

Impact Assessment for the proposal for a directive on credit agreements relating to residential property

Presentation to the IMCO
Committee, European Parliament

Extensive consultations over several years

- White Paper on EU Mortgage Credit Markets (2007);
- Consultation on responsible lending and borrowing;
- Studies: credit intermediaries, non-credit institutions, cost-benefit analysis;
- Expert Groups: credit histories, mortgage dialogue;
- Impact assessment.

Economic context

- **Increased consumer indebtedness**
 - In 2008, 16% of people reported difficulties in paying bills and 10% of households reported arrears;
 - Since 2007, an increase in default rates in all Member States and a rise in foreclosures in a number of Member States.
- **Irresponsible lending and borrowing**
 - Foreign exchange lending;
 - No income verification;
 - High LTV and LTI ratio.

Drivers

- Market failures:
 - Asymmetric information;
 - Misaligned incentives.
- Regulatory failures:
 - Regulatory gaps;
 - Inappropriate regulation.
- Other drivers:
 - Low levels of financial literacy;
 - Mortgage financing structures;
 - Other unforeseeable factors, e.g. death, divorce.

Specific problems

- Non-comparable, unbalanced, incomplete and unclear advertising;
- Insufficient, untimely, complex, non-comparable and unclear pre-contractual information;
- Provision of inappropriate advice;
- Inadequate suitability and creditworthiness assessments;
- Unsuitable and inconsistent early repayment option
- Ineffective, inconsistent or non-existent registration, authorisation and supervision regimes for credit intermediaries and non-credit institution lenders.

Consequences

- Significant spill-over effects on the wider economy:
- Risk of consumer detriment:
- Low cross-border activity
- Unlevel playing field between market actors and products;
- Low customer mobility.

=> Estimated size of problem: **EUR 17.8 billion per annum** (value of mortgage defaults each year).

Objectives

- To create an efficient and competitive single market with a high level of consumer protection by fostering:
 - Consumer confidence;
 - Customer mobility;
 - Cross-border activity of creditors and credit intermediaries;
 - A level playing field.
- Promote financial stability by ensuring that mortgage markets operate responsibly.

Need for EU action

- Prevent the pursuit of business or raise the cost of doing business in another Member State;
- Risks of financial contagion: the effects of irresponsible lending in one country can quickly spread beyond national borders;
- Action from Member States alone is likely to result in different sets of rules, which may undermine or create new obstacles to the functioning of the internal market.

Policy Options

- **Do nothing**
- **Application of the CCD rules:**
 - Advertising and marketing, explanations, creditworthiness, non-discriminatory access to databases.
- **Principles based rule:**
 - Timing of ESIS, advice standards, remuneration, suitability, responsible borrowing, authorisation + registration + supervision of intermediaries and non-banks.
- **Specific rules:**
 - Advertising and marketing, timing of ESIS, remuneration, deny credit, content of databases, warning if not suitable, authorisation + registration + supervision of intermediaries and non-banks.
- **Improve content and format of ESIS**
- **Harmonise APRC:**
 - Narrow, CCD, broad.
- **Requirement to provide advice**
- **Introduction of passport for intermediaries, non-banks**

Methodology: Costs

- One-off costs to creditors + credit intermediaries
 - Staff training;
 - Investment in IT and systems modifications;
- Recurring costs to creditors + credit intermediaries
 - Compliance costs;
 - Additional time required to do certain things, e.g. provide explanations.
- One-off costs to Member States, e.g.:
 - transposing and introducing new rules;
 - establishing a register for intermediaries/non-credit institutions
- Recurring costs to Member States, e.g.:
 - Supervision;
 - authorisation procedures.
- Reduced access to credit for consumers

Methodology: Benefits

- **Reduction in defaults;**
 - Increased financial stability;
 - Increased customer mobility;
 - Increased competition;
 - More business opportunities.
- **Cost/Benefit Quantification:**
 - Benefits to society: EUR 1272-1931 million
 - One off costs (Member States and industry): EUR 383 to 622 million;
 - Ongoing costs (Member States and industry): EUR 268 – 330 million.
 - NB: other potential benefits such as cross-border

Proportionality

- Appropriate analysis of the policy options:
 - E.g. passport for non-banks.
- Choosing the most appropriate instrument:
 - Self-regulation;
 - Recommendation;
 - Directive;
 - Regulation.
- Level of harmonisation: targeted.

Conclusion

- **Preferred instrument:** Directive
- **Content:**
 - Specific rules on advertising;
 - Revised ESIS (content and format), harmonised APRC along lines of CCD, specific deadline for providing ESIS.
 - Obligation to provide pre-contractual information.
 - Requirement to give explanations and principles for provision of advice and remuneration.
 - Requirement to assess creditworthiness and deny credit if result negative.
 - Requirement to assess suitability and warn if product unsuitable.
 - Non-discriminatory access to databases and requirement for consumers to provide information.
 - Principles based rules on authorisation, registration and supervision of intermediaries and non-banks, and a passport for credit intermediaries.
- **In line with principles of subsidiarity and proportionality.**