



HOUSE OF LORDS

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Inquiry on

RESIDENTIAL PROPERTY DIRECTIVE

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Witnesses: Jackie Bennett, Nigel Terrington and Vera Cottrell

Annik Lambert

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Members present:

Lord Harrison (Chairman)
Lord Hamilton of Epsom
Lord Haskins
Baroness Hooper
Lord Jordan
Lord Kerr
Baroness Maddock
Lord Marlesford
Lord Moser
Lord Vallance of Tummel
Lord Woolmer of Leeds

Examination of Witnesses

Witnesses: **Jackie Bennett**, Head of Policy, Council of Mortgage Lenders, **Nigel Terrington**, Chief Executive, Paragon Group of Companies, and **Vera Cottrell**, Principal Policy Advisor, Which?, gave evidence.

Q1 The Chairman: Good morning, colleagues, and welcome to this our first look at the Residential Property Directive. I am particularly pleased to see our three witnesses here this morning for the first session we are having on this issue, on which we hope to publish a one-off paper. Could I remind you, as witnesses, that it would be very helpful if you say in your opening remarks—and if you want to make an opening statement that is fine—who you are and where you come from? We will have a transcript of the evidence session that will be sent to you, so please do correct that and send it back to us. Indeed, if you have better and further thoughts after you leave the session, which always happens, we would be most grateful if you would jot them down and write to us, as we are very keen to ensure that we get all the knowledge we can on this issue. It is webcast, so I just remind my colleagues about comments sotto voce, which will be picked up, especially in the interim between now and meeting Annik Lambert, who is coming from Brussels this morning as well. Would you

please all state when you speak whether you have any interests that should be declared for the Committee? My last word to the witnesses is this: as we have a relatively short amount of time, would you be kind enough, if you hear an answer from one of your colleagues that is broadly the same as the one you were intending to give, just to say you agree? Brevity is not only the soul of wit but actually also helps move matters along quicker.

Thanks very much indeed for coming. Would any of you like to make an opening statement? If not, let me start then and ask this: colleagues, what is your overall assessment of the Commission's proposal for a directive on credit agreements relating to residential property? Would it succeed in achieving the Commission's aim of creating a responsible, efficient and competitive European mortgage market? I wonder whether you could just jog my memory. When the euro first came in some 10 years ago, unless I am wrong, there was a bit of a flurry, was there not, of euro-denominated mortgages that were available in this country—whatever happened to them? Who would like to start? Mr Terrington?

Nigel Terrington: Yes, happy to do so. Just dealing with that last one first, there is always an attraction to foreign currency denominated mortgages where there is a lower interest rate in that particular currency. Of course, you can get the benefit of lower monthly mortgage payments but what you suffer is the risk of adverse movement in the foreign exchange market. Ultimately, you have to repay the loan in the currency in which the mortgage is denominated, and you can end up paying back substantially more than you have benefitted. I think it is a dangerous practice and is probably best avoided by all but the most professional of individuals.

Vera Cottrell: I have to say that we have been informed by colleagues in other member states, especially Romania and Hungary, where these foreign currency loans are still very common, they have a very, very detrimental effect on consumers and cause severe financial

hardship for a lot of consumers. We would share the view that they are never a particularly good idea.

I would also like to come back to our overall view of the directive. We are of the view that in the UK we already have a quite well-regulated mortgage market, especially when it comes to pre-contractual information and the regulation of mortgage intermediaries; however, we can see there are some benefits to having a directive at European level, as long as the directive is implemented on a minimum harmonisation basis.

The Chairman: I am so sorry, Ms Cottrell, I think some of our colleagues are having difficulty hearing you, I do not know how close you can get to the microphone but do speak up. We will take the ear trumpets out of our ears if it is too loud.

Vera Cottrell: I will try to be more audible in future. Should I repeat what I said before?

The Chairman: Yes, please.

Vera Cottrell: In terms of our overall view of the directive, we think that we already have a quite well-regulated mortgage market in the UK. Especially, the requirements when it comes to pre-contractual information are very detailed in the UK and also when it comes to the regulation of mortgage intermediaries. However, we are aware that there are consumer groups in other member states who were really hoping for a mortgage directorate, and we can see some benefits of having a piece of legislation at European level, as long as it is implemented on a minimum harmonisation basis. I think it will not harm UK consumers.

Jackie Bennett: I think I would agree with virtually all of what has been said. It is true, the proposals do reflect the way the FSA regulates mortgages in the UK, but we believe it is unrealistic to create a single rulebook for Europe because mortgage markets are different right across Europe. If the directive is kept at a principles-based level, as Vera was saying, then we are able to implement it in the UK without detriment, but there are a number of

areas that I think we are all concerned about as the directive stands at the moment. I am sure we will come on to those.

The Chairman: Mr Terrington, did you have a full opportunity to answer the first question?

Nigel Terrington: Yes, I dealt with one aspect. I completely endorse those views; it must be kept at a high and thematic level rather than dealing with specifics.

Q2 Lord Hamilton of Epsom: Could I just have a supplementary, Mr Terrington? You went on at the beginning about the problems of foreign exchange risk if a mortgage was taken out in euros from, say, Germany, taking advantage of the very low interest rates in Germany. But there are financial instruments where you could offset that; you could hedge that risk, couldn't you? You could actually pay marginally more and have no foreign exchange risk.

Nigel Terrington: Yes, it is entirely possible to hedge out your foreign exchange risk. Usually the way the efficiencies of markets work is such that the gain you will make on your lower mortgage rate interest payments that you are making will be equally offset by the premium you would have to pay on the hedge instrument. It is because these markets are all working. If they were not perfectly symmetrical in their function, then you would have very bright chaps in the City of London making arbitrage gains from one market to another in substantial size, not £100,000 or £200,000 at a time.

Q3 Lord Hamilton of Epsom: I will come to my main question. I ought to just declare an interest that my wife and I have bought-to-let properties. Is the proposal a necessary instrument to help protect consumers from irresponsible lending and to prevent over-indebtedness? Or is it in fact an attempt to design a European solution to a US problem?

Jackie Bennett: We do not think, in Europe, that the banking crisis was precipitated by irresponsible mortgage lending as it was in the United States. We believe responsible lending is well established in the UK. That is not to say that we did not have our problems, but we do not believe it was of the same order as was in the United States. The subprime market in the UK was only ever around 5% to 6% of the market, not the 25% that it was in the United States. We did not have the same types of products that they had in the United States either in terms of having the adjustable-rate mortgages that could increase without checking what the affordability was for the individual after that rate went back up.

The Commission has been thinking about a mortgage directive for a number of years; they already have one for consumer credit, and they have been thinking about this for a number of years. I think, as Vera was intimating in response to the previous question, there are a number of states in Europe that do not have the level of mortgage regulation that we have in the UK. Again, if there is a minimum level of standards across Europe that each country can then interpret in its own way, I think that is a broader benefit to all.

The Chairman: Before the other two answer, Lord Haskins has a supplementary on this one.

Q4 Lord Haskins: Excuse my ignorance, but on that assumption has there not been a serious default of mortgage borrowers in this country in the last couple of years? The figure is not a serious figure?

Jackie Bennett: The figure has increased but nowhere near to the extent of after the previous recession. It is very difficult to get comparable arrears rates across Europe, but certainly we do not have the rates that there are in places like Spain, for example, where the rates are much higher. We can send you what information there is. As I say, it is very difficult to compare.

Lord Haskins: It is quite interesting to get that. Ireland is bad—very bad. Spain is bad.

The Chairman: I am just going to ask the other two witnesses to reply, Lord Hamilton; I will come back to you. Ms Cottrell?

Vera Cottrell: As I mentioned earlier, many consumer groups across Europe actually wanted a mortgage directive. The Commission has been working on this for many years. I suppose the economic crisis was the final push that convinced the Commission that a directive was necessary. I would like to pick up on the point that there are several member states where we see a very, very high arrears rate. Spain is a particularly bad case. We have also seen an increase in this country. There has been at least some lending that was not maybe as responsible as it should have been. We are particularly concerned by the very high LTV loans that were handed out just a few years ago, where it was quite easy to get a 125% mortgage. Consumers that have a 100%-plus mortgage at the moment, a very high LTV, are really struggling to find a new mortgage product and are pretty much stuck with their existing lenders. There is some benefit in doing something on this issue.

The Chairman: Mr Terrington, do you want to reply to Lord Haskell or shall I bring Lord Hamilton back?

Nigel Terrington: Yes, I will respond to that particular one. In terms of the arrears levels, UK mortgage arrears are currently standing at around 2%; that is around one-third of the level that they were in the early 1990s, when the country went through quite a severe recession at that time. Clearly, I think it has benefitted from the fact that we have extraordinarily low interest rates at present and maybe for the foreseeable future as well. I think I will also differentiate in terms of the products that are there. Lord Hamilton referred to the buy-to-let as a particular product. There is a perception that buy-to-let is a high-risk product. I can tell you that the arrears for buy-to-let are almost identical for

normal mortgages. There is no evidence to suggest they are a higher risk product than other mortgages.

Q5 Lord Marlesford: Per cent of arrears, is that interest or capital repayments or both?

Nigel Tarrington: It is measured as the number of months that a mortgage is in arrears calculated as the months of missed payments. So if you miss three months of your mortgage payments, then you are three months in arrears.

Q6 Lord Hamilton of Epsom: Could I just pick up Ms Cottrell's point, which is what I wanted to raise anyway, about the 120% mortgages? How will this directive actually change these things in the future? If you can play it back, what effect would this directive have had on Northern Rock, for instance?

Vera Cottrell: The directive introduces affordability assessments in mortgages and also it introduces the concept of refusing the mortgage if the lender comes to the conclusion that the individual cannot repay the mortgage. In theory, the directive should make it much less likely that someone will be able to get a 100%-plus mortgage because the affordability assessment is very likely to show that it is not affordable.

The Chairman: Thank you very much.

Jackie Bennett: I would like to respond on that, because lenders are already under responsible-lending requirements and affordability already has to be checked. It is not reasonable to say that affordability was not checked in the case of 100% mortgages or even higher. Affordability was checked and what the directive does would not have changed that position.

The Chairman: Before I bring Lord Jordan in, again, if you could just all try to speak up a bit.

Baroness Hooper: And more slowly.

The Chairman: And perhaps more slowly.

Jackie Bennett: We have lots of information we want to get across.

Q7 Lord Jordan: It is our age, you know. Considering the diversity of the market, is it necessary to provide for the degree of regulation supervision of mortgage providers as set out in the directive? Will this proposal make it more difficult for some EU consumers to get a mortgage?

Jackie Bennett: We do not believe it is necessary to go to the level of detail certainly that some MEPs are trying to introduce in the European Parliament. Again, coming back, most of the directive was set at a principles level, which again is where we think it should be. That then allows us and the FSA to look at the specific issues that they want to address in the UK. I think if we can address some of the concerns that we have in the directive, it should not make it more difficult for consumers in the UK to get mortgages. As I say, that does depend in some cases on being able to address the issues we are concerned about. As Vera was saying, in some areas in Europe it is not as well regulated, and perhaps it is then a good thing that those consumers perhaps do have to go through a few more checks and balances before they are able to get their mortgages. We hope in the UK that it should not have an effect, although again we have the FSA's Mortgage Market Review that they are currently looking at, so we are concerned about the interaction between those two things and how then we will need to implement them in the UK.

The Chairman: Mr Terrington, do you want to add to that?

Nigel Terrington: No, nothing further to add.

The Chairman: Ms Cottrell?

Vera Cottrell: Ultimately what consumers are looking for is a stable mortgage market that offers them long-term affordability. Over the last few years we have gone from feast to famine in the UK mortgage market. Ideally, the directive would get us away from this feast or famine, and if there is a slight reduction in the availability of mortgages overall then that maybe is because previously there has been lending to some consumers who really could not afford to be on the housing ladder. We are looking for a stable mortgage market, and the directive has the potential to do that.

Q8 Baroness Maddock: I wonder if you could clarify some of the points you have already touched on. Particularly, what would be the impact of the directive on the UK mortgage market, and how does our market differ from other states? You have already mentioned one particular issue. Do you think the directive sufficiently takes into account the distinctive characteristics of national mortgage markets? Again, you have touched on this. I think also, importantly, will this proposal conflict or duplicate the measures that have already been taken here by the FSA in relation to the Mortgage Market Review?

Nigel Tarrington: There are a number of points there. I think there are significant differences between the various countries and the way their mortgage and housing markets interact. I think there is a real danger that we try to achieve a one-size-fits-all approach here. The area that I am most specifically focused on is the buy-to-let market, and that probably has had the starkest differences between these various countries. You have between, say, Germany, France, Spain and the UK, major differences in regulation, differences in the tax treatment, differences in the way in which the legal structures work between landlords and tenants, all of which, by themselves, can affect the way a mortgage should be designed and lent against.

In addition to that, those markets are moving at different paces. The UK private-rented sector had been in decline for really the best part of 100 years until the 1980s. For the last 30 years or so it has been growing, and in fact it is currently the only growing form of housing in the UK. It now accounts for around one-sixth of houses in the UK. Now, if you compare that with Germany, which has 60% of its properties privately rented, France, where it is around 23% to 24%, and Spain, only 7%, you can see some stark differences. Some markets are stable and some are declining. Ours are actually growing quite significantly for a variety of factors. It is currently an area of the market that is in need of support because it is almost like the pressure valve for the housing market at present. We could damage it by imposing unnecessary and disproportionate regulations on it.

Q9 The Chairman: Before I invite the two ladies to come back on Baroness Maddock's question, Mr Terrington, is there a distinction to be drawn by the fact that the proposal is for a directive—in other words it comes from Brussels but is applied nationally—rather than a regulation? Does that give us some latitude?

Nigel Terrington: If they introduce it as a directive then leave it to the local regulator to decide whether it should be implemented, I do not think there is an issue about whether the market should be regulated. We are not against regulation; it just needs to be appropriate. Probably the key difference with the UK is that a substantial amount of the housing stock in the private-rented sector is not owned by consumers. It is owned by small businesses, for want of a better description. It would be wrong to try to shoehorn a consumer-based piece of legislation or regulation over what is, in effect, a commercial transaction.

The Chairman: Ms Bennett, you were shaking your head when I was putting that supplementary point. Would you like to respond to that, and also to Baroness Maddock's original questions?

Jackie Bennett: Sure. We think the directive should focus on the core residential market. This is the first time a directive has been introduced for the mortgage market, and right across Europe there are all sorts of individual vagaries around the different markets. Nigel has already touched on the buy-to-let market in the UK. In Spain there are commercial transactions that can be transferred to consumers. One of the MEPs has tried to introduce some amendments along those lines. We have shared ownership and shared equity in the UK. There are all of these different things. I think, as was said, we cannot have a one-size-fits-all directive. We think the core focus should be on the residential market, and let us see how that works.

In terms of where it might impact on the UK, I think there are a number of areas that we are concerned about. One area, and again Vera mentioned this in her opening remarks, is pre-contractual information that is given to customers. We have a Key Facts Illustration that has been part of the mortgage market since 2004. Under the European directive we would have to introduce a European standard information sheet. This is where we would not have any authority to move away from what the directive actually requires. This is a standard document that would be provided in all 27 countries. It does not contain as much information as we have already in the Key Facts Illustration; therefore, we think consumers in the UK would lose out because we would not have that information available anymore. The only way we could do it is to have a supplementary document.

Of course, the FSA has evidence to say that consumers do not always read the information that they have, so giving them two pieces of information is not going to improve that information flow at all. One of the other big areas of concern for us about the original proposal for the directive is that it may not allow lenders to give advice on their own products. That is a big part of the UK market at the moment. In 2010, something like 49% of products sold were by lenders with advice. We think that is a really important part of

what we need to amend as the directive goes through. I have to say we are making some good progress on that, but we do not seem to be making much headway at the moment on the information that consumers are to be given.

Q10 The Chairman: Could you just elaborate on that point?

Jackie Bennett: Just in terms of the information? Maybe Vera would like to add to that.

Vera Cottrell: Yes, I agree with Jackie on this point, and we are very concerned about the issue of the pre-contractual information disclosure in the directive. The commission tested their pre-contractual information sheets against the UK KFI in 2009 on UK consumers, and UK consumers found that they preferred KFI, the existing pre-contractual information on mortgages in the UK. We have a situation where it would cost the UK industry a significant amount of money to implement the new pre-contractual information but UK consumers would, in a way, be worse off with the new information and disclosure regime. This is one area we are also doing a lot of work on, and unfortunately I have to agree we are not getting very far.

The other area I think we have particular concern about is the passport for mortgage intermediaries that is being introduced in the directive. Again, you talked about the differences in markets across Europe; in the UK we have an incredibly well-developed market in mortgage intermediation. We believe that it is for the advantage of consumers to be able to go to an independent mortgage intermediary and get advice or to get advice from their lender. This concept is not very well developed in the vast majority of other member states. To introduce a passport would allow mortgage intermediaries to set up in another member state and passport into the UK, and although they have to be supervised by their home state regulator, that regulator has no experience of supervising mortgage intermediaries and is probably not really set up to do so. There is a real risk that UK

consumers will experience advice from mortgage intermediaries that are not being properly supervised.

Q11 Baroness Maddock: There are a couple of things that I wanted to ask. Carrying on from your last point, are there other countries in Europe that have the same concerns that we have about this? I think about Scandinavia, where they probably have quite good financial regulation. Do they have the same concerns as you?

Jackie Bennett: There are one or two countries that do have similar concerns around particularly the pre-contractual information, but I think there will be more member states that perhaps already use these because they have not developed their own documents. So on a majority basis, we are not really getting very far.

Q12 Baroness Maddock: We are unique because we have this well-developed, long-standing advantage?

Jackie Bennett: I think that is right. We are ahead of a lot of the rest of Europe in terms of mortgage regulation. That means we need to be doubly careful to make sure that the directive is not in conflict with what we already have in place. Again, I think as Vera was saying, something like changing the Key Facts Illustration to the European standard information sheet would cost us tens of millions of pounds, but there would be no benefit to consumers from doing that. It makes it quite difficult.

Q13 Baroness Maddock: The other question is on the buy-to-let mortgages: again, is there any indication that we can separate the two out?

Jackie Bennett: There are some amendments that have gone down as part of the European parliamentary debate: one would take buy-to-let out of scope completely for this directive—

as Nigel was saying, we do see this as a commercial transaction rather than a residential one—and another UK MEP put forward an amendment to allow member states to choose whether they apply it or not. Certainly, in France and Germany they already have this as part of their normal mortgage market. They do not have it as a separate product, although we do not think the directive works well for buy-to-let mortgages. For example, the credit worthiness assessment, which is our affordability assessment, at the moment would not allow rental income to be taken into consideration, which is really where that assessment is done for buy-to-let, not on the normal affordability of income and expenditure that you would expect for a normal consumer. I think, as Nigel said, it is not about it not being regulated; it is about whether this is the appropriate way to do it. It feels like you are shoehorning something into a system that it is not necessarily designed for.

Sorry, I am also conscious that I did not answer your question about how it interlinks with Mortgage Market Review.

Baroness Maddock: Well, you sort of indicated a bit.

Jackie Bennett: We are still waiting for those proposals to be finalised and we are still waiting for the next consultation paper, which is due sort of any time, from the FSA. We are really mindful, and to be fair the Treasury is as well, of the need to look at these two proposals and how they interact with each other and the implementation that lenders will then need to make in terms of that. We hope we can have it very sensibly done, so that we do not have one wave of changes come in through the Mortgage Market Review and then another through the directive that, again, would cost a lot of money for perhaps little benefit.

Q14 Lord Moser: Both of you, in your last remarks, have stressed, “But we are not getting very far.” I did not understand what the blockage is.

Jackie Bennett: I think the blockage is that within Europe you need to build a consensus of support across all 27 member states, and because the buy-to-let market is unique in the UK, we cannot build that support. Similarly, on the European standard information sheet, as I said, there are probably more member states that have already got that in place and are using it or who do not have something and therefore are quite ready to introduce a standard document, than there are those that have their own document. Although we are trying to get amendments, and UK MEPs have put amendments down on our behalf around this, it is whether when it comes to the vote there are enough supporters of those issues to be able to make it through.

Lord Moser: Was it the same point when you said it?

Vera Cottrell: We have liaised with consumer groups in other member states on the pre-contractual information, and we have managed to get a common position on this from the European Consumers' Association. Their position is also that member states should be allowed to keep their existing pre-contractual information sheet; however, the challenge is really more at a Government level when it comes to other member states: there is no real appetite to follow the UK's position.

Q15 Lord Moser: We gather that there has been a compromise proposal on the table from the presidential area. I am not sure whether we are very clear what the compromise proposal is, but the main point is, from your angle, is it helpful? Is it going to make the directive better, worse or no different?

Jackie Bennett: The Council operates in parallel with the European Parliament to look at the directive. On the Council there are representatives of the Governments of the 27 member states and the Treasury represent the UK on that. I have to say, we think the compromise text is going in the right direction in a large number of areas—a number of the

things I talked about around advice. There are also a number of delegated acts proposed in the directive, which means the Commission would be able to make changes without consultation and without impact assessments. Again through Council, a lot of those are starting to come out of the directive. We think where they have got to so far is a big improvement; however, on the buy-to-let issue, on the pre-contractual information issue, again, because we cannot build this consensus amongst other Governments, as Vera was saying, we have not been able to get that same agreement in Council. So, yes we have made a lot of progress, but there are still a couple of issues that we would like to make a bit more progress on if we could.

The Chairman: Do you dissent from that, Mr Terrington?

Nigel Terrington: No, no, no—completely agree.

Vera Cottrell: We have seen some progress on the passporting requirements but not to the full extent we would like to see. There are also some things that we actually liked in the original directive that the Council compromise has taken out around Article 14. When it comes to pre-contractual information, I absolutely agree with Jackie that we are not really seeing any improvement.

Q16 Baroness Hooper: I wanted a supplementary on Baroness Maddock's question, because it is the eternal problem where we have a well-regulated developed market, and also the effect of our different legal system and therefore different approach that somebody referred to. What I am not clear about is, do you think the object of this proposal is to encourage more cross-border mortgages, or is it simply to provide regulation for those countries that do not have any or much and cannot achieve it on a national basis and therefore use the excuse of having to comply with EU regulation? Is there a balance between those two objectives or is it just the latter?

Jackie Bennett: I think it is a little bit of both, but the Commission's aim is really about trying to create a single market exactly because of the issues you have raised; there are different legal systems and different mortgage markets across Europe. I think it is very, very difficult to create a single market. The amount of cross-border lending that goes on, certainly from the UK—we do not have exact figures—is probably less than 1%, I am guessing. I do not think there are good figures around cross-border lending, but it is certainly very small. I think if you do have standard regulation across Europe, it might give some opportunities for lenders or intermediaries from the UK to operate abroad. But again with the financial crisis, there is not that much appetite to do that at the moment. I think in the short to medium term, it is difficult to see where those opportunities would come from. There is an element as well that not all countries across Europe are as well regulated as we are, and there is then that minimum level of regulation that can be applied across Europe. There is the dual aim but the primary aim is about trying to create a single market, which is perhaps ambitious.

Vera Cottrell: I can just support what Jackie said.

Nigel Terrington: The one thing I would add to that is we have a very competitive market in the UK. There are over 100 mortgage lenders, thousands of individual mortgage products and I think the potential supply of extra finance that may come in to the UK through cross-border lending opportunities will add nothing to the competitive position of the UK.

Q17 Lord Haskins: I detect a singular lack of enthusiasm for this directive generally, but it borders on the suggestion of irresponsibility when it comes to suggestions that mortgage borrowers should be borrowing all over Europe in different currency areas. This sounds the height of irresponsibility to be even contemplating that; maybe it is possible within the

eurozone, but the experience of doing it right across Europe seems to be completely outrageous.

Vera Cottrell: Clearly, there is very little appetite amongst consumers to borrow across borders. The legal differences in different regimes not only relate to the mortgage lending but also how the home-buying process works in different member states. It is a massive barrier. Language is a huge barrier, and obviously currency is also a barrier in the UK. We do not see consumers wanting to take out mortgages cross-border. Probably out of all the financial products that are there, mortgages are right at the bottom when it comes to consumers' willingness to purchase cross-border.

The Chairman: Ms Bennett, anything to add?

Jackie Bennett: No, nothing to add.

Nigel Terrington: I would also add it is dangerous for lenders as well, not just for consumers. The minute you cross a national boundary, you are into clearly different legal, tax, regulatory structures as well as custom and practice. The operation of the local custom and practice could have dramatic effects on the performance of the loan portfolio that you have just made. We, for ourselves, restrict our operations to the UK, and there is very little comfort we would draw from being able to lend in France or Germany. We would want to establish local operations to do that, which therefore does not become cross-border lending.

Q18 Baroness Maddock: In your opening remarks, Ms Cottrell, you said you could see the value for the consumers in having a directive, but, in all the evidence you have given, you have given us reasons why actually we do not need to have it. I wonder if you could just clarify.

Vera Cottrell: I should qualify this because we are very active when it comes to liaising with other consumer protection groups across Europe, and obviously there are different ways the mortgage directive is going to impact. Having an unstable mortgage market in Spain or Hungary or Romania ultimately has an effect on Europe overall. Having a piece of legislation that puts stability into these markets would be good for consumers.

Q19 Lord Woolmer of Leeds: Jackie Bennett, I think Nigel Terrington has already said quite a bit about the buy-to let-market being excluded, and your organisation takes a similar view. Is there anything to add on why you take that view? On the second theme, the Government said that, although the majority of mortgage lending in the EU involves borrowing from mainstream lenders, there is a diverse range of niche products that add choice in specific circumstances. I think you touched on one or two already, and they do not fit easily into the directive. Two things: could you tell us about one or two niche products that do not fit in this directive very easily, and are you concerned about that? What can be done to correct that problem?

Jackie Bennett: We have talked quite a lot about buy-to-let, and I think we have probably covered most of the issues and why we see that as different in the UK. In terms of niche products, I talked about shared ownership and shared equity where there is an element of lending from housing associations for example. At the moment, it is quite difficult to see how they might fit into the directive. As Nigel said, we have a very competitive mortgage market in the UK; we have things like guarantor mortgages and off-set mortgages. Again, it is not entirely clear how some of those would fit in the directive. Taking the guarantor mortgage, for example, where a parent or some other relative would help with the mortgage or at least guarantee part of it, again with the way the credit worthiness assessment is proposed to be carried out, there is something called the duty to deny credit.

If the affordability in very plain terms does not match up, then the lender has no leeway but has to not give them a mortgage. In the case of a guarantor mortgage, if you just look at the borrower, that may not work, but with the support of a parent or somebody else you can do that. Again I think we have concerns about, for example, the self-employed, who may have seasonal income, and particularly in the early years it may not look quite as good as it will look in future years. The lender will be able to take a rounded view about that business proposition and whether that is suitable for a mortgage. I think we are concerned that the way the directive is currently drafted means some of those things may not be able to be easily operated in the UK. Again, through the amendments that we are seeking and the way the Council text is progressing, we think some of those things can be addressed or are being addressed, but it is about trying to make sure that the unique and diverse nature of the UK mortgage market can be protected under the strict regulation that we have with the FSA without it being interfered with by the directive, which is sort of looking for this one-size-fits-all approach.

The Chairman: Mr Terrington, Ms Cottrell, would you like to answer anything or elaborate on that?

Vera Cottrell: No.

Nigel Terrington: To add perhaps just one additional point, niche products, by their very nature, are quite often not the domain of the main high street lenders; it is just because it is small by nature and allows that smaller lender to operate in a much smaller market and be a little bit more thoughtful, perhaps, rather than a production-line approach to lending. One of the consequences of having a new layer of regulation imposed is that if it hits the specialist products then the opportunities to lend to consumers in that space will be restricted. In addition, the ability of those specialist lenders to access funding will be restricted, because they usually do not operate through deposit basis through high street branches, so they have

to finance themselves usually through say the securitisation market. If you impose different sets of rules or an extra burden on those markets, that could impact the way in which those organisations have to fund themselves.

Q20 Baroness Hooper: We have already touched on the issue of the passport—the proposal to provide intermediaries with a passport regime. I think it was said there were problems on this. Do you agree with the Government that additional requirements in line with the regime of a national regulator should be placed on intermediaries acting within that national jurisdiction? As an additional question, who is going to monitor this passport regime? Will it be done from Brussels or will it be done by national regulators?

Vera Cottrell: We are very supportive of the work the Government is doing on the passporting regime, because as I pointed out it is one of our main areas of concern. In the UK, about 50% of mortgages are currently sold through mortgage intermediaries. The figure used to be even higher prior to the financial crisis but now quite a few lenders only sell directly to consumers, so it has reduced the range of products available through intermediaries. It is a very popular channel with consumers; we believe that it is very beneficial for consumers to be able to get independent mortgage advice. Setting up a passporting regime does open up the door for potential consumer detriment by allowing firms to go past the FSA, which is a very experienced regulator when it comes to mortgage intermediaries, and come from a country where there is currently no experience with mortgage intermediaries and where the regulator is probably not adequately resourced to supervise and monitor them. What the Government is trying to do is give the home state regulator, in this case the FSA, more power over what the passporting firms do once they are in the UK. Obviously, that applies to firms that set up a branch in the UK. If a firm decides to just provide services, i.e. set up on the internet, then what the Government has

proposed is not really going to make much difference because it is not going to catch these firms.

Q21 Baroness Hooper: I am sorry, I think I must have misunderstood. I thought this applied in relation to cross-border activity, but it applies to national activity as well, does it—intermediaries and passporting?

Jackie Bennett: It would allow intermediaries from another member state to come and operate in the UK.

Q22 Baroness Hooper: So it is the cross-border activity, which is so minimal in our case?

Jackie Bennett: It is very minimal, but I think we share the concerns around intermediaries perhaps authorised from another member state coming and operating here. Again, the lenders would have to take a lot more care in the cases that came forward to them. If the FSA could not impose any additional regulations on them, as they do already in the UK, then we could not be sure that the mortgages we were getting from any overseas intermediaries operating in the UK were of the same standard. I think that would be a concern as well because it is about making sure the lenders' money is safely lent as well as making sure the consumer is safely lent to as well.

The Chairman: Mr Terrington, anything to add?

Nigel Terrington: Yes, I think it is a potential invitation to fraud as well. The FSA is, as we said, very experienced, and the eagle eye of the FSA keeps a very tight rein. You see a number of mortgage intermediaries struck off because of poor standards and behaviour. They are less able to keep an eye on something maybe a thousand miles or more away, operating through the internet, and you will have the potential for people from the UK going

across to a different country, via the internet, and producing a mortgage application that purports to look fine whereas actually it could be fabricated evidence.

Q23 Lord Marlesford: My Lord Chairman, I declare an interest, owning let residential property. My question is primarily for Ms Cottrell. It is really about whether or not you feel, under Article 17 of the proposal, the provision of advice by lenders to borrowers is going to be beneficial to what happens at the moment in the UK or, as far as you are aware, in other countries? Is it the right sort of provision, Article 17?

Vera Cottrell: Article 17 in its current format raises the potential problem that a mortgage lender would be restricted in providing advice if they only sold their own products and did not provide mortgages from other providers, which they obviously do not do in most cases. There have been some amendments tabled, both in the European Parliament and also the Council has taken account of this, to make it clear that, where a mortgage lender provides advice on products, they only have to sell their own products; they will not be required to sell the products of other members, which is something we support. We believe it is good for a consumer to get advice when they go to a mortgage lender; however, we also are of the view that consumers should be told whether the sale is advised or not. This is the case at the moment in the UK and it has clearly been shown by the FSA, when they carried out the Mortgage Effectiveness Review, that consumers only were able to tell whether they had received advice or not when they were actually told whether they had received advice or not. Otherwise, there is a risk that consumers will walk away and think that they have received advice when they have not received advice.

Jackie Bennett: This is an area where we are making good progress. It is about consumer choice and the amendments that have been put down—making sure that consumers are clear on the basis on which they are getting advice, whether that is just from one individual

provider or from a whole range of providers. That is the current position in the UK, and if the amendments are successful that is where we will be in Europe as well. We have a lot of support from other member states on that as well, so we think that is positive.

Q24 Lord Marlesford: It always seemed to me that much of the mischief, starting with the sub-prime stuff in America and all the rest of it, has stemmed from the fact that most borrowers feel that, if they can find somebody to lend them money, it is sensible to borrow it. What I am not clear on is who there is to give them objective advice, and is it objective?

The Chairman: Anyone prepared to answer that? Mr Terrington?

Nigel Terrington: I have some sympathy with your view. When consumers go in to take out a mortgage, they are quite often naturally apprehensive; there is a raft of information they have to absorb; and for them to be able to get advice is something that should be readily available. I think the issue here is some people want it and some people do not want it. The issue is making sure it is clearly appreciated and understood by the consumer when they have had advice, because sometimes they do not understand that what they have had is just information. They think it is advice but it is not. That is the key difference: making sure they clearly understand they have not been given advice or they have.

The Chairman: Our last set of questions from Lord Vallance.

Q25 Lord Vallance of Tummel: I should declare an interest as a member of the International Advisory Board of the financial services group Allianz SE. A specific question to Jackie Bennett, if I may: why does the Council of Mortgage Lenders believe that the requirement for creditors or intermediaries to assess the financial knowledge and experience of consumers should be removed? Then as a general sweep-up point for all

three of you, we touched on the Commission's proposals on disclosure of information earlier on but if there is anything you want to add then feel free to do so.

Jackie Bennett: I should make it clear that we are not against information being given to consumers in any sense. Our concern with Article 11 as drafted by the Commission was that creditors and credit intermediaries had to somehow try to gauge the financial knowledge of the person sitting in front of them. I think that is a very difficult thing to do. We could almost see that you would have to complete a multiple choice exam—whether you understand what interest only, variable and fixed-rate mean—before you could try to gauge what level of explanation you needed to give that person. So it is not that we are against advice at all and giving people proper explanations. Again, the amendments that are going through in Council and have been put down in the Parliament are very much about trying to make it much clearer about the information that a person should be given. That is about the key features of the mortgage they are going to be taking out. I think it was just about the way it was drafted rather than what it was in itself. I am sorry, what was the final question?

Q26 Lord Vallance of Tummel: A general point on disclosure of information: do you believe that the Commission's proposals are appropriate or not? You commented on that already.

Jackie Bennett: Sure, we talked about pre-contractual information. One area we have not touched on so much is the advertising regulations that are proposed under the directive. These were very, very detailed, and again we do not believe necessarily at the advertising stage you need as much detail as the directive was proposing. It included, for example, a representative example of what a mortgage would look like. All of you around the table will know that every mortgage is very individual to your circumstances. We thought in some

ways a representative example is virtually meaningless because it will not apply to any individual's situation. We are trying to make sure that the right information is given to consumers at the right time because that is the best way they receive it. We are hoping that some of those proposals can be simplified.

Vera Cottrell: We believe the proposals need to be simplified. We know from talking to other consumer groups that we all have different things we want in the disclosure information, both in advertising and the pre-contractual disclosure, and, if you put everything in that is currently being used in every member state, the document would become completely unwieldy. Therefore, allowing member states to carry on with their existing rules would be much better.

The Chairman: Is there anything else, colleagues, that you want to get off your chests before you leave us today?

Q27 Lord Hamilton of Epsom: Would it be right to sum up your collective view as: we would be better off without this directive in the United Kingdom than with it?

Nigel Terrington: I think we understand the need of the European Union to have better standards of mortgage regulation across the entirety of the 27 member states. I think we, in the UK, are well down the road to that. This will not sound very good, but they need to be brought up to our standard, I think. What we are concerned about is an extra layer of regulation that will not achieve the objectives that it sets out to achieve: to enhance cross-border competition. I do not really see much there. I think it will increase perhaps consumer protection in a number of member states. I think we already have high standards within the UK; particularly the FSA has got the latest version of the Mortgage Market Review, which is due imminently. I think once that is implemented it will be of a gold standard of its own. I think we understand the wider set of responsibilities and we need to

make certain that this does not impose undue levels of extra regulation or importantly cost, which ultimately will have to be borne by someone, on the UK mortgage industry.

The Chairman: Let us conclude at that point. Can I say you have been most generous with your time? We are very grateful. We are very grateful, too, for the brevity of the answers but the fullness of the answers in the sense of the quality of them. I suppose it is very difficult when you have three witnesses and many questions being fired at you. We will issue transcripts of this exchange. We do ask you to just check and make sure they are correct, or indeed if you think there is an infelicity, correct it and if you could just clarify that. We are always ready for an *arrière-pensée*—the afterthoughts that you think would be helpful to us. In the mean time, on behalf of the Committee, many thanks indeed for attending today and for the evidence that you have given, which will be very useful to us indeed.

Examination of Witness

Witness: **Annik Lambert**, Secretary General, European Mortgage Federation, gave evidence.

Q28 The Chairman: First of all, our Committee's thanks for you chancing over from Brussels this morning on the Eurostar. We are very pleased to see that you have made it, and made it on time. Thank you very much indeed for coming to see us on this Residential Property Directive. We are all ears to hear what you have to tell us. Would you like to make any kind of opening statement? Within it, would you say a little bit about what the European Mortgage Federation does? Are there any British representatives, UK representatives, on it? I should also add that we will at the end of this session do a transcript of the exchange between us. We will send that to you, and we would be very grateful if you could correct that in the fullness of time. Indeed if you have additional thoughts after you leave the room, once again we would be very grateful to hear those from you. We are being webcast today. Perhaps I can invite you to say a little bit about the EMF before we move to the questions.

Annik Lambert: Thank you very much, Lord Chairman. Good morning, ladies and gentlemen. The Mortgage Federation was launched in 1967 to represent the interest of mortgage lenders throughout Europe. It was a smaller Europe at the time, but it has become bigger and bigger. We are a product federation, so we represent all institutions of mortgage credit background, be they commercial banks, savings banks, whatever kind of institution, and we cover the retail side, like this directive we are discussing today, as well as the funding side. We have been following this specific file ever since 2003 when the

Commission started investigating with the hope of further integrating mortgage markets. In a nutshell, I do not know if you have more precise questions, but that is what I would like to say. We are very active with the Commission, with the European Parliament. It is more difficult with the Council, but for the time being we, and the Council of Mortgage Lenders, have been on all fronts represented by Jackie Bennett here, as well as the Building Societies Association, who have been our members forever—since the beginning of the Federation.

Q29 The Chairman: Excellent, good. What is your overall assessment of the Commission's proposal for a directive on credit agreements relating to residential property? Will it succeed in achieving the Commission's aims of creating a responsible, efficient and competitive European mortgage market?

Annik Lambert: To start with perhaps a clarification: it is a very different thing if we speak from the Commission's initial proposal and the Council text, or if we are speaking from Mr Sánchez Presedo's report. They are two different worlds, so depending on the issues I will make clear what I am speaking about. The Commission's proposal, I mean the text that we have seen tabled, now some time ago, represents a complete shift in the Commission's policy. Initially they were really looking at how to further integrate mortgage markets, and now this proposal only deals with consumer protection. Given that we know the integration of mortgage markets will be supply-driven, this consumer protection focussed text will not achieve an integrated European market; but then I do not have the impression that anybody around the table is really concerned about this objective right now. I think the Commission's objective right now is really consumer protection. Of course, consumer protection, in principle, is an initiative that is not without any merit but it is definitely not a priority today. In the crisis we are facing the priority is really the deregulatory aspect of

regulation for the banks and for supervision, so CRD IV, but definitely consumer protection is not what we should be dealing with right now.¹

As to the possible outcome, of course it depends if we are speaking of the Commission's proposal or if we add in a number of the amendments by Mr Sánchez Presedo, but what we believe is that it is going to lead to a much reduced offer because there is an unbalanced shift of responsibility from the consumer to the lender. So the offer is going to decrease and the cost of credit is going to increase significantly, which means that access to credit in housing will diminish across the European Union, with the risk of exclusion for a number of citizens like first-time buyers, self-employed or low-income people, in a nutshell.

The Chairman: Thanks very much. Perhaps we will get an opportunity to explore the differences that you identified between the report and the directive as it started life.

Q30 Lord Vallance of Tummel: Setting aside the point that you make about the timing of these proposals, are they really necessary anyway to help protect consumers from irresponsible lending or indebtedness, or are they really an attempt to design a European solution to a United States problem?

Annik Lambert: I would say the response is very much in the question. In fact, in the European Union a small share of the mortgage market in very few Member States was sub-prime. It was in no way toxic sub-prime lending as we have seen in the US. Therefore, irresponsible lending was not in any way the source of the crisis in the EU. The source of the crisis in Europe is the fact the banks have invested in US securitisation without being aware of the risk that was in those products. Then, of course, from there we saw a very strong decrease in confidence and the liquidity crisis that ensued. What I would say here is

¹ Note by witness: Ms Lambert has suggested that the preceding sentences should be amended to read as follows: "Of course, consumer protection, in principle, is an initiative that is not without any merit but it definitely cannot be the only priority today. In the context of the crisis, the main priority is really the regulatory aspect of regulation for the banks and for supervision, i.e. CRD IV, but definitely an initiative focussing solely on consumer protection is not what we should be dealing with right now."

that there is no business case at the European level. In some countries where there have been problems, of course, measures need to be taken. Those measures are being taken at national level where necessary and in a way that is more suitable to the national markets. I would very much say that there is no business case at EU level.²

One last point on this, which is interesting because it is a question of responsible lending—why and how—is that within the EU funding is based on a mix of techniques, but especially on the Continent the main funding tool is still savings deposits. The second one is covered bonds and then securitisation, but with savings deposits and covered bonds it means the loans remain on balance sheet. The risk remains on the lenders' balance sheets. There is no choice but to do responsible lending because if a bank is doing anything else and the loans are not being repaid, it is going to go very, very quickly into bankruptcy. The creditworthiness assessment procedure has existed and has been applied to other member states, I would say, for decades. The situation is very different from the US where the totality of the loans were funded through securitisation and externalised from the banks. That is the problem we saw in the US.

Q31 Lord Jordan: The way you have described it, it is as though the emphasis is shifting for this to be seen primarily as a consumer protection directive. Is the degree of regulation and supervision too onerous? Will it, in fact, make it more difficult for EU consumers to get a mortgage, and could you give us an example of where this might happen?

Annik Lambert: Yes, definitely. Here, also, there are a number of different aspects. First, in the Sánchez Presedo report there are a number of potential provisions that deal more with financial stability and supervision. There is no place in this retail proposal for such provisions; they should be in the CRD where they are already are, and there should be no

² Note by witness: Ms Lambert has suggested that this sentence should be disregarded.

overlap with possible problems of incompatibility. That is one side. The second side, I would say, is as long as the initiative remains principle-based, as the Commission proposal was, I would say that it is realistic, it is workable, but it will make it more difficult for consumers to get a mortgage. For instance, a problem we have even with the Commission proposal is the duty to deny credit when the creditworthiness assessment outcome is negative. Well, it seems obvious; whenever a creditworthiness assessment is negative, obviously the credit is going to be refused, but making this a legal obligation makes it a problem in terms of potential liability for the lender and in terms of increased litigation. It is difficult to explain and perhaps all the more for me in a different language.

It works the other way around. If the credit was granted it means that the creditworthiness assessment was positive.³ The creditworthiness assessment is an assessment carried out by the lender in order to establish that the consumer will be able to repay his loan based on his income.⁴ Of course, there are a number of elements that come into the picture, like possible other guarantees and personal guarantees. The collateral, of course, plays a role also, because without the collateral, although the aim is never like in the US—to say, “We do not care; we are going to get repaid on the foreclosure”—this is never case, but still it is a guarantee that allows the lender to take the risk and also to grant, I would say, a reasonable interest rate.⁵ Rendering it a legal obligation will lead lenders to stop granting a number of loans that they would probably have granted in the past and that would in all likelihood have been repaid without difficulty.⁶ This is really due to the fact that this causes

³ Note by witness: Ms Lambert has suggested that this sentence should be disregarded.

⁴ Note by witness: Ms Lambert has suggested that the following should be added to the end of the sentence: “, but also on a number of other factors” at the end of this sentence.

⁵ Note by witness: Ms Lambert has suggested that the preceding sentences should be restated as follows: “The collateral, of course, plays a role also, and it is the existence of the collateral which enables lenders to lend in the first place and to do so at affordable interest rates. We must be clear here however that in the EU a lender will never grant a loan based only on his ability to foreclose on the property; this was however the case in the US.”

⁶ Note by witness: Ms Lambert has suggested that the following should be added at the end of this sentence: “Studies from the CML on the FSA’s Mortgage Market review have drawn interesting conclusions on the impact of regulation on lenders’ ability to lend and the subsequent impact on consumer access to credit.”

an imbalance in the responsibility between the consumer and the lender, knowing that at the end of the day it is still the consumer—the candidate borrower—who needs to make the final decision as to whether or not to take out credit and which product better suits his needs. Furthermore in relation to the duty to deny, and all the more so with regard to the obligation to explain to the consumer why the credit has been refused, a lender has no obligation to explain why; he should have the freedom to contract. If he is to give some reasons and some motive, that could furthermore later on be used in court against him. It is really biasing the whole process, I would say.

Q32 Lord Moser: We gather that the Council has announced that there is some kind of compromise to the directive on the table. I am sure that we here are aware how far-reaching that compromise is. The main question to you is: is this good news, is it bad news or is it no news?

Annik Lambert: I would say the Council is good news at this stage. The Council text I would say is very much in line with the Commission's initial proposal. Of course, as with the Commission, we have some concerns, but I would say on the whole it is realistic and workable. It is totally different from the report we have received from the ECON rapporteur Mr Sánchez Presedo. We have some concerns that would need some discussion and possibly some adjustments, but I would say that this is a realistic basis for discussion with industry.

Q33 Lord Moser: What is the main point of the compromise that has been suggested from presidential routes?

Annik Lambert: I can give you more details but it is very close to the Commission's initial proposal. For example, the use of delegated acts in the Commission Proposal is really a

concern for the industry because we believe they are misapplied and overused because normally, according to the Treaty, delegated acts should be used only for provisions in a directive that are non-essential. They should not be applied to the core elements of the directive, for instance. In this respect, the Council, along with the industry, criticised and would get rid of a number of delegated acts as they stand now in the proposal. For the duty to advise, they have also, I would say, a more flexible approach than the ECON rapporteur. We have a problem with the competence requirements for the staff of lenders, where they seem to be very, very strong and not very flexible on the issue of the competence required for staff in contact with the customers in the bank. On the creditworthiness assessment, it seems like it is still open but it would be closer to the principles-based approach of the Commission than to the prescriptive approach of the Parliament. As for the duty to deny, they also have a more flexible approach than the Parliament, for instance.

Lord Moser: Nothing really dramatic.

Annik Lambert: Things to be still discussed but realistic and workable in general.

Q34 The Chairman: You mentioned earlier that Mr Sánchez Presedo had some differences or divergences. Would it be useful just to try to sum up the direction of travel they have?

Annik Lambert: This is 177 amendments. The Sánchez Presedo report is a totally different picture. We are not speaking of the same legislative text anymore. He goes further in every respect, and is much more prescriptive than the Commission in its proposal. He also introduces brand new provisions, which needless to say have never been assessed or even considered. We have no idea at all whether or not they would be workable, and, if they were workable, what the potential impact in terms of benefits for the consumer and possibly of detriment to the lender; we have no idea at all. For a number definitely he is going very,

very far, for instance in terms of flexibility for the consumer to be able to switch creditor, but then it is not even clear whether his amendments relating to the "switching of the creditor" is something different from "early repayment" and whether "early repayment" is different from "payment flexibility". It is very difficult to assess without a very thorough, in-depth impact assessment.

There are proposals that we know do not make sense in any case. For instance, Mr Presedo wants to use the valuation that the lender has done by a valuer before he grants the loan, provided he does grant the loan. This valuation is very much a tool that is used by the lender and is used with respect to his own risk assessment and his regulatory obligation. The valuation has nothing to do, in fact, with the borrower. He wants to introduce an obligation for the lender, in case of repossession foreclosure, to use the amount of the latest valuation that was done in the context of the CRD.⁷ He wants to use that as the minimum amount that the consumer is entitled to in case of foreclosure, even if the property is sold at a price which is much lower than that last value. If the valuation was carried out a year earlier and both the market and the value have since decreased, the lender will still be obliged to use the amount of this last valuation.

Q35 The Chairman: Has he any support for his views do you think?

Annik Lambert: Hopefully not. I have to say that I think Mr Presedo has been going around and listening, and has heard many things that he has tried to fit into the proposal, but he has no idea whether the tool he is using is going to take him where he believes he wants to go. We have problems with first, his objective, where he wants to go; for some of the aspects is it not workable and not sensible. The other part is that we are not sure that the tool he is

⁷ Note by witness: Ms Lambert has suggested that the preceding sentences should be amended to read: "For instance, Mr Presedo wants to introduce an obligation for the lender, in case of repossession foreclosure, to use the amount of the latest valuation that was done in the context of the CRD."

using will take him, at the end of the day, where he believes he wants to go. There is a lot to be said about many of his proposals.

Q36 Baroness Hooper: Has the Sánchez Presedo report been approved by the Committee yet or does it still have to go through its Committee stage? When is it expected that the plenary debate will take place, because presumably the plenary debate would take into account this compromise proposal?

Annik Lambert: Yes, that is the good news: this was very much his first report. It was very much Mr Sánchez Presedo's own report; it was not the ECON report, and in the mean time we have seen tabled a second ECON report that presents more than 800 amendments,⁸ which go in many directions but I would say in general tend to bring the situation back closer to the initial principle-based approach text from the Commission, and therefore also the proposals from the Council.

Q37 Lord Haskins: We find it very difficult to find anybody who has got any enthusiasm for this directive. Searching bravely on, one of the proposals is the directive's aim of creating the European mortgage market, although as far as the United Kingdom is concerned we understand 1% of mortgages are designated outside the UK. This is not just fanciful; is it not entirely unrealistic for the Commission to be pushing a European mortgage market with all the differences of currency, of regulation at national levels, etc? No consumer is going to bite that one.

Annik Lambert: There are a number of responses. It is true that a fully integrated mortgage market is certainly the right objective but it is not for tomorrow. There is some time before

⁸ Note by witness: Ms Lambert has suggested that the preceding passage should be redrafted to read: "It was very much Mr Sánchez Presedo's own report; it was not the ECON report, and in the mean time 800 amendments have been tabled to his draft Report, which ..."

we get there. The internet and e-commerce should at some stage help to go in that direction. This is, I would say, a more distant objective, and in this respect one aspect that needs to be taken into account is the mortgage credit product. By going on your computer and checking what conditions and offers you can find in different countries, you can easily buy a car in Finland and get it brought to the UK. If there is a financial interest, at least practically, materially, it is possible.

The mortgage product is very specific in this respect because it is linked to the national territory and the national legislation, because the mortgage credit is directly linked to the property you want to buy. The property is submitted to national legislation as it is submitted to national taxation and so on. Even—and possibly we will get there—if at some stage the obstacles are removed, mortgage credit is never going to be a product for which there will be a huge appetite to buy on a cross-border basis. On the other hand, one thing we have seen is that it depends on what you call cross-border, what you call integration. If cross-border is really buying from one consumer in one country from a provider in another country, that is the pure definition of cross-border. Cross-border is also a company from one country establishing in the territory of another country. What we have seen for mortgage credit is that the cross-border activity is very much supply driven. The consumer is not going to shop around on the internet to find mortgage products in other countries, but if the lender moves from whatever country into UK territory for example, then consumers are willing to buy from these providers.

Therefore, I come back to my first point, if the real objective from the Commission and the European Parliament and the Council was to be the integration of the mortgage market, as was the case from 2003 to 2007, then what needs to be done is not consumer protection but the removal of the obstacles that prevent lenders from going cross-border and establishing in other countries. It is everything that has to do with, for instance, land

registers, credit registers—it is not harmonisation but convergence. It is accessibility on a cross-border basis.

It is also some definition of concepts in valuation procedures, so the valuation in one country can be recognised in another country, as well as in terms of the foreclosure procedures, which does not mean making it easier to foreclose, which was never the idea. In some countries it is very efficient: once the lender decides he needs to foreclose because he does not see any other possibility, it takes six months until the procedure is achieved. In some countries—I think I can name Italy because everybody knows—it is going to take five years in the best case. This is definitely an obstacle. No lender will want to establish in Italy if they believe they will never be able to repossess. The idea here is to say that once the decision to foreclose is taken and the procedure is launched, it should go as smoothly and quickly as possible because the longer it lasts the more costly it is for both the consumer and the lender. These are the issues which were addressed in the consumer white paper that was the conclusion of their five-year investigation from 2003 to 2007. In December 2007, they published their white paper. Of course the timing was very bad because that was when the crisis hit. This white paper was never spoken about anymore, and at the same time there was a proposal for a recommendation from the Commission on those subjects to remove the obstacles to lenders going cross-border. This has really been buried for the time being, but, if the idea is integration of mortgage markets, what needs to be done is removal of the obstacles to lenders going cross-border.

Q38 Baroness Maddock: We seem to be getting to the point where we are not sure if this is a good idea or not, and as you said it is mainly for consumers. Given that the directive is there and we are trying to look at it, does it sufficiently take into account the distinctive characteristics of the national mortgage markets? You touched on it in your

comments of course. How do you see the UK mortgage market differ from the European mortgage markets?

Annik Lambert: It is true there is a huge diversity throughout the 27 countries' mortgage markets and the principles. Very often the principles are the same but the application and the way the markets work are really very different. You have different models, so of course you have different legislation. That was why the Commission's initial proposal was welcome: because it was principles-based. If you have a principles-based regulation, then the national regulator can adjust these principles to their national environment. If it becomes prescriptive, as we have in Mr Sánchez Presedo's report, then you do not have this flexibility anymore and it would mean a problem and some constraints for a number of national markets.

If you ask me how different the UK market is, it is first very different by its size. It is the biggest market in Europe; it represents more than 22% of the whole market. It has been the biggest market for a very long time. Despite the crisis, which has hit pretty strongly in the UK, it is still by far the biggest market. You have many differences. For instance, in the UK, I would say the range of product is wider than in many other countries, so obviously the market is very innovative. Also the role of credit intermediaries is very important. At some stage before the crisis you had up to 40,000 credit intermediaries. In some countries they just are really not present at all. I would say the countries where they are really very present are mainly the UK, Ireland and the Netherlands. In some countries they exist but their role is not significant at all, and of course when they are present they play an important role in the whole loan granting process.⁹

⁹ Note by witness: Ms Lambert has suggested that the following section should be deleted from the end of this sentence: “, and of course when they are present they play an important role in the whole loan granting process”.

Also what is specific to the UK market—which is the only such market, and it has to do with the size of the market I expect—is that before the crisis, at least from what I have understood and seen, people in the UK would buy a first dwelling, a first apartment, very early, and they would move on every time their financial situation improved, which means that over a lifetime people would move a number of times from one dwelling to another. In most other countries, you are pretty happy and lucky if you buy once. If you are doing really well, then perhaps at some stage you upgrade to a second house, but that would be it. This is partly cultural, but, because everything is linked, this is also related to taxation. In this country, if I am not mistaken, the transaction cost when you are buying a property and taking out a mortgage credit is somewhere between 1% and 2%. If you do this in Belgium, it is 17%. You do hesitate. You do not recover it; you do not get your money back. You cannot sell the house for as much as it has cost you including the transaction cost. Everything of course plays a role. It is very much related to the system, but there are really significant specificities to the UK market, I would say.

Q39 Baroness Maddock: In the evidence we had earlier on we heard how different the markets were, and I think this is what I am finding difficult to understand. From what you said, most of Europe has one view and Britain has another, which I think came through in our earlier evidence, and therefore it is very difficult for Britain to have any influence over this because there are not any other countries with which we can take a common course, because we are so different, and yet we are the biggest market in Europe. How can we use the fact that we have the biggest market to influence what goes on? It looks as though it is a bit of a lost cause.

Lord Hamilton of Epsom: We only have one vote.

Annik Lambert: I think what I have said from the UK could be said about other markets from other countries with different characteristics. Markets are different and they have their specificities. It is still true you are the biggest market, but I think you do influence the legislation process in Brussels. I would say that the UK delegation is very present in the EMF to start with. I hope we do reflect the CML and the BSA views, but then the CML and BSA are present directly in Brussels, meeting with MEPs and so on. I would say the UK is present, but from my point of view what is rather strange is that, in the past, you were opposed to EU regulation—I would say for very good reasons. Now it looks as though your own regulator is going further and moving faster than the EU legislation, and perhaps this is the main problem here. It is possible that the UK will already have implemented more stringent legislation, by the time the EU implements a less stringent Mortgage Directive. This would cause some discrimination. It would really not allow for a level playing field at European level. But on top of it the risk is that once the EU legislation is adopted it is not fully compatible, so you would have to implement two different sets of legislation, and as everybody knows it is pretty costly to implement legislation. You would have two, possibly not fully compatible, sets of legislation which would bring problems. Furthermore, from what I see, it would potentially be more severe, which would put the UK market at a disadvantage vis-à-vis the rest of the EU countries.

The Chairman: Colleagues I am anxious not to go way over time.

Q40 Lord Woolmer of Leeds: The Council of Mortgage Lenders, as you will know, believes that the scope of the directive should be limited to residential mortgages loaned to consumers for residential purposes. Buy-to-let and part-residential/part-commercial properties should not be caught with these proposals. Two things: what view is taken of

that element of the proposals elsewhere in the EU? Are there any other countries that are sympathetic to that view? Secondly, what is the position taken by your organisation?

Annik Lambert: That is really an easy one, because I would say the whole of Europe, all the member states that contribute to this work, are in agreement that the scope of the directive should be limited to residential mortgage credit. We are all in agreement with this. On this, non-residential/commercial loans are different in many respects. For instance, when you do the creditworthiness assessment on residential mortgage you would not take into account a possible rent. It is really the borrower's income that is taken into account as to the possibility to repay. If it is a commercial loan, of course the fact that there is a rent and the level of the rent would be taken into account. It makes it a different product really, and they should not be submitted to the same rules, especially as this directive, as I said, is about consumer protection. You would not regulate even small companies under the same regime as individuals.

As for the buy-to-let and coming back to the specificity of the UK system, it took us some time to understand what the problem was. In many countries you have buy-to-let. Especially nowadays, with the problems we are seeing and the uncertainty over the markets, instead of putting your money into the bank you buy a property and you rent it out, and you believe it is safer than to have stocks or to have your money in the bank. When it is done in most countries it is just an individual, like me, deciding that he is going to buy a second property—when he is lucky enough to have a second one—to rent out, just because he believes it is a better deal than having his money in a bank. This is not a specific product. It is done under the same rules and same conditions as when you are buying a property for yourself. In the UK, buy-to-let has become a product of its own with its own rules, which do take into account the fact that the property is not going to be inhabited and occupied by the buyer but that it is going to be rented out.

I think that probably it makes sense not to have the buy-to-let in this directive because it is not purely residential anymore, and it comes under specific regulation that would not be compatible with this directive. This product as it stands, buy-to-let in the UK, does not exist as such in most other countries. It should not come into the same regulation as a purely residential mortgage, I would say—although this is not really for me to say, but if you ask me my opinion—all the more so because it is regulated at national level, if I understand it well.

The Chairman: Colleagues, I will take your advice if I may—I am addressing Lady Hooper and Lord Marlesford—we have run over time, and it is my intention to take Ms Lambert for a drink and colleagues would be most welcome to come and join us after this session. I will also ask if she will reply to the remaining questions, but unless either of you are very keen, I would like to close the session.

Q41 Lord Marlesford: Lord Chairman, if I may, I was very interested in what we were told about the difference in transaction costs between Belgium and Britain. I wondered whether we could be supplied with any statistics that you have comparing the EU countries that you represent in terms of some of the basic stuff: what proportion of home ownership; what proportion of people have mortgages? Whatever you have easily available I think we would find very useful to have to give us some feel for Europe.

Annik Lambert: We have comparative surveys and publications easily accessible. I can have them sent to you.

The Chairman: On that note, first of all I would like to thank you very much indeed for your very interesting answers. If you feel you would like to tackle some of those issues we have not had time to do, please write to us. We will send the transcript. If you can correct

it, that would be most useful. In the mean time I am going to close the evidence session now with thanks to Annik Lambert. But can I say to colleagues that I am taking both Annik Lambert and Ms Bennett for a drink downstairs, and if colleagues would like to join us in the Peers' Guest Room just to carry on the conversation a little bit, you would be most welcome to join us. But thank you very much indeed, everyone, for getting in a really good session.