, legal and other barriers.

Answers to specific points

Information

We consider that the code of conduct should be allowed a further period of time to be tested and fully embedded. We do not believe it should be replaced by binding legislation unless this is found to be the only possible alternative after exhaustive investigation into all other possible measures. The code of conduct gives a flexible approach, which allows market development and will involve lower implementation costs, being principles based.

We agree that a careful balance is to be struck between information deficiency and information overload. Currently in the UK information given to customers prior to a sale is contained in a key facts illustration (KFI) which has been in use in the UK for 12 months. Anecdotal evidence suggests that the KFI contains too much information for consumers to absorb usefully. This carries an attendant risk that important information is overlooked by consumers.

We consider it unlikely that a specific point during the mortgage transaction can be found for giving information, which is common across all EU members. This suggests that a more flexible and principled based approach would be more effective, since guidance could be given which would allow consumers enough time to make informed decisions about their mortgages.

We consider that brokers and intermediaries should be subject to the same principles as lenders.

Advice.

Many consumers prefer to exercise their own choice over which products to choose. Furthermore, it is not appropriate in all cases for lenders to make a recommendation as to the suitability of mortgages. We do not, therefore, believe that it would be right to make the giving of advice compulsory to all consumers. In the UK lenders are free to decide whether or not they give advice to consumers and, conversely, consumers may choose whether they make their purchases on an advised basis or on a non advised basis.

Early Repayment

In the UK consumers have a legal right to repay loans before the end of the agreed term of the loan (usually 25 years). In some cases, however, lenders will incur costs in such cases (where, for example, funds are hedged or where other product features – such as initial discounts rely on consumers maintaining their loan over a given period of time). In these circumstances we consider that lenders should be able to recover legitimate costs where losses are incurred or where there is a reasonable expectation that such a loss will be incurred.

As always in such matters transparency is the key and lenders should be under an obligation to make it clear to consumers what the effect of early repayment would be.

Such a system operates in the UK where consumer choice is very wide and the number of available products is very high. Placing a restriction on the ability to recover such costs or compensation would restrict innovation and we therefore submit that fees and charges should not be capped but should, instead, be subject to some guiding principles. In the UK, for example, lenders are only entitled to recover what they can demonstrate as a genuine pre-estimate of the costs likely to be incurred in the early repayment.

Annual percentage rate

Consumers typically use APR's both for information purposes and in order to make comparisons. While we generally support the use of APR's in principle there are some difficulties in standardising calculation. We would support a standardised APR calculation, but suggest this should be defined on a comparatively narrow basis (including only the specific costs controlled or required by the lender).

In relation to costs not specified in the APR, although we are generally supportive of ensuring customers obtain all relevant information, there is the ever-present danger of information overload.

Interest rate variation

Subject to the overriding principle that we would support any moves designed to avoid extortionate credit bargains, such rules can often be too difficult to enforce. We would not, however, support a cap on interest rate variations since we consider this would be unduly restrictive on product innovation and the market generally.

Credit contract

We consider that achieving standardisation of contract terms would be very difficult to achieve although it may well be desirable. There is a danger that standardisation could limit product development, thus the subject should be approached with caution.

We would support the Commission's suggestion that it would undertake to explore the merits of a 26th regime.

Enforcement and redress

One of the obstacles identified by the forum group on mortgage credit was the wide diversity of the enforcement experience across member states. This is undoubtedly a barrier to cross border lending in some countries. Alternative means of redress are attractive in principle, but we consider that attempts to standardise such alternative means would be difficult to achieve given the diversity of legal regimes across member states.

Applicable law

Given that cross border lending could involve having to decide between three potential jurisdictions, the number of different options is very high. We support the view advanced by some members of the forum group that so far as the property related matters are concerned the law applicable in the country in which the property sits should apply (*lex rei site*) and that so far as the financial side of the transaction is concerned the parties should be free to choose which jurisdictions applies. Essentially this is support for the second approach identified by the commission, namely that the Treaty of Rome should be followed.

This would allow lenders to operate in foreign countries with greater ease.

Client credit worthiness

It is an essential part of the decision process that lenders should have access to relevant consumer data. We consider that non-discriminatory access would be an important move towards facilitating cross border lending.

Property valuation

Obtaining an accurate valuation is central to mortgage lending and confidence in those valuations is, again, an important step towards market integration. We would therefore support a single EU standard for valuation processes and valuers.

There has been some movement towards international standards, but this is not yet universal and we would therefore support action by the Commission to ensure mutual recognition of national valuation standards.

Forced sales procedures

Once again we support the view that uncertainty about certain aspects of forced sale procedures in different member states is a disincentive to mortgage providers wishing to lend on a cross border basis. The speed in which a defaulting loan can be enforced or recovered is a fundamental part of the mortgage lending decision and risk assessment so we would therefore generally support any measures intended to speed up procedures. We would, in particular, support the measure proposed by the Commission in monitoring standards in different member states.

Land registers

One of the principle barriers identified by the forum group was the different approach in different member states to registration. In some member states "hidden charges" exist which do not need to be registered on the land register. Also, different member states follow different procedures in terms of the way in which priority is both obtained and preserved.

The CML has suggested common protocols for the registration of charges and a shared understanding of what charges are registered: and we agree that this would be a significant improvement on the existing systems.

To that end we would support the EULIS project since the significant improvements made in the UK in land registration processes have given significant improvement to the flexibility of the mortgage and property market.

Euro mortgage

The concept of a euromortgage has long been a subject for discussion at varying different levels. There is little doubt that if, it was possible to develop such a security instrument, and it would significantly overcome many of the barriers identified by the forum group.

For this reason we would support a further assessment by the commission on the feasibility of this instrument.

Funding

We would generally support the proposals put in forward in the Green Paper.