

# Mortgage Credit in the EU

## Response to the European Commission's Green Paper

For further information please contact:

Jill Craig  
Head of Policy – Europe  
[jcraig@rics.org](mailto:jcraig@rics.org)

1. RICS welcomes this opportunity to comment on the Commission's green paper on mortgage credit, which we recognise as a response to the report and recommendations of the Forum Group of which we were able to be part.
2. RICS (Royal Institution of Chartered Surveyors) is the largest organisation for professionals in property worldwide. With 120 000 members, RICS is a leading source of property related knowledge, providing independent, impartial advice to governments and global organisations. Asset valuation is a key skill which underlies the services provided by a large number of these members.
3. We have limited our comments to the property-related issues affecting home loans.
4. Equity in a home can represent a significant asset which may have the potential to be used to finance consumption or, more long-term, to bring financial security in retirement. A more efficient and competitive mortgage market could also facilitate labour mobility which in turn would help the EU to achieve its Lisbon economic goals.
5. It is important to put the discussion on mortgage market integration into context. The differences in housing markets and home ownership rates across Europe reflect differing cultural factors as well as attitudes towards and treatments of, for example, regulation, taxation policy, government intervention, new housing construction and other changes made in the private and social rented sectors of the market. All of these factors are interlinked.

### **Summary and priorities**

RICS welcomes the Commission's extensive consultative process on this important dossier and hopes that the doors will continue to be open to stakeholders throughout any further phases of policy development. More specifically, however, we urge the Commission to continue its **commitment to better regulation** by ensuring that any measures it considers proposing undergo an individual and rigorous impact assessment in advance. Any action taken should reflect a clear business case.

The demand for direct cross-border sales is clearly still very low, at a widely reported below 1% of the overall residential mortgage credit activity. The indications are that these loans are predominantly granted to finance the purchase of retirement and/or second homes. While there is a boom in this sector – and a chapter of the *RICS European Housing Review 2005* (see <http://www.rics.org/ehr>) looks specifically at the reasons for this – it will for the foreseeable future remain a niche market. We would therefore question the **cost/benefit justification** for regulatory action in the area of cross-border shopping by consumers.

We do, however, believe that considerable progress towards an integrated mortgage market in Europe can be achieved through **market-led measures** which are designed to increase lender confidence through mutual understanding and cooperation cross-border. This is particularly true with regard to unrestricted cross-border access to information – such as property valuation, land registry, credit data (positive and negative) and foreclosure information – required by a lender in order to carry out a responsible risk assessment.

European funding markets are another potential area for greater integration. While the Commission should play an active role in encouraging this and in helping to promote common standards across the EU, a **pan-European secondary market** should be achievable through non-regulatory market initiatives.

Property valuation is central to mortgage transactions and EU mortgage lending is increasingly funded through international wholesale markets. It is essential that the Commission encourages measures which deliver global transparency and comparability, such as the **use of international property valuation standards**, to promote European markets to the global investors identified in the green paper.

RICS therefore sets out the **following priorities** for further Commission work:

- **To explore with market participants the development of a pan-European secondary mortgage funding market which would increase transparency, comparability and efficiency and so reduce costs to consumers.**
- **To encourage international standards of property valuation that are widely recognised, understood and trusted by valuers, lenders, rating agencies and investors globally.**
- **To encourage the continuing development of EULIS into a greater number of countries as a means to boost transparency and trust in cross-border activity.**

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## **6. Specific comments**

Our more detailed comments are arranged below in the order in which the issues are discussed in the green paper.

### **Advice and Credit intermediation**

7. Mortgages are complex and high value products. It is therefore essential that information given to consumers, who will largely be uninformed, is accessible and kept to a manageable level.

8. There is, however, a need for a clear distinction between the provision of information to a consumer and the provision of advice, perhaps better labelled “recommendations” to a consumer. Advice/recommendations, when given, should be of a high quality, transparent and reliable, but not compulsory.

9. Given the importance that consumers place on face-to-face contact in purchasing a mortgage, lenders may increasingly choose intermediaries, such as mortgage brokers and agents, real estate and financial professionals, as a channel through which they could expand their reach cross-border, without having to set up a costly branch network. The Commission would therefore be justified in considering the regulatory issues regarding the scope and conduct of intermediaries and we note the Commission’s Green Paper on

Financial Services Policy (2005-2010) has highlighted credit intermediation as an area for further work.

10. As a self-regulating professional body, RICS has significant experience in this field. Should the Commission decide to move forward with any regulatory measures on mortgage credit intermediaries or at a more horizontal level on credit intermediation, we would be very keen to offer our input.

11. We also urge the Commission not to repeat the experience of the directive on insurance intermediation (2002/92/EC) which had application far beyond both those sectors which the Commission consulted and those it was intended to regulate.

### **Property valuation**

12. Property is a primary form of collateral for bank lending and it is therefore vital that financial institutions have the benefit of reliable valuation of the property assets they use as security in the mortgage transaction. Differences in the way a property is valued affect the nature, the funding and the prudential rules applicable to the credit.

13. Because of the local nature of most individual mortgage credit decisions in Europe today, property valuation is still based on national custom and law. Indeed, in some countries property valuation is not regulated at all, while, as the London Economics study points out, there are other cases of national standards being created for specific products.

14. In line with our thinking on land registers and on credit data, we do not see an overwhelming need to intervene in valuation at national level. The only exceptions would be:

- in markets where there are restrictive practices which prevent well qualified valuers from other countries from operating; and
- to encourage higher educational standards for valuers where necessary.

15. However, there is clearly a need to enhance confidence in both the valuer and the valuation report in cross-border situations. Lenders and investors could more easily compare portfolios in different countries if property was valued to consistent standards. Lenders operating in a number of countries may also benefit from an enhanced level of standardisation of systems and products which consistent standards would bring.

16. It is unrealistic to expect lenders and investors to understand and use, i.e. mutually recognise, national valuation standards from other countries as these can differ greatly from those which the lender recognises and needs to make his own lending decision. It would be more appropriate in cross-border situations for the valuation to be carried out according to internationally recognised standards which are neutral and so more easily transferable.

17. Internationally agreed standards exist – International Valuation Standards developed by the International Valuation Standards Committee (IVSC) of which RICS is a key supporter; and European Valuation Standards developed by TEGoVA.

18. The new Basel Capital Accord (Basel II) and the EU's revised Capital Requirements Directive reflect the need to achieve maximum consistency between the prudential

framework and international standards in accounting and valuation. Without this, there can be no level playing field for banks worldwide.

19. More importantly, when the Commission rejected the idea of introducing regional standards at European level in the financial reporting field by adopting the Regulation (1606/2002) on international accounting standards, it recognised the need for the EU to play an enhanced role on the global financial stage. RICS strongly believes that these arguments are equally valid for property valuation standards and that the Commission should put its weight behind a high quality set of international standards. Moreover, just as with IFRS, International Valuation Standards would benefit from even greater European level input at development stage.

20. We note the Commission's intention to look more closely at the funding markets as a way forward for European integration and support this move (see below). It is imperative to the success of these markets that issuers, rating agencies and investors have confidence in the value of the underlying assets they are trading in. Only International Valuation Standards have the capacity to deliver the levels of transparency and comparability that will be key here.

#### **Forced sales procedures**

21. The forced sale procedure is recognised as critical to the effectiveness of the mortgage collateral. It is fundamental to the risk strategy and pricing for the lender, and complex and lengthy foreclosure procedures will act as a deterrent for those who are considering operating cross-border in certain markets.

22. Forced sales procedures are affected by a number of different national factors and so direct Commission intervention in this area, such as EU-wide harmonisation, would be undesirable and in any event extremely difficult.

23. However, we support the Forum Group's recommendation that the Commission produce a regularly updated scoreboard of the cost and duration of these procedures in all Member States, initially to increase transparency but also gradually to encourage improvements in those countries which perform least efficiently.

24. The Commission should ensure for the sake of usefulness and effectiveness that the data collected and presented are comparable.

#### **Land registers/EULIS**

25. Land registry information is another key element in any lending transaction where real estate is used as mortgage collateral. Legal certainty with regard to the ownership rights of the property is essential for any lender and must be equally achievable in cross-border situations as for national market players.

26. RICS is a supporter of the EULIS initiative which enhances access to and understanding of land registry information between owners and controllers of registers without requiring national level changes of law.

27. It is encouraging to see that the number of participating countries is set to expand beyond the original partners in the pilot project – a sign of the initiative’s usefulness and potential added value to the market. It is our view that the further development of EULIS should be driven by this market. Indeed we understand that EULIS is developing a funding model based on a user fee. However, the Commission should continue to encourage this initiative, not least to maximise its initial funding investment in the project, but also as an example of best practice in cross-border cooperation.

#### **Funding of mortgage credit**

28. Progress in the area of pan-European markets should be considered by the Commission as a priority for action. However, this is another area where the market could drive this forward.

29. RICS agrees with the analysis of the Forum Group report that cross-border market entry could be considerably enhanced by developing a pan-European capital market. Incentives for European cross-border collateral pooling should be encouraged by Commission action, in recognition of the risk mitigation effect of a pan-European mortgage portfolio for capital and investment regulations of investors. Better risk diversification would also result in lower prices for consumers and allow mortgage lending to new groups of consumers.

30. It is important that investors and rating agencies can be confident of the basis of the valuation of the properties being traded. The transparency and comparability required by investors for trading pooled mortgage loans are likely to lead to a degree of standardisation in definitions, such as of market value, and in mortgage products across the EU. This could best be achieved through the use of International Valuation Standards.

31. We welcome the Commission’s intention to create a stakeholder working group on the funding aspects of mortgage credit and urge the Commission to consult widely on all aspects of this business to business environment.

**28 November 2005**