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Your Ref., Your message dated	Our Ref., Official in charge	Extension	Date
	BSBV 65/2005 Dr. Rudorfer/Ob	3137	10 November 2005

Green Paper on Mortgage Credit

The Bank and Insurance Division of the Austrian Economic Chamber representing the interests of all Austrian banks and building and loan associations welcomes the opportunity to give its opinion on the considerations of the EU Commission laid down in the Green Paper on Mortgage Credit dated 19 July 2005:

Principal remarks:

We welcome the Commission's approach of broad consultation and support the principle of a "better regulation" emphasised by the Commission.

Therefore, we consider a diligent accounting of consequential costs and a related cost-benefit analysis a priority. A merely macro-economic analysis is definitely not sufficient.

All in all, there are doubts as to whether the need for further integration of the mortgage credit market justifies such a far-reaching change. (In this respect see the comments on the study carried out by London Economics).

Prior to implementing measures for further integration of the mortgage credit market far-reaching legislative steps in the field of civil law would definitely be required. The question arises to what extent, in particular in the case of mortgage credits, there is an actual demand on the part of the customers for cross-border financial services through the available possibilities. In view of the enormous expenses a thorough cost-benefit analysis is definitely indispensable.

Should this project be pursued, our primary request is the following:

In view of the different land register systems in the Member States it has to be ensured that legal certainty will be secured through relevant registration of all tasks relevant to real properties in the land register and that legalisation and validation of land register instruments will be facilitated.

Furthermore, it is particularly important that a prepayment will be maintained in the case of early repayment in violation of the contract.

London Economics Study

As a matter of principle, case-related model estimates should be assessed with caution because, as in this case, only little data on relevant periods of time is available and, thus, it is not possible to exactly verify assumptions made.

The surge in growth of 0.89% of GDP expected by London Economics is not comprehensible in the way it is presented.

This is, above all, due to the fact that in the case of a model calculation the fiction of a "perfect market" is assumed, which is impossible to achieve in reality.

After all, this would mean that every market participant is provided with all product information at all times and is able to recognise the product which is most beneficial for him/her. But that is not the case. In addition, decision-making criteria, such as personal preferences, would have to be taken into account, which cannot be defined by abstract parameters.

London Economics does not take account of the costs that would arise due to a harmonisation of the legal framework conditions. The Commission itself states in the Green Paper that in case of an integration of the mortgage credit market numerous interactions with the Member States' legal, housing and social policies exist and "fears" that a large number of cross-border transactions could add to the price of mortgage credits.

Also the consequences for consumers in the investment area which result from a reduction of the interest rate level in the financing sector have to be taken into consideration.

Green Paper on Mortgage Credit

In connection with the Green Paper we would first of all like to express the following request:

Harmonisation of the different land register systems in the Member States is necessary in order to achieve a harmonised mortgage credit market. In this connection, the necessary legal certainty regarding registration of circumstances relevant to real properties in the land register would have to be ensured, which has not been achieved yet to the desirable extent. We are, in principle, in favour of easing accessoriness for liens on real property.

(16):

Should the Code of Conduct be replaced by binding legislation or remain voluntary?

Answer: The Code of Conduct should remain voluntary.

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

Answer: The objective can only be that comparable conditions are guaranteed in cross-border lending and that the borrower, irrespective of where s/he takes out a loan in the EU, will be informed about the essential provisions of the credit contract affecting his/her interests. In addition, it should be ensured that the consumer is provided with the possibility of comparing the terms of the loan (actual interest rate).

Question: *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 State' traditions and legislations?*

Answer: It should make no difference whether the consumer is informed about the essential provisions of the credit contract already on the occasion of an initial meeting or at a later point in time, e.g. when the bank's binding credit offer is handed over.

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?

Answer: The information provision regime contained in the draft directive should not only apply to banks but also to brokers and other third parties involved in loan brokerage. In order to ensure competitive equality it is necessary that the standards applying to banks also apply to financial intermediaries.

Advice Provision and Credit Intermediation (18):

Question: *Should the provision of advice to the borrower be made compulsory or be a matter of choice?*

Answer: The provision of advice to the borrower is an essential part of a credit transaction *per se*. However, it is not necessary to provide for compulsory regulations in an EU Directive. It would definitely be sufficient for the provision of advice to be a matter of choice.

In this respect it should to be noted that also the future Consumer Credit Directive (CCD) will change from the envisaged obligation of the lender to provide advice to a duty of the lender to inform. The same should apply to mortgage credits.

Question: *Should conditions be applied to any advice actually provided, whether under a duty or by 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)?*

Answer: Advance disclosure of advisory fees, if any, and of the adviser's role makes sense. Recording of the content of the advice provided on a durable medium (paper/data carrier) has to be rejected for cost reasons alone.

Early Repayment (22)

Question: *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 a compensation in the form of fees?*

Answer:

If the customer had a legally unrestricted right to early repayment at any time, of which s/he would make use, in particular, in case of more favourable interest rates, the long-term calculation which is currently made in the field of mortgage credits would become impossible. The concept of more favourable credit interest rates based on the long term of mortgage credits would be questioned in principle. Due to the possibility of termination at any time an increase in credit interest rates would be inevitable in order to adequately compensate for this incalculable risk.

A prepayment indemnity has to be provided for. The amount of such prepayment indemnity is based on the costs incurred by the mortgage lender due to early repayment. Since such costs are closely related to the current market interest rate level at the time of early repayment, a statutory cap is not expedient. An examination as to the content of agreed/demanded prepayment indemnity in compliance with the civil-law regulations on void contractual provisions or provisions which are *contra bonos mores* that are applicable in the individual Member States is sufficient.

In this context it seems to be significant that the cost factors of long-term transactions are to be allocated differently than in case of short-term transactions, namely irrespective of whether fixed or variable interest rates apply. Erroneously, debates in this context are mostly held in connection with fixed interest rates.

Question: 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?

Answer: A possibility of repayment prior to expiration of the fixed period must always be linked to a regulation on early repayment which ensures that the bank will not have to bear the (partial) loss resulting from early repayment. Also in this case we are not in favour of caps on the amount of such repayment indemnity.

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

Answer: If the Commission adheres to its claim for early repayment, then the possibility of early repayment should be included in the mortgage credit contract.

Annual Percentage Rate (24)

Question: What is the purpose of an APR? Information? Comparison? Both?

Answer: Both.

The formula for calculation of the actual annual percentage rate follows precise mathematical and economic logic and was used by the legislator as a criterion for information, transparency and comparability. However, practice shows that a consumer who is no expert in mathematics can do nothing but accept the figure. As regards comparability of one "actual annual percentage rate" with those of other offers, the figures are only comparable if the providers offer exactly the same product and have used the same calculation methods. Thus, usefulness of the actual annual percentage rate has to be questioned.

Question: Should there be an EU standard covering both the calculation method and the costs elements?

Answer: In the past the banking industry had to bear high costs due to extensive adaptations in the computing centres already when the different calculation methods were introduced. It is not acceptable that now such costs will have to be incurred again by the banking industry due to a harmonisation of methods.

Question: 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 in concrete terms such as the cost per month or the overall cost of the loan.

Answer: Third-party costs should be disclosed.

It is not possible to state all fees related to the mortgage credit. This applies, in particular, to costs owed to third parties (e.g. notary, land register courts, insurance companies, etc.).

All costs which are not included in the actual annual percentage rate should be stated separately. As regards the effects of the actual annual percentage rate in actual figures it is sufficient to express the same in the (e.g. monthly) repayment instalment and in the overall costs of the loan. However, also this issue should be handled in the same way as consumer credits.

Usury Rules and Interest Rate Variation (26)

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

Answer: According to Section 879 Austrian General Civil Code [ABGB] usury interest rates are anyhow prohibited by law in Austria. We do not consider any further statutory regulation necessary.

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

Answer: This issue should be discussed in a broad context.

(28)

Question: Do such restrictions hinder market integration?

Question: What impact can they have on the development of particular products such as equity release products?

Answer: Like legally binding interest rate caps also restrictions on compound interest rates do not hinder the market integration aimed at.

There will be no impact on the development of equity release products.

Credit Contract (29)

Question: The Commission welcomes views on whether the merits of the standardisation of mortgage contracts (e.g. via a 26th regime instrument) are considered desirable.

Answer: No. As already stated in the Green Paper on the Financial Services Policy 2005 - 2010, we believe that there is no need for a discussion about the 26th regime instrument at present.

A standardisation of mortgage credits does not meet the specific requirements of an individual case. Product variety would be lost and consumer options would be reduced. Product variety can be secured by means of the principle of mutual recognition so that banks will be able to offer their mortgage credits which have been developed for the domestic market also abroad with no changes, if possible. In this connection, of course, there has to be the right to choose the applicable law.

Enforcement and Redress (30)

Question: 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?

Answer:

In general, and not only to mortgage credits, the following applies:

Due to the different means of redress in the individual Member States mandatory alternative means of redress are not necessary.

However, if this proposal should be pursued despite principal scepticism we are in support of an integration into the existing ombudsman system.

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

Answer: See our answer to the previous question.

Client Credit-Worthiness (36)

Question: Following the same approach as for consumer credit, the Commission considers that the priority could be to ensure cross-border access to databases on a non-discriminatory basis. It welcomes comments on this.

Answer: We agree. However, issues of data protection law will have to be clarified.

While, in principle, welcoming cross-border access to databases for all lenders on equal terms, we consider the development of new database structures not to be useful because such new developments may be connected with high costs which, ultimately, would also have an impact on the consumer.

Property Valuation (38)

Question: What are the merits of a single EU standard, for both valuation processes and valuers?

Answer: We consider it necessary that the respective bank will remain free to select the valuation standard it wants to use.

It seems to be of essential importance that every bank should have the right to accept uniform valuations, if available. However, there should be no obligation to do so because, ultimately, it has to be the responsibility of each lender to choose the valuation methods or criteria he wants to use for valuation of the collateral. However, the decision made by a foreign valuer according to his/her valuation standard must not be binding on the foreign bank granting the loan. The decision how a real property or other collateral is to be valued must always be the responsibility of the lender. Related prudential rules are being stipulated in the Basel II regulations anyhow.

Question: What are the merits of Commission action to ensure mutual recognition of national valuation standards?

Answer: See our answer to the previous question.

Forced Sales Procedures (42)

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

Answer: We are, in principle, in favour of a gradual approach of the Commission to collect information on the individual forced sales procedures in Member States.

We welcome the Commission's intention to provide all involved with information on the cost and duration of forced sales procedures in the Member States and to update the same on a regular basis. However, a special regulation for mortgage credits does not seem to be useful.

Taxes (43)

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

Answer: In this respect, we take the liberty of mentioning the credit contract fee, which only exists in Austria, and the fee for registration in the Land Register.

We consider the Commission's approach to eliminate tax obstacles to the cross-border provision of mortgage credits worthy of support.

Land Registers (46)

Question: Before making further assessments, the Commission would welcome input on all these issues.

Answer: As already explained in the forum group report, we welcome those issues with respect to land registers which ensure that, on the one hand, legal certainty will be ensured by registration of all circumstances relevant to real properties in the land register and, in addition, that legalisation and validation of land register instruments will be facilitated. We also welcome the fact that in future it is intended to ease the accessoriness for liens on real property existing in some countries.

As with respect to databases we are of the opinion that cross-border access to land registers should be possible for all lenders on equal conditions.

Euromortgage (48)

Question: The Commission invites views on the feasibility and desirability of the Euromortgage. It will, in any event, await the outcome of ongoing initiatives to inform its assessment of this issue.

Answer: It is clear that the Euromortgage will constitute a future legal form which will still have to overcome obstacles on its way to realisation. The Euromortgage should in any case be designed with the objective of creating a mortgage the secured claim of which may be exchanged.

We support the creation of a Euromortgage instrument provided that it is ensured that the title will then be registered without problems also in the respective lien register of the Member States. However, it will have to be checked in advance whether this is in principle possible and, if so, whether and/or what amendments to national land register law will be required in order to enable adequate implementation.

Funding of Mortgage Credit (51)

Question: The Commission intends to create an ad hoc stakeholders working group to examine the need for and nature of action on the funding aspects (primary and secondary) of mortgage credit.

The Commission's intention to create a working group to examine the need for and nature of action in the area of mortgage credits in the primary and secondary market are, in principle, supported.

Question: It is interested to assess to what extent a pan-European market in 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.

Answer: Rather, the aspect of transferability of mortgage credits is of importance.

(52)

Question: In this respect, 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 rules.

Answer: We expressly reject any extension of the right to grant mortgage credits to institutions which do not take deposits or repayable sums, i.e., mortgage lending must remain an activity restricted to banks.

Mortgage credit contracts are long-term contracts. Usually, an EU citizen takes out such a loan only once, to finance his/her home, and repays it in small instalments throughout his/her active working life. Accordingly, continuity and existence of the funding lender throughout the term of the loan are of great importance to the borrower because the credit facility which is open throughout the entire term and continued existence of the flat/house will be secured in this way.

Yours sincerely,

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