Study on Equity Release Schemes in the EU
Part II: Country Reports
Project No. MARKT/2007/23/H

submitted by
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The country reports in Part II of the final report for this study on Equity Release schemes (ERS) in the EU, contain country-specific information and some comparative statistics from the Part I of the Report.

The development of these country reports has relied on the following different sources:

- Questionnaire for financial supervisors, central banks, provider and consumer organisations with open as well as closed questions on the situation of ERS as well as on existing barriers in the respective country;
- Questionnaire for Providers with some open questions concerning products, markets, general situation in their country and their opinion on risks and barriers;
- Expert reports from legal experts adding factual information;
- Interviews with specialists in the UK, Spain, Germany and France;
- Statistical information from the OECD, the European Mortgage Federation and literature.

The country reports are behind the analysis and conclusions of the main report. The following items broadly provide the basic structure for the country reports:

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The country reports are presented using the groups identified in the Socio-economic analysis section E. of Part I: General Report. The first group described contains the three EU Member States where the market for ERS is the most developed, namely, the UK but...
also Spain and Ireland. These are followed in the next section by another seven countries where ERS exist and where their markets will generally only contain offers for Loan Model ERS. The third group is made up of two countries where only Sale Model ERS currently exist and where business is currently conducted on a very small scale. The fourth group of countries is composed of those countries, which for various reasons, do not have ERS available in their national markets. This latter group can be divided into two sub-sections. Starting with Belgium, where legal barriers have been identified and significant preparatory work has been undertaken to allow for the introduction of a Loan Model ERS, another seven countries namely, Greece, Malta, Portugal, Poland, Slovakia as well as Denmark and the Netherlands, serve as examples to explain why ERS are not available in all EU Member States. The remaining group containing further statistical analysis of market conditions for the introduction of ERS, covering Slovenia, Cyprus, Luxembourg, Czech Republic, Estonia, Latvia and Lithuania, where all of the respondents indicated that there was no equity release market and that there were no barriers to the introduction of ERS in their country.

The country reports were assembled by the research team at iff with the help of legal experts from the countries concerned, and have used the answers received from the stakeholder and provider questions contained in the survey questionnaire. The level of detail for each country varies based on the development of the ERS market, the regulatory framework, the quantity and content of country responses received and material from interviews. Each country report contains a table with core statistics for the country alongside a column containing the EU median average value for the corresponding indicator. The data is indicative only, and some is based on own internal iff calculations. The source for the statistics is the European Mortgage Federation, using statistical tables from its Hypostat 2006 A Review of Europe’s Mortgage and Housing Markets, 11/2007 for Total Outstanding Residential loans, Owner occupation rates, and to derive average house price growth and the number of housing transactions per capita. It is important to note that concerning the statistics used for home ownership, these refer to owner occupancy rates for households, a figure that can be very different to other homeownership ratios from other sources such as Eurostat. The lack of official harmonised definitions at European level for housing also affects mortgage indicators. Data on residential mortgage lending outstanding refer to all Home Loans (i.e. loans granted for housing purposes, mortgage loans granted for consumption purposes and housing loans that are either unsecured or secured by non-real estate). Population, old-age dependency data are available from the Eurostat online database. Statistics on net replacement rates by individual earnings level for mandatory pension programmes are from the OECD online database, as are data on the level of assets in private pension funds. With reference to the questionnaires used to gather the information (SQ for stakeholder questionnaire, and PQ for provider questionnaire), answers from these were broadly allocated to the following country sections: General information (SQ items 2.7; PQ item 1), Market/Product/Provider/User (SQ items 1-3; PQ items 3-6 and 9), Law & Regulation (SQ items 5 and 8; PQ items 2 and 7), Risks/Benefits/Barriers (SQ items 1.3, 4, and 6-7; PQ item 8).

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2 The two exceptions being Hungary and Germany where Sale Model offers also exist alongside Loan Model.

3 It should be noted that at the closing stages of our research, a provider whose product appears to meet the definition of a Sale Model ERS was identified in the Netherlands. However, because no information about this product or the market for it was available at the time of publication, the Netherlands has been classified in Group 4 alongside Member States with no ERS. Please take note of this technicality.

4 Caution in terms of comparability must also take account that these owner occupation ratios will sometimes include businesses as well as households. The figures also refer to data from different years (ranging from 2001 to 2006), and the latest year’s data available has been used.

**Group 1: Member States with significant ERS**

From the findings of our research, there are three EU countries that detach themselves with regard to the overall importance, awareness, and extended existence of ERS and markets. The first country in this grouping, the United Kingdom (UK), has by far the most sophisticated ERS market, based on any of the possible criteria that can be used to measure so called development of the market: size of business, number of providers, number of years for which products exist, level of consumer awareness with ERS, or quantity of literature, material and analysis describing the market. A number of countries, but the UK especially, is already demonstrating the market-driven process of product innovation when circumstances present an opportunity. By allowing the free-market forces of creative enterprise to be rewarded, EU citizens are likely to have loans tailored increasingly to general demographic evolution, and hopefully, if the observations featuring in the previous 'Risks and Benefits' section in Part I of this report are taken into consideration, increasingly tailored to their personal circumstances and needs as well. Though small in comparison with the UK in terms of size of the market, Spain and Ireland also have a significant number of providers and share a number of similarities which have played a favourable role in the development of a market for ERS, the most obvious one being a dynamic housing market that has seen very strong growth in prices.
## United Kingdom

<table>
<thead>
<tr>
<th>Category</th>
<th>United Kingdom</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>70.0</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>10.0</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>59.0</td>
<td>20.6</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>1745.8</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>8.9</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>86.3</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>28760</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>41.1</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>30.0</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>24360</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>61.3</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>15.4</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>24.3</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>16.1</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>40</td>
<td></td>
</tr>
</tbody>
</table>

Because of the size and maturity of the Equity Release market in the UK (judged on the basis of the number of providers, number of transactions, and number of years of existence), the research team conducted an especially in depth analysis of the UK situation. Face to face meetings and telephone conferences with the major stakeholders complemented and strengthened the understanding of information received through the questionnaire. Of the many stakeholders interviewed and expertise shared, iff would like to particularly thank Prof Iain Ramsay and Prof Toni Williams from the University of Kent Law School, and staff at the following organisations that shared their insights and knowledge: SHIP, the Financial Services Authority and the Financial Services Consumer Panel, the ABI, Norwich Union, Which? and all those who contributed with their questionnaires.

### 1. General information

Sometimes referred to as a nation of homeowners, the UK has a high owner occupancy rate, a large financial services market, and an appetite for both innovation and credit. With a high level of home ownership in the UK, the market for ERS is continually evolving, with an increasing number of product providers entering the market, based on...
an increasing recognition that the population in the age bracket 55-65+ is growing (it now stands at 17.2 million people in the UK alone) and that their need to pursue their lifestyle in retirement cannot be supported by savings, pensions and investments alone. The amount of equity that people have tied up in their property has grown very rapidly and over a sustained period over decades. The more recent falls in house prices have not wiped out the big price increases of the past, meaning that for many, their property is still an attractive and accessible financial asset.

Before describing ERS in the UK, it may be useful to briefly describe the mortgage credit market from the outset. The UK mortgage market is highly competitive with thousands of products available from many lenders, although a reduction in the products offered has been seen in recent months. 32% of the UK population over the age of 18 hold a mortgage. There has been a strong increase in the remortgage market in recent years - consumers have moved mortgage to get a better deal even though they are not moving home. There are two distinct sales channels - direct to consumer (which accounted for 33% of mortgage sales in 2007) and third party intermediaries (which accounted for 67% in 2007). The UK mortgage market has grown strongly in recent years, supported by rising house prices, low interest rates and increased competition amongst lenders. Over GBP 1 000 billion (EUR 1 180 billion) of mortgage balances are outstanding - balances have doubled in the past 6 years. In June 2008, the average UK homebuyer put down a 22% deposit, the average first time buyer borrowed 3.33 times their income and the average home mover borrowed 2.94 times their income. The majority of lending continues to be on conservative terms, as lending criteria have tightened in response to the shortage of funding and current market conditions, including a slowing housing market. A very large increase in the number of older owner-occupiers (those aged 60 and over) is in prospect over the next 20 years, estimated as a 2.8 million increase between 2006 and 2026 with the proportion of older households aged 60 and over rising from 71% in 2006 to 75% in 2026. Much of this reflects the ageing population. The value of unmortgaged housing equity owned by older households stood at GBP 1 000 billion in 2006.

2. Products

Both types of ERS are offered throughout the UK.

Products today bear no resemblance to those that were prevalent a few decades ago. The Home Income Plans and shared appreciation mortgages do not exist anymore. Lifetime mortgages (Loan Model ERS) are the most offered product, but the Home Reversion product (Sale Model ERS) has existed in its current form for a very long time.

There has been a clear move towards more flexible product offerings, the flexibility of these new plans allow a whole range of possibilities from taking lump sums to a series of smaller sums or access to the equity on an ad-hoc basis. The drawdown facility is popular for a number of reasons, but other features that either cap the level of indebtedness or guarantee a remaining share of the property value for the estate are also becoming increasingly common. This is likely to be the result of competition in the equity release market, whereby individual niches are being served by offering specific features catering to ever more differentiated customer needs. However, this provider

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6 Using the Halifax House Price Index as a measure of UK national house price statistics, the average UK house price which reached GBP 100 000 in January 2002 and peaked at GBP 199 770 in August 2007, now stands at GBP 168 176 as of October 2008. Forecasts from Summer 2008 from the website http://www.housepricecrash.co.uk/ range from Nationwide expecting a 25% decline between 2008-2010 in the UK housing market and the National Housing Federation predicting that the average house price in England will rise by 25% per cent over the next five years to reach GBP 274 700.

7 These were rather experimental and were offered only on a small scale by Barclays and Bank of Scotland. However, their lack of success may have been down to timing as well, as they were introduced at a time of a buoyant housing market and upward trend in house prices which does not favour these forms of ERS.
market-led experimentation to find the right product has led to an increasingly complex market. This increased complexity means that professionals advising and selling these ERS to the customer, typically intermediaries in the UK, face the burden of research and are responsible for keeping abreast of latest products etc., which we will return to in the section discussing risks and benefits.

One feature of the equity release market in the UK testifying to its advanced maturity in comparison with other domestic markets of the EU, is that products with a drawdown feature, where the consumer has an overall borrowing facility that they can choose when to access (draw down) are now the most popular product being sold. According to the standard setting trade body SHIP, these drawdown products account for 58% of equity release plans sold in Q3 2008 as opposed to 40% in Q1 2007. These drawdowns can apply to home reversions just as well as lifetime mortgages, and the minimum amounts for individual drawdowns (like those applicable to lump-sum payments) are determined and specified by the individual firm rather than through regulation.

a) Loan Model ERS: Lifetime mortgage

As explained in the general section of the report, lifetime mortgages allow the consumer to borrow a sum of money up to a maximum loan-to-value ratio set by the provider depending on the age (and the partner’s age if appropriate). For a given property value, most products are offered amounts based on similar ratios, however, some providers may offer to lend higher amounts in return for a higher interest rate. In addition, if the maximum loan size is not taken out from the outset, there may be restrictions on some products which limit the time after which further advances are allowed.

Interest rates are fixed for life in all the product offerings seen. Though almost all providers in the UK calculate fees for early termination of the contract (early repayment charges, also known as early redemption fees or prepayment penalties) based on a backward sliding scale where the percentage of the product value decreases over time, one major provider has in fact suggested a different method based on the market interest rate prevalent at the time. This last method is said to be fairer (more closely reflecting the actual true cost of adjustment) but is often perceived by consumers as more complicated to understand. Although the former method penalises everybody, it is transparent.

b) Sale Model ERS: Home reversion plan

Unlike the Loan Model ERS where the legal structure involves the provider placing a charge against the customer’s property, with the Sale Model ERS, as elsewhere, the provider buys a share of (or all) of the customer’s property so that there is a transfer of ownership. As part of the transaction, a lease for life is granted to the customer enabling them to live in the property for the rest of their life. The contract will also generally contain other important rights such as the ability to move to a suitable new property. Sale Model ERS will almost always enable the consumer to obtain a larger amount of

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8 As reported by SHIP in October 2008, the flexible nature of the drawdown product, by allowing consumers to take a small sum initially with the option to get at more if needed, has led to a year on year growth of 12% in the number of these types of products sold (4 577 in Q3 2008 – constituting GBP 219 million of commitments and GBP 118 million of advances in Q3). See http://www.ship-ltd.org/bm~doc/21-october-2008.pdf.

9 Preferences were voiced by the UK consumer association Which? in 2006 when it reported that “Norwich Union’s early redemption charge (ERC) is based on the performance of gilts so it’s hard for customers to work out in advance what it will be.” See http://www.money-advice.net/media.php?id=3162. However, as reported in a 2007 report done for the Equity Release Working Party of the Actuarial Profession “Although most providers still offer products with fixed rate charges applied irrespective of market movements (ranging from 3% flat for the first 5 years and nil thereafter, to 7% initially stepping down to nil after 10 or 20 years), mark to market penalties are becoming more common (i.e. with the charge applied depending on interest rate movements between inception and repayment)”. See http://www.actuaries.org.uk/__data/assets/pdf_file/0013/37012/sm20071029.pdf.
funds than would be possible using a Loan Model ERS. As opposed to the Loan Model ERS, which have evolved in terms of accessing funds, the majority of Sale Model ERS are still sold as cash products (reversion paid as a single cash lump sum at the outset of the scheme). This results from a general trend for the market to provide unbundled products and the fact that only a life assurance company can be authorised to offer a monthly payment version of ERS. Most providers however will offer cash reversions with the optional purchase of an annuity if required, but as mentioned it is generally assumed that an annuity could be bought with the cash.

Two of the 12 home reversion products also offer an impaired health option, a feature which it is so far uncommon for Loan Model products to have. This is an offer with enhanced terms as a result of a medical illness which is very likely to affect one’s life expectancy. Furthermore, two providers of home reversions offer a product variation which contains a growing transfer of the equity over time. These stepped reversions mean that the amount that is repaid by the consumer is expressed as a proportion of the property sale proceeds. The proportion starts as the share of the initial advance to the initial property value and steps up by a fixed percentage each year, adjusted for further payments as they are made. These features overcome the main criticism of reversions, that the schemes are very expensive on early death (though the disadvantage is that the amount of equity, which will be committed and transferred to the provider, is uncertain).

c) Sale and lease back

Also in need of mentioning at this point is the sale and lease back market, also and more accurately referred to as 'sale and rent back'. Such offerings are different to ERS not just because of their lack of regulation, but because they confer no absolute security of tenure and will require regular payment from policyholders in the form of a monthly rent. As opposed to the regulated equity release products that give consumers the right to live in their homes for life, sale and rent back arrangements involve a company buying an owner’s home for significantly less than the market value, and then allowing that person to continue living in the property, but only by paying full market rent and often with only an assured short hold tenancy agreement. There are thus no guarantees that the consumer will be able to stay in the property long term. There is little reliable data on the size of the industry. However, it is likely that there are upwards of 1,000 firms, together with an unknown number of non-professional landlords, who have conducted about 50,000 transactions to date. Although not an ERS, sale and rent back arrangements should be discussed in some detail here because of their potential to cause serious and permanent harm to often vulnerable homeowners. Irrespective of whether there is regulation or not, the very nature of these unconstrained alternative products to ERS makes it important for this study to help distinguish these from ERS. As mentioned elsewhere in the report, the UK can serve as a good example because the competition authorities have just published their study on what is in that country a relatively new type of property transaction whereby firms buy homes from individuals, usually at a discount, and then allow those individuals to stay on in the property as tenants. Among the findings from the OFT report12 are that some consumers enter into sale and rent back back

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10 Also referred to as income based schemes, these products are those where consumers access their funds released on a regular basis (e.g. annually) either for a set period e.g. 10 years, or for life. Though schemes with this payment method can usually be combined with lump sum schemes to provide a higher advance at outset followed by a regular income, there will be extra risks involved for the provider (when the property reaches a negative equity situation) if the product confers a guaranteed level of income for life. See http://www.actuaries.org.uk/__data/assets/pdf_file/0013/37012/sm20071029.pdf.

11 In response to a more challenging economic environment for indebted homeowners in the UK and aggressive marketing and misleading advertising by providers of these schemes, the UK ERS trade body SHIP launched a consumer checklist on sale and rent back in order to help consumers differentiate between these and Equity Release schemes. See http://www.ship-ltd.org/bm~doc/06-oct-08.pdf.

12 During this short market study, the OFT looked at the characteristics of the sale and rent back product, the circumstances in which these products are sold and considered whether existing consumer protection legislation is sufficient and effective. This included contact with trade bodies, consumer groups, industry
transactions when this is not the best option for them; that firms may mislead customers as to the value of their property or the security they have as tenants; some firms impose substantial rent increases or even evict tenants (this can also be caused by landlords defaulting or tenants themselves not being able to afford the agreed rent). As a result, the main recommendation of the OFT report is that there should be statutory regulation of the sale and rent back sector by the Financial Services Authority (FSA). If the decision is taken to regulate these products, the details of regulation will be up to the FSA to determine but the OFT considers it should include an obligation on firms to be more transparent (about the initial valuation, the terms of the tenancy, rent) and a requirement on firms to tell consumers about the free, independent advice available to them before they decide to sell.

3. Providers

There are 40 providers of ERS in the UK. These range from big insurance companies to smaller specialised outfits. Of these forty, some will no longer be active and will only still be holding loans on their books (in the case of Loan Model ERS). 22 providers have signed up to the codes of conduct of the Safe Home Income Plans (SHIP) by becoming a member of the trade body concerned with product safety. Of these 22, 6 offer a Sale Model (three of which offer at least two similar products but with different features and under a different product name), and only two providers sell both Loan and Sale Model to their clients. Sales of ERS per year for these 22 providers represent over 95% of the total market in value terms, and very close to 100% in the Sale Model market.

The development of the market in the UK especially stands out by the overwhelming role played by intermediaries. These are professionals who are not the originators of the product but who come into contact with the consumer and from whom the majority of UK consumers buy their Loan Model or Sale Model ERS. The legal rules applying to these advisers and brokers are mentioned below. It is interesting to note that ERS are sold exclusively between direct marketing or intermediaries, and that there is a stark difference between the channels used depending on the type of ERS concerned. Credit-based Loan Model products (called lifetime mortgages in the UK) are transacted 81% of the time through intermediaries, whereas the corresponding figure for Sale Model products sold via intermediaries is only 66%.

High Street providers have been attracted to ERS, which has given the market a credible presence and should pave the way for more providers of this type to enter. Between Q1 and Q2 2008, the value of the equity release market grew by 14%.

4. Markets

As of the end of 2007, statistics from the Council of Mortgage Lenders show the value of loans to be GBP 154 983 million (EUR 211 336 million). The value of total equity release over the 12 month period up to March 2008 is just over £1 159 million, with home reversions currently making up approximately 5% of the UK equity release market. Based on the estimated market sizes from the findings of this research, the market in

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13 These calculations have been made using figures provided by SHIP in October 2008 (covering ERS for only their 22 members) and adjusting these with the difference from the combined figures from the Council of Mortgage Lenders as reported in their ‘Please release me!’ report in March 2008 conducted by Peter Williams: http://www.money-advice.net/media.php?id=3251.

14 See Section 5.c) of the UK country report on the regulation of intermediaries (on p.12).

15 Based on a currency conversion using the exchange rate of 0.73335 EUR/GBP as of 31.12.07.
ERS in the UK represents by far the most significant market for ERS in the EU as a whole.\footnote{Figures for the UK market size at end 2007 come from Response PQ28. These are consistent with figures available elsewhere. Data on national ERS market size have come from stakeholder questionnaires and interviews with regulators and providers of ERS. See Part I: General Report C.1. for an overview of the EU market, and Part III: Annexes for a list of stakeholders who have participated in our research.}

The relatively widespread development of ERS in the UK market, together with some severe experiences with mis-selling mean that the regulatory environment was forced to adapt out of necessity. One result of this mis-selling and potential reputational damage for the entire product ranges as a result of the unsafe ‘Home Income Plans’ of the 80’s, where interest rates were not fixed, stock exchange performance changed direction, home prices fell, and because funds released were used for investment on the stock exchange, many people lost their homes.

There was thus a need to have parameters in place and therefore Safe Home Income Plans (SHIP) was created. This industry self-regulation does not exist anywhere else in Europe. This regulation and organised supply-side of the UK equity release market, make statistics on the nature of the distribution of these products available.

The UK has a cultural predisposition towards releasing the equity which one may have accumulated in their housing asset over the years, and the average UK consumer is generally familiar with the concept behind equity release. The existence of mortgage withdrawal more broadly and in its different forms, allows a smoother transition to equity release products (for consumers and for providers). It may not be a building block as such but providers will be more familiar with lending based on collateral value, notwithstanding the added element of needing to assess mortality risk that is intrinsic to ERS. This explains why in the UK, these products are often associated with insurers (though this is slowly changing). The small market does not provide the economies of scale that mainstream banks are used to and thus is not likely to see considerable new activity by the more established financial institutions in the medium term (mis-selling in the past also constitutes a barrier for reputational concerns).

A recent detailed analysis of the market was done by the Mintel report\footnote{Iff researchers have not purchased this report for the purposes of this study. See outline http://reports.mintel.com/sinatra/reports/display/id=290769#about.} which is bullish on the effects of the credit crunch on the ERS market, and despite the fact that Northern Rock and Bradford and Bingley have faced severe difficulties, the ERS business is in itself not typically funded on the securitisation market (because there is no income stream to securitise).

A reason for the variety of products is that some customers will prefer to go to the big names and more established players such as Norwich Union, while others will prefer to shop around (either on their own or through an independent financial adviser (IFA)). The typical user of ERS will also be different, e.g. home reversions are generally preferred by those who want to extract a greater lump sum immediately. Some products concentrate on a specific category of users, e.g. offering enhanced terms for impaired health (4 providers\footnote{Based on information from SHIP provided to iff on a confidential basis.}), or react to social preferences e.g. the rising demand for domiciliary care.

5. Legal situation

Both Loan and Sale Model ERS are regulated by the FSA. The regulatory regime consists of eleven “high-level” Conduct of Business principles, which apply to all financial
transactions within the FSA’s jurisdiction; detailed rules in the Mortgage Conduct of Business Sourcebook (MCOB) on matters such as advertising and promotions (MCOB 3), responsible lending (MCOB 11), and charges (MCOB 12) applicable to all regulated mortgage and home finance contracts; and specific rules, also in the MCOB, that adapt the FSA’s rules on disclosure (MCOB 9) and advice (MCOB 8) to the particular characteristics and circumstances of loan and sale forms of equity release. These adaptations are described in detail below on page 17 in Section 5 (g).

a) Licence

Authorisation and licences are required by a provider wishing to sell an ERS whether this scheme is a Loan or Sale Model ERS.

The authority to regulate ERS stems from the Financial Services and Markets Act 2000, (hereafter FSMA) as amended by the Regulation of Financial Services (Land Transactions) Act 2005. The FSMA implemented a comprehensive reform of the structure of financial regulation in the UK and the Regulation of Financial Services (Land Transactions) Act 2005 extends the FSMA regulatory scheme to Home Reversion Plans. A central aspect of the reforms is the establishment of the FSA as regulator of a large range of consumer financial products and markets. The FSMA came into force at the end of 2001 but mortgages were not originally subject to the FSA’s rules as a ‘regulated activity’. The FSA assumed jurisdiction over home finance transactions in the form of first charge mortgages (defined as loans secured on land), including lifetime mortgages, on October 31, 2004. Home reversion plans are not structured as loans secured on land and thus were not part of the FSA’s original mortgage regulation regime, nor were they subject to any other set of regulatory rules authorised by a statute. (Home Reversion Plans and Lifetime mortgages are governed by the Code of Conduct published by the Industry body, Safe Home Income Plans (SHIP), when provided by a SHIP member). In 2005, the government passed the Regulation of Financial Services (Land Transactions) Act 2005 to permit extension of the FSMA regulatory scheme to Home Reversion Plans. This extension was implemented in April 2007, since which date the Sale Model form of equity release (home reversion plan) has been governed by the same regulatory system as credit arrangements.

The basic scheme of control under the FSA regime is that persons who provide, administer, arrange for, or advise on equity release transactions by way of business
must be authorised or be exempt from authorisation\textsuperscript{24}. Contravention of the authorisation requirement is a criminal offence under section 23 of the FSMA, (unless the person falls into one of the exemption categories). Authorisation requires the firm to meet general threshold conditions for running a financial services business in the UK (relating to legal form and status of the business, location of offices, adequacy of its financial resources, and competence, suitability and fitness of its management and other human resources), and to obtain permission to provide the particular FSMA regulated activities that the firm intends to offer.

b) Regular controls and Supervision

The FSA has extensive supervisory powers, detailed in its supervision handbooks, which apply to all of the financial firms that it regulates, including investment and insurance as well as the mortgage and home finance markets\textsuperscript{25}. The FSA describes its approach to supervision as ‘risk-based’ by which it means that it adjusts the resources devoted supervision according to the perceived risk that different categories of financial firms, products and services are thought to pose to the FSA’s regulatory objectives of (1) maintaining confidence in the financial system; (2) promoting public understanding of the financial system; (3) appropriate consumer protection; and (4) reducing financial crime. The FSA’s supervisory activities include regular reporting by firms, documentation review, site visits, mystery shopping, education and training, circulating documentation such as good and bad practice guidance and thematic reports on particular aspects of financial services markets and the exercise of disciplinary powers. The FSA has powers to censure and fine financial firms and to cancel permission to carry out regulated activities, or terminate authorisation.

Specifically in relation to the equity release market, the FSA maintains a regular reporting system and conducts site visits. It has published findings from two mystery shopping studies, which show widespread non-compliance with disclosure and advising standards;\textsuperscript{26} the FSA also has published a good practice guide and a letter addressed to mortgage advisors with low levels of equity release business, alerting such firms to the regulatory requirements for advisory work in this sector.\textsuperscript{27} Lifetime mortgages have been incorporated into the FSA’s thematic review of the effectiveness of mortgage regulation. The FSA has taken disciplinary action against at least one small intermediary for failings in relation to advising equity release consumers\textsuperscript{28} and the FSA has negotiated changes to

\textsuperscript{24} Exemption from authorisation means that the activity is regulated by the FSA but the actor belongs to a category of persons that does not require authorisation under the FSMA. Exemptions are stipulated in the Financial Services and Markets Act 2000 (Exemption) Order 2001 (available at: http://www.opsi.gov.uk/si/si2001/20011201.htm). The original instrument, SI 2001 No. 1201, is periodically amended to modify the categories of exempt persons. The FSA’s April 2006 Consultation document on Regulation of Home Reversion and Home Purchase Plans (available at: http://www.fsa.gov.uk/pages/Library/Policy/CP/2006/06_08.shtml) references the following categories of exempt persons that potentially may undertake regulated activities pertaining to equity release transactions (para 4.16):

(a) an appointed representative (this status is discussed below);
(b) an exempt type of professional firm (e.g. solicitors, accountants or actuaries) whose participation in regulated activities is "incidental to its main business";
(c) a registered social landlord in Scotland, England and Wales;
(d) the Housing Corporation, Scottish Homes and The Northern Ireland housing Executive;
(e) a municipality.

\textsuperscript{25} See http://fsahandbook.info/FSA/html/handbook/SUP.


\textsuperscript{27} The good practice guide is referenced in the annex to the letter to mortgages advisors: Lifetime Mortgages: Letter addressed to firms carrying out low volumes of business by the FSA (2007), available at http://www.fsa.gov.uk/pubs/other/letter_lifetimemortgages.pdf.

\textsuperscript{28} Final Notice to The Minel Group 2007, available at: http://www.fsa.gov.uk/pubs/final/minel_group.pdf. The FSA found that the firm’s procedures were inadequate to control the quality of advice it provided to consumers interested in lifetime mortgages; and in particular that the advisors were unable to show that
the standard contract terms of a major equity release provider using its powers under the Unfair Terms in Consumer Contracts Regulations. These changes affected two terms that the FSA regarded as creating a “significant imbalance” in the rights and obligations of the contracting parties. Both terms concerned the maintenance and repair obligations of the consumer’s estate during the period between the consumer’s death and the sale of the property. One impugned term essentially imposed on the consumer’s estate liability for maintenance costs and taxes until the property was sold, but did not impose any obligation on the firm to take reasonable steps to secure a timely sale. In response to the FSA’s complaint that the term as drafted contravened Regulation 5 (as well as the FSA’s own MCOB rule requiring firms to take reasonable steps to sell the property within a reasonable period of time (MCOB 2.6A.15R)) the firm added a new term to its standard contract that specified the firm’s obligation to “take reasonable steps to ensure that the Property is sold within a reasonable period of time” and setting out a non-exhaustive list of “legitimate reasons” for the firm to delay a sale. Under the second impugned term, the firm had assumed “absolute discretion about dealing with any management, repair and maintenance of the Property which we consider necessary pending sale”. In this instance the FSA regarded the absence of any reasonableness constraint on the firm’s discretion as a breach of Regulation 5 and as potentially permitting the firm to act in breach of the FSA’s Treating Customers Fairly principle for business by for example demanding that the estate pay for repairs that improved the condition of the property beyond the state it was in at the time of the lifetime mortgage. The firm claimed that it did not rely on the term to exercise its discretion unfairly, but agreed to add explicit wording that clarified the respective responsibilities of the firm and the consumer’s estate.

c) Regulation of intermediaries

The licence compulsory for intermediaries actively selling ERS is an authorisation given to the firm by the FSA. It involves both the registration in a list by the aforementioned regulator, and imposes a code of conduct on the provider of these products or advisory services.

The authorisation scheme outlined above governs the activities of ‘arranging for’ and ‘advising on’ (and agreeing to arrange or to advise on) and as such, it applies to equity release intermediaries as well as to providers. There are, however, two caveats or clarifications to consider in relation to intermediaries.

First, section 39 of the FSMA creates a category of ‘appointed representative’ of an authorised person, who is exempt from authorisation and thus from direct regulation and supervision by the FSA. An appointed representative is not exempt from FSA requirements, for example in relation to disclosure, advising standards and other conduct of business regulation, but responsibility for the securing compliance by the appointed representative lies with the authorised person (principal) who made the appointment and

they adequately determined customers needs and objectives and provided suitable advice. The FSA found also that the firm did not adequately train its staff about the risks of lifetime mortgage products nor did the firm put in place systems for monitoring staff competence in the sale of lifetime mortgages. The Minel Group was fined £10,500 for exposing customers to the risk of being sold an unsuitable equity release product; it was required to review its sales of lifetime mortgages since it had been FSA authorised with a view to compensating customers losses caused by unsuitable advice, and required to withdraw from the lifetime mortgages market.


30 The Unfair Terms in Consumer Contracts Regulations 1999, SI 1999 No. 2083, Reg 5. NB: The FSA is a Qualifying Body under the regulations which means that it has powers to consider complaints about contract terms, to secure administrative remedies, such as a firm’s undertaking not to rely on an unfair term, and to apply for an injunction to prevent reliance on an unfair term. It does not have the power to give an authoritative “legal” determination of whether a term contravenes the Regulations.

who is subject to FSA discipline and penalties. In relation to equity release and other home finance transactions, appointed representatives may engage in arranging and advising activities.\(^{32}\)

Second, the regulatory scheme excludes the activity of ‘introducing’ from the regulated activities of ‘providing’, ‘arranging for’ and ‘advising on’ financial products and services including home equity transactions. The FSA regulates ‘introducing’ by requiring disclosure of relationships between introducers and the person or firm to whom the consumer is referred and of the fee or any other financial benefit received by the introducer.\(^{33}\)

d) Bank Law

The Glossary of the Financial Services Authority Handbook\(^{34}\) defines an equity release transaction as "a lifetime mortgage or a home reversion plan". The Glossary defines a lifetime mortgage as:

... a regulated mortgage contract under which:

(a) entry into the mortgage is restricted to older customers above a specified age; and

(b) the mortgage lender may or may not specify a mortgage term, but will not seek full repayment of the loan (including interest, if any, outstanding) until the occurrence of one or more of the following:

(i) the death of the customer; or

(ii) the customer leaves the mortgaged land to live elsewhere and has no reasonable prospect of returning (for example by moving into residential care); or

(iii) the customer acquires another dwelling for use as his main residence; or

(iv) the customer sells the mortgaged land; or

(v) the mortgage lender exercises its legal right to take possession of the mortgaged land under the terms of the contract.

and

(c) while the customer continues to occupy the mortgaged land as his main residence:

(i) no instalment repayments of the capital and no payment of interest on the capital (other than interest charged when all or part of the capital is repaid voluntarily by the customer), are due or capable of becoming due; or

(ii) although interest payments may become due, no full or partial repayment of the capital is due or capable of becoming due; or

(iii) although interest payments and partial repayment of the capital may become due, no full repayment of the capital is due or capable of becoming due.\(^{35}\)


The extension of the FSA's regulatory jurisdiction to Home Reversion plans is authorised by: The Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.2) Order 2006 (No. 2383). The Order³⁶ sets out the following definition:

a) a ‘regulated home reversion plan’ is an arrangement comprised in one or more instruments or agreements, in relation to which the following conditions are met at the time it is entered into—

(i) the arrangement is one under which a person (the ‘plan provider’) buys all or part of a qualifying interest in land (other than timeshare accommodation) in the United Kingdom from an individual or trustees (the ‘reversion seller’);

(ii) the reversion seller (if he is an individual) or an individual who is a beneficiary of the trust (if the reversion seller is a trustee), or a related person, is entitled under the arrangement to occupy at least 40% of the land in question as or in connection with a dwelling, and intends to do so; and

(iii) the arrangement specifies one or more qualifying termination events, on the occurrence of which that entitlement will end.

The Handbook Glossary basically sets out this definition, with minor modifications. Thus, the Glossary defines a Home Reversion Plan³⁷ as:

"... an arrangement comprised in one or more instruments or agreements which meets the following conditions at the time it is entered into:

(a) the arrangement is one under which a person (the reversion provider) buys all or part of a qualifying interest in land from an individual or trustees (the reversion occupier);

(b) the reversion occupier (if he is an individual) or an individual who is a beneficiary of the trust (if the reversion occupier is a trustee), or a related person, is entitled under the arrangement to occupy at least 40% of the land in question as or in connection with a dwelling and intends to do so; and

(c) the arrangement specifies that the entitlement to occupy will end on the occurrence of one or more of:

(i) a person in (b) becoming a resident of a care home;

(ii) a person in (b) dying; or

(iii) the end of a specified period of at least twenty years from the date the reversion occupier entered into the arrangement;

in this definition 'related person' means:

(A) that person's spouse or civil partner;

(B) a person (whether or not of the opposite sex) whose relationship with that person has the characteristics of the relationship between husband and wife; or

(C) that person's parent, brother, sister, child, grandparent or grandchild."

e) Housing Law

The Social Security (Housing Benefit, Council Tax Benefit, State Pension Credit and Miscellaneous Amendments) Regulations 2004, No. 2327 Reg.2(10)(b) inserts into the Housing Benefit Regulations the following definition of an 'equity release scheme': a loan

(a) made between a person ("the lender") and the claimant;
(b) by means of which a sum of money is advanced by the lender to the claimant by way of payments at regular intervals; and
(c) which is secured on a dwelling in which the claimant owns an estate or interest and which he occupies as his home. The purpose of the definition is to add any income paid regularly under an equity release scheme to the "types of income which are prescribed for the purposes of section 136A(3) of the Social Security Contributions and Benefits Act 1992 (c. 4)"

The quoted definition now appears in:
- Statutory Instrument 2006 No. 214 Social Security: The Housing Benefit (Persons who have attained the qualifying age for state pension credit) Regulations 2006, Reg. 29(1)(w). It can be seen that this definition would apply only to the lifetime mortgage type of product.
- Statutory Instrument 2006 No. 216 Social Security: The Council Tax Benefit (Persons who have attained the qualifying age for state pension credit) Regulation 19(8).

ERS are not specifically regulated by either tax law or contract law, however there is a specific feature of the UK relating to entitlement to state benefits which makes the product market dependent on the income characteristics of the potential consumer. These will be discussed in the following section on legal impediments to development of the Equity Release market.

f) Self-regulation - SHIP

In addition to the principles and rules established by the FSA to regulate the products and practices of the mortgage and home finance industry, there is an industry trade body that has developed basic but fundamental codes to which its members’ products must abide.

Safe Home Income Plans (SHIP)\(^{40}\) is a trade association founded in 1991. It now has 22 members covering over 90% of the volume of the Equity Release market in the UK. Providers not included are generally small firms with the exception of two big ones, Scottish Widows and the Royal Bank of Scotland. One main reason why these firms prefer to remain outside the membership of this trade association may be due to the cost associated with the body’s self imposed rule of having to provide independent legal advice (as these providers may have alternative preferred structures in place).

SHIP and its members try to ensure customer safety in the equity release market by requiring all members to abide by a Code of practice which itself has developed over time. These safeguards are:

- A right to live in their homes until they either die or move into long-term care.
- A guarantee that they will never owe more than the value of their property and therefore there will never be a debt left to their estate.
- In the event of a lifetime mortgage, the interest rate will either be fixed or capped so that they will know how much they owe at any one time and they will not have to worry about interest rates spiralling out of control.
- They can move from their main residence without financial penalty.

\(^{40}\) See http://www.ship-ltd.org/.
They must take independent legal advice and their solicitor must sign the SHIP certificate to confirm complete client understanding.

All applications must come from a specifically qualified adviser whom has followed a robust advice process, including the consideration of implications for you and your family.

All members of SHIP agree to provide fair, simple and complete presentation of their plans.

What the Code basically provides for are important consumer safety measures such as:

- Insistence on obtaining independent legal advice;
- Fixed or capped interest rates;
- Clear easy to understand plans;
- No negative equity guarantee;
- No pre-payment fee on moving property (new home must however meet terms and conditions of provider); etc.

However, there are also areas where the trade body is not able to influence directly. Despite asking for mandatory qualifications for advisers used, SHIP does not for example interfere in the setting of standards in advice, as these guidelines and documents such as the Factfind are the competence of the advisory community and the FSA.

The monitoring and enforcement of the Code is also not particularly robust. SHIP does not directly conduct checks on its members, but instead relies on its members conducting mystery shopping themselves. The annual signature of compliance to the Code required by SHIP from providers is supposed to confirm that members have their own robust processes in place and that they can check the independent financial advisers that are generating their business. The Code is not able to demand elaborate compliance requirements from its members (in part because such requirements affect the smaller members disproportionately more than the larger ones). SHIP is funded through annual subscription fees from its 22 members (of which 6 are on the management board). The application process for membership is based on a consensus of opinion, and there has been no member sanctioned by SHIP so far. Moral hazard may be hard to contain if members know that ejection from SHIP is unlikely. The high profile nature of any sanctions would constitute excessive reputational risk. Though a whistle blowing facility exists, there is no naming and shaming mechanism in place at present.

Self-regulation of the industry through the establishing and strengthening of SHIP is seen to be a useful addition to the market, even if the SHIP name, logo and what it signifies is not always as familiar with the average consumer, as it is within the industry. One criticism in the existence of a trade body setting standards, as SHIP does, is that the choice for a provider to opt out from membership of the trade body is far too easy for those firms that do not want to comply with restrictive rules affecting their business practice. Those firms who willingly adhere to SHIP guidelines, so to speak the ‘good guys’, are said to be very lax on exerting pressure on those firms who choose not to respect these rules necessary to design a safe product. It can be that a provider has a good reason not to join the club, and this does not mean that its products are automatically ‘unsafe’, but full membership would be the best way to ensure that the overall market is not negatively affected by the bad press that harmful products will generate. The role and work of SHIP will be referred to again in a later section on risk and benefits for the consumer.
g) Consumer protection legislation

(1) Advertising

The FSA sets out a general standard that communications by a financial firm, including advertisements and other financial promotions must conform to principles 6 and 7 of the FSA's Principles for Business, and as such must be "clear, fair and not misleading". This general standard is elaborated in MCOB 3 in the form of detailed rules on the conduct and content of written and non-written communications about qualifying credit (including lifetime mortgages) and home reversion plans, as well as the territorial scope of the FSA's rules.

In terms of territorial scope, the rules essentially apply to financial promotions that are communications to persons in the UK, approvals of financial promotions that are communications to persons in the UK, and the "communication or approval for communication of financial promotion that is an electronic commerce communication to a person in an EEA state other than in the UK" (MCOB 3.3.1(4)). Where a firm's communication is also within the scope of the Distance Marketing Directive as implemented in the firm's home state, the Directive's rules replace those of the FSA.

The rules on non-written (or "real time") communications prohibit unsolicited "cold calling" and require firms:

- to ensure that an individual who makes a financial promotion of qualifying credit on its behalf in the course of a personal visit, telephone conversation or other interactive dialogue:
  - does so in a way which is clear, fair and not misleading;
  - does not make any untrue claims;
  - makes clear the purpose of the financial promotion at the initial point of communication;
  - identifies himself and the firm which he represents.

Where the consumer had previously consented to the firm making contact for the purposes of financial promotion of qualifying credit (including lifetime mortgage) or home reversion plans but there was no prior agreement about time or method of communication, the firm must ensure that at the time of contacting the consumer, the individual acting on its behalf:

- Checks that the recipient wishes him to proceed;
- Terminates the communication if the recipient does not wish him to proceed (but the individual may ask for another appointment);

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41 See PRIN 7, available at http://fsahandbook.info/FSA/html/handbook/PRIN/2/1; MCOB 3.6.3 (lifetime mortgages and other forms of "qualifying credit"); MCOB 3.8A (home reversion plans).
42 See MCOB 3.3.5R: This exemption substitutes the Distance Marketing Directive's rules for the FSA rules on information about Name and contact point, required risk statements, transient advertising, multi-rate mortgages, fees for advice and arranging, and form and content of real time qualifying credit promotions.
43 See MCOB 3.7.3.
45 See Key Rules, p.8.
• Promptly recognises and respects the right of the recipient to end the communication at any time and refuse any request for another appointment;
• Gives any person with whom he arranges an appointment a contact point;
• Does not communicate with a person at an unsocial hour or call an unlisted telephone number, unless the person has previously agreed.\(^{46}\)

The rules on written (non real time) financial promotions require a firm before communicating or approving the promotion to:
• show it is clear, fair and not misleading;
• show it complies with the financial promotion rules; and
• have this checked by someone with appropriate expertise.\(^{47}\)

There are several provisions on the steps that firms should take to show that a non-real time communication is clear, fair and not misleading. Some of the most important steps include:

• Giving the same prominence to the possible disadvantages as to the benefits of any product feature that is described;
• Ensuring that any statement of fact, promise or prediction is clear, fair and not misleading and that any relevant assumptions are clearly and prominently disclosed;
• Verifying the facts on which any comparison or contrast is made, prominently disclosing relevant assumptions and presenting any such comparison or contrast in a fair and balanced manner that includes all factors which are relevant to the comparison or contrast;
• Locating required statements close to each other.\(^{48}\)

Firms are individually responsible for ensuring that the above standards are met, although a firm may be able to rely on another firm’s compliance checking of the communication if the relying firm:

- takes reasonable care to establish that another firm has already confirmed its compliance; and it communicates the financial promotion only to recipients of the type for whom it was intended at the time the other firm confirmed compliance; and it is aware [on reasonable grounds] that the financial promotion has not ceased to be clear, fair and not misleading since the time confirmation was given; and the other firm has not withdrawn the financial promotion.\(^{49}\)

These general standards of clarity, fairness and veracity are supplemented by detailed restrictions on and requirements for the contents of written (non real time) financial promotions of mortgages and home reversion plans. The Key Rules summarise the restrictions as follows\(^{50}\):

A written financial promotion of qualifying credit must not contain any of the following (or similar) expressions unless the relevant condition is met.

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\(^{46}\) See Key Rules p.8.
\(^{47}\) See Key Rules p.9.
\(^{48}\) See Key Rules p.10.
\(^{49}\) See Key Rules p.9.
\(^{50}\) See Key Rules p.10.
### Expression | Condition
---|---
Overdraft | The agreement enables the customer to overdraw on a current account.
Interest free 0% finance | The total amount payable by the customer does not exceed the cash price. OR In relation to a multi-rate mortgage, for a rate of charge of 0% provided that during the period in which the rate applies there is no interest charged and no increase in the amount of the mortgage loan.
Interest free option | No Deposit | No advance payments are required to be made on the loan.
Mortgage guaranteed Pre-cleared | The mortgage availability is not conditional on the customer’s credit status.
Gift Present | There are no conditions requiring the relevant money or items to be returned.

In addition, the FSA rules prescribe the use of particular terminology in written financial promotions. MCOB 3.6.9. states that:

*A non-real time financial promotion must:*

1. describe any early repayment charge as an 'early repayment charge' and not use any other expression to describe such charges;
2. describe any higher lending charge as a 'higher lending charge' and not use any other expression to describe such charges;
3. not contain the 'key facts' logo unless it is required by a rule; and
4. describe any lifetime mortgage as a 'lifetime mortgage' and not use any other expression to describe such a mortgage.

The most important required statements in a written financial promotion for qualifying credit (including a lifetime mortgage) or a home reversion plan include:

- Name and contact point of the firm
- Risks – a prominent statement of relevant risks.\(^5\)

The wording of the required risk statement for a lifetime mortgage is: "This is a lifetime mortgage. To understand..."

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\(^5\) The MCOB provides guidance on prominence in 3.6.14G, which states that: "(1) Prominence of relevant information can play a key role in ensuring that a communication is clear, fair and not misleading. ...The FSA will assess prominence in the context of the promotion as a whole. Use can be made of the positioning of text, background and text colour and type size to ensure that prescribed information meets the requirements of MCOB. The surrounding of required statements with other information should be avoided where this might detract from the prominence which it is obligatory to afford to the statements. (2) Firms may if they wish include a foreign language version of any required warning, in addition to the English language version required by these rules. If foreign language versions of warnings are included, firms are reminded of prominence requirements. Information should not be included which detracts from the required prominence of warning statements."
the features and risks, ask for a personalised illustration.” (MCOB 3.6.13) The required wording for a home reversion plan “must prominently state that [the promotion] relates to a home reversion plan and that the customer should ask for a personalised illustration to understand its features and risks” (MCOB 3.8A.3(2)(a)). If a lifetime mortgage were denominated in a currency other than sterling, the financial promotion would be required also to include prominently, as its final risk statement, the assertion that: “Changes in the exchange rate may increase the sterling equivalent of your debt.” (MCOB. 3.6.13(4) & 3.6.13(5)).

- APR – If a written financial promotion of qualifying credit contains price information for specific qualifying credit; or makes reference to availability of credit for customers who might otherwise consider their access restricted, it must state the APR using prescribed wording (“The overall cost for comparison is [X]% APR”) and in a form that is no less prominent than other price information in the promotion. The APR statement must be positioned, “after any other rate of charge, clearly distinguishing it but without putting any other information between the APR and any other rate of charge”. If the APR varies depending on the circumstances of the customer, the promotion must state that: “The actual rate available will depend upon your circumstances. Ask for a personalised illustration.”. Finally, the APR disclosed (or less) must apply to at least 66% of customers responding to the promotion and who enter into a relevant qualifying credit agreement, including a lifetime mortgage.

- Multi-rate mortgages: if the interest rate for the lifetime mortgage is envisaged to change during the life of any contract, the financial promotion “must contain a clear and no less prominent description of all of the rates of charge that will apply”. There are detailed rules about communicating the particular rate(s) applicable to the contract and about communicating the changeable nature of the rate: MCOB 3.6.26.

- Fees: Any advice or arranging fees that a firm expects to derive out of business arising from the financial promotion are to be “prominently indicated” (MCOB 3.6.27).

The MCOB rules also regulate contrasts and feature comparisons in financial promotions as an aspect of the “clear, fair and not misleading standard”. The core elements of these rules require contrasts and feature comparisons to:

- Compare credit meeting the same needs or purpose;
- Objectively compare the representative features, which may include price;
- In any comparison referring to a special offer, indicate in a clear and unequivocal way: its start date (if it has not yet begun); and its end date or (if appropriate) that it is subject to the qualifying credit’s availability.

In addition to the particular FSA rules and any applicable EC directives, financial promotions for mortgages and home finance products, including equity release products may be subject to other regulatory schemes including codes published by the Advertising Standards Authority, the Independent Television Commission and the Radio Authority. (MCOB 3.5.3G).

52 See Key Rules, p.12. MCOB 3.6.18. For detailed rules on the calculation of APR in mortgage contracts and financial promotions for mortgages, see: MCOB 10.

53 See Key Rules p.13, MCOB 3.6.3(2). This MCOB provision also includes detailed rules about using the trademarks, and other identifying information of other firms.
(2) Involving stakeholders in the decision-making process

To avoid any nasty surprises and unnecessary family conflict, it is seen as better practice to include the inheritors into the advice procedure. In the UK, firms advise customers to discuss an equity release transaction with family members\(^54\) but there is no legal requirement to inform or include anyone other than the firm’s customer(s). See Ombudsman News Issue 72 Sept/Oct2008 for several case studies drawn from complaint files about conflicts that arise when family members and legatees are unaware of the equity release transaction\(^55\).

(3) Advice and Information provision

Detailed prescriptive rules about the form, content and timing of information disclosure prior to conclusion of a financial services contract have been a central element of the FSA’s regulatory technique. These rules essentially require brokers and providers of housing finance products on first contact with a customer to provide in standardised information about the firm and the financial service (Initial Disclosure Document) and then to provide detailed, personalised product and price information (the Key Facts Illustration) before the customer submits an application and at the time of the offer. The rules require those who advise or arrange equity release transactions to "take reasonable steps" to ensure the suitability of any equity release product that is recommended and the rules spell out what is meant by this suitability standard.

For a variety of reasons, including the complexity of the detailed rules and costs of maintaining its rulebook, the FSA has sought to shift away from detailed prescriptive rules and to rely more heavily on 'high-level' principles as its preferred regulatory technique in situations where it has a choice, (e.g. in those situations where there are no binding EC Directive provisions). The eleven ‘high-level’ principles are set out in the FSA’s Principles for Business Handbook\(^56\).

In recent years, the FSA has invested heavily in its ‘Treating Customers Fairly’ initiative, a supervision / educational project for financial firms, the goal of which is that firms take responsibility for translating the general norms of the Principles for Business into concrete operational policies and practices that produce fair outcomes in consumer financial markets. Principles 6 (Customers' Interests) and 7 (Communications with Clients) are most relevant to the FSA's expectations in relation to pre-contractual disclosure and Principle 9 to the FSA's advising standards\(^57\). Principle 6 reads: "A firm must pay due regard to the interests of its customers and treat them fairly;" Principle 7 states that "A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading;" and Principle 9 provides that: "A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment."

Despite the FSA’s expressed preference for regulation by way of high-level principles, it has continued to maintain detailed rules, which we summarise here, on information disclosure and advising practices.\(^58\) The rules envisage three distinct stages of disclosure

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\(^{54}\) Based on interviews with the Association of British Insurers during a visit in September 2008.


\(^{56}\) See http://fsahandbook.info/FSA/html/handbook/PRIN.


\(^{58}\) One of the difficulties with these rules is that in some instances the FSA has drafted a specific rule for equity release transactions, in other instances it relies on a rule that applies to all mortgage and home finance transactions, and in some cases the source is a hybrid between the rule that is generally applicable to home finance and that which is specific to equity release. We have endeavoured to provide accurate source information, as of the time of writing.
before the contract is made: on first contact; pre-application; and at the time of the offer and they regulate these communications through very detailed provisions about the form and content of the documents that firms may and must supply.

(A) First contact: initial disclosure document

The first important document is the Initial Disclosure Document which describes the nature and scope of the services that the firm provides. While the equity release advising and selling standard is MCOB 8, this standard incorporates the disclosure rules from MCOB 4, which apply to all regulated mortgage transactions.

The rules about initial disclosure in relation to equity release provide that:

Any firm (seller, broker or other intermediary) that anticipates providing "personalised information or advice" on an equity release product must "on first making contact with" a consumer: establish whether the transaction will entail the provision of advice or information; establish how much the consumer will pay or the basis on which the firm is paid; and provide the customer with an initial disclosure document (IDD) or combined initial disclosure document. Initial disclosure documentation, which must be provided in writing or another durable medium and reissued when relevant information changes, gives information about the firm and its FSA regulated status, the nature of the service offered by the firm and the scope of any advice it provides.

MCOB 4.4.2 clarifies that for transactions involving more than one firm, such as an intermediary and a lender, the IDD should be provided by the firm that first makes contact with the consumer, normally the intermediary. Any other firm involved in the transaction "should take reasonable steps to establish that the customer has been provided with an initial disclosure document as required by MCOB 4.4.1".

The Template for the initial disclosure document pertaining to an equity release transaction can be found in MCOB 8 Annex 1. Additional sample IDD and CDD templates and advice for equity release brokers are also available.

MCOB 4.3 regulates the information that all mortgage intermediary firms must provide about the scope of their services. Intermediaries are to indicate in the IDD whether any advice or recommendations are based on products selected from either the whole market for an equity release product; or a limited number of home finance providers; or a single provider only.

Intermediary firms that purport to offer a service based on the entire market must consider a 'sufficiently large' number of products that are generally available based on criteria that reflect adequate current knowledge of that market: MCOB 4.3.5 and 4.3.6.

An intermediary firm that holds itself out as independent must: provide its services "wholly or predominantly based on the whole market" in equity release; and "enable the customer to pay a fee for the provision of that service". MCOB 4.3.7.

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60 A Combined Initial Disclosure Document (CIDD) is intended for situations where the firm is likely to provide services that "relate to a combination of different types of home finance transaction, or will relate to home finance transactions and one or more of non-investment insurance contracts or packaged products". Note that firms must not use a Combined IDD in relation to a transaction that combines a non-equity release mortgage with an equity release transaction, MCOB 4.4.1(4).
61 See MCOB 4.4.1(1).
Where a firm's first contact with a customer is by telephone, then unless the customer has already received an IDD, the firm that makes contact by phone must at the start of the telephone call tell the customer:

(a) the name of the firm and (if the call is initiated by or on behalf of the firm) the commercial purpose of the call;

(b) the scope of the service provided by the firm (within the meaning of MCOB 4.3.1 R);

(c) if the scope of the service is based on [a limited number of providers] that the customer can request a copy of the list of mortgage lenders whose regulated mortgage contracts it offers and confirmation of whether the firm provides services in relation to all of the regulated mortgage contracts generally available from each mortgage lender;

(d) whether or not the firm will provide the customer with advice on those regulated mortgage contracts within its scope; and

(e) that the information given under (a) to (d) will be confirmed in writing.

After the nature and scope of the service has been described in the prescribed form of the IDD, the next important set of disclosure requirements concern the equity release product. MCOB 9 sets out detailed product disclosure rules for equity release transactions at four stages: pre-application; offer; the start of the contract; and after sale. These rules draw on the product disclosure rules for other home finance transactions in MCOB 5, 6, and 7 but are specifically adapted where necessary to the characteristics of the equity release transaction.

Although MCOB 9, (and also 5, 6, and 7) consists of highly detailed rules about the form, content, accuracy and timing of disclosure the provisions are characterised as simply 'amplify[ing]' the Treating Customers Fairly Principles for Business (Principles 6 & 7).

The general purposes of the pre-contract disclosure rules are to ensure that at each stage of the home finance transaction the customer receives information that describes the features and the price of the financial product in a standardised form and does not receive extraneous or superfluous information that might distract, confuse or mislead. The overall effect of the disclosure rules is that the FSA has created a set of personalised standard form documents, with tightly regulated form and content, for pre-contractual communications, offers, variations, and annual statements.

(B) Pre-application disclosure requirements: Detailed rules

According to the FSA, the purpose of pre-application disclosure requirements for home finance transactions is to "ensure that, before a customer submits an application for a particular home finance transaction, he is supplied with information that makes clear: (a) (in relation to a regulated mortgage contract) its features, any linked deposits, any linked borrowing and any tied products; and (b) the price that the customer will be required to pay under that home finance transaction, to enable the customer to assess whether it is affordable to him."

The disclosure rules also are intended to ensure that information "is disclosed in a consistent way to facilitate comparison between products of different providers." A useful summary of the main rules of this standard as well as the other rules pertaining to

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64 See MCOB 4.4.7.
66 See MCOB 5.2.1, 6.2.1, 7.2.1, 9.2.1 and quoted above at the beginning of section 5(g)(3) (on p.21).
67 See MCOB 5.2.1(2).
68 See MCOB 5.2.1(3).
equity release intermediaries is available in the Key Rules for Mortgage and Home Reversion Brokers Handbook pp.26-34\(^{69}\) (hereafter ‘Key Rules’).

The pre-application disclosure rules require a consumer to be provided with specific information in the form of a Keyfacts Illustration (KFI) before submitting an application for an equity release (or other home finance) transaction and prohibit the entering into of such a transaction unless the consumer has submitted an application. The rules restrict the provision of information that is not in the prescribed form of the KFI and prohibit the provision of supplementary information that "significantly duplicates information in the KFI." Specifically, a firm cannot provide written or printed information except in the form of a KFI and where information is initially supplied on a computer screen or orally the firm must "provide the means for the customer to obtain a KFI as soon as practicable, through a delivery channel acceptable to the customer." (Key Rules p.26). It can be seen that the purpose of these rules is that the consumer should receive information only in the standardised form prescribed by the FSA, a format that purports to facilitate comparison and to reduce confusion.

Rules on the form and content of the pre-application KFI for equity release transactions are set out in MCOB 9.4, a 54 page document\(^{70}\). KFI templates, which provide the KFI’s table of contents, prescribed text and prescribed section headings and subheadings, are available for lifetime mortgages\(^{71}\) and home reversion plans\(^{72}\). Some parts of the illustration must be personalised to the consumer’s particular circumstances. The minimum content of such personalised disclosure is specified in MCOB 9.4.6, and elaborated in MCOB 9.4.5-9.4.16.

MCOB 9.4.6, the minimum personalised content provision, requires the KFI to reflect the following:

- the specific equity release transaction in which the customer is interested;
- the amount of the loan or equity, required by the customer, or for drawdown mortgages and instalment reversion plans, the amount the customer wishes to draw down or to receive on a monthly (or such frequency that amounts are available) basis. Where the amount the customer can draw down is variable, the firm must agree with the customer an expected amount to be drawn down per year\(^{73}\);
- the price or value of the property on which the equity release amount is based (estimated where necessary);
- such information relating to the customer, or the property, or both as is necessary to determine that the customer would qualify for the equity release transaction in question; and
- the term of the instalment reversion plan or, in the case of a lifetime mortgage and an open-ended instalment reversion plan, the estimated term.

The KFI presents in a prescribed format, which includes specific titles and section headings, the above personalised ‘required content’ alongside the following standardised provisions:

A) An explanation of the nature and purpose of the document, a reference to the FSA’s independent watchdog function and its information booklet titled

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\(^{71}\) See http://www.fsa.gov.uk/pubs/other/mcob_forms/mcob9_annex1.pdf.

\(^{72}\) See http://www.fsa.gov.uk/pubs/other/mcob_forms/mcob9_annex2R.pdf.

\(^{73}\) See MCOB 9.4.13 R.
“Raising money from your home”, and the expectation that customers should receive a similar document for each home equity product that interests them.74

B) A statement about whether the firm is recommending a particular product after having assessed the consumer’s needs (an advised sale), or instead providing particularised information about a specific product based on the consumer’s “answers to some questions”, so that the consumer “can make your own choice or find out about other ways in which you may be able to release equity from your home.”75

C) Explanation of the general nature of the particular form of equity release referenced in the KFI (lifetime mortgage or home reversion plan) and of how the product works, using content provided by the FSA.76

D) Summary of the information that the consumer gave the firm and that formed the basis for personalisation of the KFI.77 At the end of this section the KFI must warn the consumer that: “changes to any of the information obtained from the customer, and where appropriate to the valuation of the property, could alter the details elsewhere in the illustration” and “encourage the customer to ask for a revised illustration in this event.”78

E) Description of the particular product that is the subject of the KFI by reference to identity of the mortgage lender or plan provider and a description of the specific product. For lifetime mortgages this section must include also: the interest rate type and rate79; an estimated term of years with prescribed warning text to the effect that the term is not fixed and could run beyond the years estimated; a description of any tied products; a statement of any restrictions on the product; and where applicable (i.e., where the consumer has an adverse credit history) the statement that: “The terms of this lifetime mortgage reflect past or present financial difficulties”. The rules specify detailed requirements for presenting information about the type and rate of interest and provides sample text to describe ‘drawdown’, ‘interest-only’ and ‘roll-up of interest’ mortgages.80 The term for a lifetime mortgage or an open-ended reversion is to be estimated by reference to specified mortality tables published by the Institute of Actuaries and the Faculty of Actuaries81

F) Description of the ‘benefits’ of the product in prescribed form.82

G) Indication of the specific risks of the product under the heading: “Risks - important things you must consider”.83 For a lifetime mortgage the detailed rules in MCOB 9.4.33-9.4.35 specify that the KFI must provide:

74 See MCOB 9.4.18, KFI template section 1 headed “About this information”.
75 See MCOB 9.4.19, KFI template section 2, headed “Which service are we providing you with”.
76 See MCOB 9.4.20, KFI template section 3, headed “What is a lifetime mortgage?” or “What is a Home Reversion Plan”).
77 See MCOB 9.4.21, KFI template section 4.
78 See MCOB 9.4.22, KFI template section 4, headed “What you have told us”.
79 See MCOB 9.4.24(4).
80 See KFI template section 5; the rules for lifetime mortgage KFIs are in MCOB 9.4.24 - 9.4.30 and equivalent rules for home reversion plans are MCOB 9.4.139R – MCOB 9.4.141G.
81 See MCOB 9.4.10.
82 See KFI template section 6, MCOB 9.4.31R-9.4.32G & 9.4.142R-9.4.144G.
83 See KFI template section 7, MCOB 9.4.33-9.4.35 lifetime mortgages and 9.4.145-9.4.147 for home reversion plans.
“(1) a brief statement of the specific circumstances in which the mortgage lender is able to repossess the property;

(2) a statement of how the mortgage lender will treat any negative equity arising during the life of the lifetime mortgage and at the time the amount borrowed under the lifetime mortgage is due to be repaid in full;

(3) a statement of the effect of the customer wanting or needing to move home (either into another property or into sheltered accommodation or long term care or residential care), covering the circumstances in which the lifetime mortgage is portable, and whether early repayment charges are payable (the illustration is not required to include under this heading the exact amount of any early repayment charges);

(4) a statement of the effect on the lifetime mortgage of another party moving into the property (for example on marriage or the formation of a civil partnership or where a family member acts as a carer);

(5) a brief statement of the mortgage lender’s requirements for repair and maintenance of the property, including the mortgage lender’s right (if any) to enter the property to effect essential repairs, and the circumstances in which this may occur;

(6) a warning that taking out this lifetime mortgage may affect the customer’s tax and welfare benefits position, that tax and welfare benefits can change and that the customer should consider seeking further information from HM Revenue and Customs, Benefits Agency or another source of advice such as a Citizens’ Advice Bureau;

(7) a brief statement as to whether the customer can secure borrowing from any other source on the property in the future (and if applicable a warning that an increasing debt may mean that it may not be possible to borrow more in the future); and

(8) a statement included prominently at the end of Section 7: “Risks - important things you must consider” using the following specified text: "Check that this mortgage will meet your needs if you want your family or others to inherit your home. If you are in doubt, seek independent legal and financial advice."  

"Under the heading "Risks - important things you must consider" the illustration must also include the following if they apply:

(1) for drawdown mortgages where there is a monthly (or such other frequency as may apply) cash sum payable, a statement that inflation can erode the value of the cash sum over time;

(2) where:

(a) the lifetime mortgage is linked to an investment; and

(b) the payments required on the lifetime mortgage will be deducted from the income from the investment; and

(c) the customer will receive a fixed net income;

See MCOB 9.4.33.
(d) a statement that inflation can erode the value of the cash sum over time;

(3) for drawdown mortgages, details of any circumstances where the mortgage lender may alter or discontinue payments to the customer without their prior consent; and

(4) for all lifetime mortgage, a statement or warning with regard to any material issue not covered elsewhere in MCOB 9.4.33 R and MCOB 9.4.35 R."

H) Section 8 of the pre-application KFI is headed “What you will owe and when” in the lifetime mortgage KFI templates and “What you will have to pay and when” in Home reversion plan KFI template. With regard to lifetime mortgages, the prescribed text and elements vary depending on the whether the consumer is to make payments during the mortgage86, whether the mortgage is multi-part (9.4.47-9.4.48), and whether the interest is rolled-up.87 For mortgages where the interest is ‘rolled-up’, the KFI must include prescribed explanatory text and a projection of the interest payable, presented in the form of a table, based on the estimated term given in Template Section 5.88 Equivalent rules for home reversion plans are in (9.4.148R – MCOB 9.4.151R).

I) Section 9 of the lifetime mortgage KFI is headed “Will the interest rate change?” and the prescribed content, which includes prominent risk warnings of the potential for significant increases in payment or debt as appropriate, is described in MCOB 9.4.53-9.4.61. There is no such heading in the template for the home reversion plan KFI.89

J) Section 10 of the lifetime mortgage KFI is headed “How the value of your home could change” and the rules governing the content of this section are.90

K) Section 11 of the lifetime mortgage KFI (and section 9 of the home reversion plan KFI) is headed “What fees must you pay?” This section provides for detailed itemisation of all fees included in the APR calculation, under specified headings.91

L) Section 12 of the lifetime mortgage KFI (and section 10 of the home reversion plan KFI), headed “insurance”, specify the information that firms must provide about any tied insurance products and about contractual requirements for the consumer to maintain insurance on the property that is subject to the mortgage or the reversion plan.92

85 See MCOB 9.4.35.
86 See MCOB 9.4.36-9.4.46.
87 See MCOB 9.4.49-9.4.52.
88 See MCOB 9.4.50-9.4.51.
89 If the KFI is produced in relation to “further advances”, then Section 9 deals with “total borrowing”; Interest rate changes become the subject of Section 10 and subsequent sections are correspondingly renumbered.
90 See MCOB 9.4.62 - MCOB 9.4.64. There is no such heading in the template for the home reversion plan KFI.
91 See MCOB 9.4.65R to MCOB 9.6.71R (lifetime mortgage) and MCOB 9.4.152R – MCOB 9.4.158R (home reversion plan).
92 See MCOB 9.4.72R to MCOB 9.4.75R and MCOB 9.4.81R (lifetime mortgage) and MCOB 9.4.159R– MCOB 9.4.166G (home reversion plan).
M) Section 13 of the Lifetime mortgage KFI is headed “What happens if you do not want this mortgage any more?” These rules concern the form and content of information about early repayment charges. The equivalent section of the home reversion plan KFI template is headed “What happens if you do not want this home reversion plan any more”.

N) “Additional features”. This section of the KFI “must include, where relevant, details of how the mortgage lender would treat any payments by the customer in excess of those required, and details of any additional features or facilities under specified sub-headings”. Again, the requirement is to provide detailed information about the circumstances and conditions under which particular facilities arise (such as payment holidays for lifetime mortgages that include interest payments). The specified conditions, facilities and features that must be addressed where relevant are (1) “Overpayments”; (2) “Underpayments”; (3) “Payment holidays”; (4) “Borrow back”; (5) “Additional borrowing available without further approval”; (6) “Additional secured borrowing”; (7) “Credit card”; (8) “Unsecured borrowing”; (9) “Linked current account”; and (10) “Linked savings account”.

O) Section 15 of the lifetime mortgage KFI is headed “Overall cost of this mortgage”. This section of the KFI includes prescribed text explaining the elements of the overall cost and reminding the consumer that one of the purposes of the KFI is to facilitate comparison of different lifetime mortgages by standardising important information including the presentation of cost information in the form of an APR. After the required explanatory text this section must state in the form and layout prescribed:

(1) "The total amount you would pay back over the example term of [insert number of years in accordance with MCOB 9.4.10 R or MCOB 9.4.12 R] including the amount borrowed is £ [insert total amount payable]", and

(2) "The overall cost for comparison is [insert the APR]% APR."

P) Section 16 of the lifetime mortgage KFI, headed “Using a mortgage intermediary”, provides for disclosure of all amounts payable by the mortgage lender to the intermediary “directly or indirectly”. Rules governing the equivalent section in the home reversion plan KFI (numbered 12 on that template) are in MCOB 9.4.168R – MCOB 9.4.174G.

(C) Pre-Contractual Disclosure: Offer Illustration

An “updated and suitably adapted illustration” must be provided as part of the offer documentation for the equity release contract. The purpose of this illustration is to enable the consumer “to check the features and price” before entering into the contract and to enable the consumer to compare the offer with the information received before making the application. The basic structure and format of the offer illustration is the same as the pre-application KFI with appropriate modifications. The required modifications are specified in MCOB 9.5.4:

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93 See MCOB 9.4.38R to MCOB 9.4.90R (lifetime mortgages).
94 See MCOB 9.4.167R.
95 See MCOB 9.4.91R to MCOB 9.4.110R (No equivalent section for home reversion plan).
96 See MCOB 9.4.111R to MCOB 9.4.112G (No equivalent section in the home reversion plan KFI).
97 See MCOB 9.4.119R to MCOB 9.4.125G.
98 See MCOB 6.2.1G.
"(1) the illustration must be suitably adapted and revised to reflect the fact that the firm is making an offer to a customer and updated to reflect changes to, for example, for a lifetime mortgage the interest rate, charges, the exchange rate or the APR required by MCOB 10 (Annual Percentage Rate) at the date the illustration is issued;

(2) the illustration must be based on the example term estimated in accordance with [the mortality tables specified in] MCOB 9.4.10 R;

(3) MCOB 9.4.2 R(2)(a) [requiring the use of the “KeyFacts” logo] does not apply;

(4) MCOB 9.4.17 R (Information to be included at the head of the illustration) does not apply — this information relates to pre-application disclosures only;

(5) Section 1: ‘About this information’ is replaced by the following: “Section 1: ‘About this offer document’. Under the section heading ‘About this offer document’, the following text must be included:

(a) "You are not bound by the terms of this offer document until [insert relevant circumstances, including the names of any documents that must be signed. For example "you have signed the legal charge and the funds are released for your lifetime mortgage"] or "you have signed the agreement to sell your property to the reversion provider"]. We are required by the Financial Services Authority (FSA) - the independent watchdog that regulates financial services - to provide you with this offer document."

(b) (unless the offer document is being provided in place of an illustration )"You should compare this offer document with the key facts illustration given to you before you applied for this [lifetime mortgage] [home reversion plan], to see how the details may have changed."

(6) either:

(a) The heading for Section 2 is replaced with ‘Which service did we provide you with?’ and the following text should be presented as two options each with a ‘check box’, one of which must be marked prominently to indicate the level of service provided to the customer: "We have recommended, having assessed your needs, that you take out this [lifetime mortgage] [home reversion plan]." "We have not recommended a particular [lifetime mortgage] [home reversion plan] for you. You must make your own choice whether to accept this [lifetime mortgage] [home reversion] offer.";

(b)if the service described in Section 2 of the earlier illustration was provided by another firm, the heading for Section 2 is replaced by ‘Which service were you provided with?’ and the following text should be presented as two options each with a ‘check box’ one of which must be marked prominently to indicate the level of service provided to the customer: "[name of firm] recommended that you take out this [lifetime mortgage] [home reversion plan]." "[name of firm] did not recommend a particular [lifetime mortgage] [home reversion plan] for you. You must make your own choice whether to accept this [mortgage] [home reversion] offer.";

(7) the fees recorded in the illustration that is part of the offer document must include any fees paid or payable by the customer;

(8) any requirements to disclose whether a fee is refundable must be read as including fees that have already been paid;

(10) for a lifetime mortgage:

(a) where additional features are included in accordance with MCOB 9.4.91 R and these are credit facilities regulated by the Consumer Credit Act 1974, the relevant parts of Section 14 of the illustration that is part of the offer document must include the following text: "This credit facility is regulated under the
Consumer Credit Act 1974. Please refer to the separate credit agreement which describes the facility and the terms on which the credit is available.;

(b) The text required by MCOB 9.4.102 R (2)(a) or MCOB 9.4.102 R (2)(b) should be adapted to include, or tell the customer where they can find, the information required by MCOB 6.5.4 R; and

(c) MCOB 9.4.119 R and MCOB 9.4.120 R apply to the illustration that is part of the offer document if the illustration given out in accordance with MCOB 9 was issued by, or on behalf of, a mortgage intermediary.

Because the sale form of equity release, the home reversion plan, entails an outright transfer of a share of the property, the regulation also requires the firm to provide a consumer with "copies of the valuation report for the property and the terms of the home reversion plan including the terms on which he will occupy the property, together with the offer document” (MCOB 9.5.5.).

(D) ADVISING STANDARDS (MCOB 8.5 and MCOB 8.6)

The FSA rules cover both advised and non-advised sales of equity release products.

NON-ADVISED SALES (MCOB 8.6): are to be conducted on the basis of scripted questions that together with the disclosure documents are intended to help a consumer to choose an appropriate product. These questions must cover:

MCOB 8.6.1:

(1) the matters regarding eligibility criteria, customer’s preferences for his estate, customer’s health and life expectancy, customer’s future plans and needs, customer’s preference or need for stability in the amount of payments, and whether the customer has a preference or need for any other features, set out in MCOB 8.5.8 R (NB. MCOB 8.5.8R basically references the same matters more fully, see below under advised sales);

(2) whether the customer has considered alternative methods of raising the required funds, and in particular;

(a) an equity release transaction from the other market sector; and

(b) where relevant, grant assistance from his local authority (or other provider); and

(3) whether the customer has established whether either his entitlement to means-tested benefits or his tax position or both will be adversely affected.

MCOB 8.6.2G instructs firms conducting non-advised sales to:

"encourage a customer to seek advice on an equity release transaction if the customer is unsure about making their own choice. In relation to grant assistance, means-tested benefits and the customer’s tax position, a firm should, where relevant, encourage the customer to seek further information from an appropriate source such as their local authority or Citizens Advice Bureau (or other similar agency).”

Firms must train staff to use the script. They also must train staff “to understand what constitutes a personal recommendation and instruct staff not to give such a recommendation unless the staff member has been assessed as competent to do so”.

ADvised Sales (PRINCIPLE 9 AND MCOB 8.5): A useful summary of the MCOB 8.5 rules on advised sales, which are an elaboration of high-level principle 9 is found in the

See Key Rules for Mortgage and home reversion Brokers p.22.
key rules for mortgage and home reversion brokers at pp. 18-22. This summary states (sources inserted):

“A firm must take reasonable steps to ensure that any personal recommendation to a customer to enter into (or vary) a mortgage or equity release transaction is suitable for that customer. A firm should recommend, out of all the appropriate mortgages or equity release transactions, the transaction that is the least expensive for the customer, taking into account those pricing elements identified by that customer as most important. Firms may, however, make recommendations that take account of other grounds such as speed or quality of service of the product provider.

A firm must not make a recommendation if there is no appropriate product within the scope of service provided.

A product (or variation of it) will be suitable if the firm has reasonable grounds to conclude that:

• Where relevant, the customer can afford to enter into (or vary) it. See PRIN 9 & MCOB 8.5.1-8.5.2.
• It is appropriate to the customer’s needs and circumstances. See MCOB 8.5.10 to 8.5.15.
• It is the most suitable of those the firm has available to it within the scope of service provided to the customer. See MCOB 8.5.16.
• the customer benefits outweigh any adverse effect on any customer entitlement to means-tested benefits and the customer’s tax position (e.g. loss of an age allowance); and alternative fundraising methods are less suitable, such as, in particular, a home reversion plan (where a lifetime mortgage is recommended), a lifetime mortgage (where a home reversion plan is recommended) and, where relevant, a local authority or other grant. See MCOB 8.5.4.

This conclusion [about suitability] must be reached having regard to the facts disclosed by the customer and other relevant facts about the customer of which the firm is or should reasonably be aware.”

In determining whether the benefits of an equity release transaction outweigh any adverse effects on entitlement to means-tested benefits and on the consumer’s tax position, a firm that “has insufficient knowledge of means-tested benefits and tax allowances to reach a conclusion must refer a customer to an appropriate source or sources such as the Pension Service, HM Revenue and Customs or Citizens Advice Bureau (or other similar agency) to establish the required information.”

In determining whether a local authority (or other) may be available for housing repairs a firm should:

(a) establish, on the basis of information given by the customer about his needs and objectives, whether these appear to be within the general scope of a local authority (or other) grant (for example where the customer requires funds for essential repairs to his property); and

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100 See PRIN 9 & MCOB 8.5.1-8.5.2.
101 See MCOB 8.5.10 to 8.5.15.
102 See MCOB 8.5.16.
103 See MCOB 8.5.17 to 8.5.19.
104 See MCOB 8.5.4.
105 See MCOB 8.5.5.
106 See MCOB 8.5.6(1).
(b) refer a customer to an appropriate source such as his local authority or Citizens Advice Bureau (or other similar agency) to identify whether such a grant is available to him.

The MCOB 8.5 rules make provision also for ‘failed’ advice, that is situations where the customer does not follow the firm’s advice to seek further information, e.g., about the implications for taxes or benefits; or rejects the product that the firm has recommended as the most suitable. Essentially, a firm in this situation may recommend an equity release product that is ‘appropriate’ to the customer’s needs, objectives and circumstances if such an appropriate product is available. If an appropriate product is not available or is rejected by the customer then the firm should treat the situation as a non-advised sale issue a new IDD setting out the altered scope of the service and provide information based on its scripted questions. Obviously, the basis of the information or modified recommendation should be recorded.

(4) Complaint board

A complaint procedure does exist for consumers of ERS in the UK and is administered by the Financial Ombudsman Service (FOS). A recent FOS bulletin reports on ERS and notes that: "constitute a small but significant number of cases" before the FOS and provides several case studies drawn from completed files.107

6. Reasons for slower than expected development of the markets

a) Legal barriers

The following two legal impediments to a stronger development of the UK market for ERS have been identified on the basis of questionnaire responses, interviews, articles and research reports published on the subject.

(1) Entitlement to state benefits:

The Social Security (Housing Benefit, Council Tax Benefit, State Pension Credit and Miscellaneous Amendments) Regulations 2004, No. 2327, Regulation 7 para 2 amends the State Pension Credit Regulations 2002 regulation 1(2) in two ways.

First, under paragraph 2, it defines an ‘equity release scheme’ as "a loan - (a) made between a person ("the lender") and the claimant; (b) by means of which a sum of money is advanced by the lender to the claimant by way of payments at regular intervals; and (c) which is secured on a dwelling in which the claimant owns an estate or interest and which he occupies as his home." [this definition is that same as that indicated above for housing law].

Second, Paragraph (3) of Regulation 7 adds payments made at regular intervals under an ERS to the descriptions of income which are prescribed for the purposes of section 15(1)(j) of the State Pension Credit Act 2002 (c. 16). Paragraph (4) adds payments made at regular intervals under an ERS to the descriptions of income listed as retirement pension income in section 16(1) of the State Pension Credit Act 2002.

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(2) Uneven regulation

With regards to whether a different level of regulation has hindered certain forms of ERS compared to others (i.e. have home reversions in the UK suffered from a later regulation of their activities as compared to lifetime mortgages?), there is no reliable empirical data on this issue. Some providers believe that reputational legacy of equity release mis-selling scandals in the late 1980s and early 1990s have had a long-term dampening effect on the equity release market, causing consumer groups to regard equity release products with suspicion and slowing rates of consumer take-up. Providers therefore supported the inclusion of 'lifetime mortgages' when the FSA's jurisdiction was extended to home finance transactions in October 2004. It was thought that integration of the lifetime mortgages into the regulatory regime for all mortgages would reassure consumers about the safety and legitimacy of these products. The industry continued to believe that the absence of regulation hampered the development of the home reversion form of equity release and thus lobbied for the extension of the regulatory regime to this type of transaction. This extension occurred in April 2007.

According to a study conducted in Malta in 2005,108 “the experience of the UK market shows that there may be scope for regulating Equity Release Plans. In fact, the UK is moving towards regulating this market namely due to three common factors:

- the relative complexity of the products per se;
- the relatively aggressive sales of these products; and
- the consumers who purchase these products are largely unable to understand the details or risks involved.

So far in the UK, only the sale of first charge Lifetime Mortgages is regulated by the Financial Services Authority (“FSA”), while the UK Government has completed a consultation exercise with stakeholders regarding the regulation of Home Reversion Plans.” This quote dates from 2005, since then, home reversion plans fell under regulation in April 2007, which is generally seen as a good thing even though there has been no significant resulting increase in the growth of these Sale-Model ERS transactions since that date.

b) Economic barriers

One economic barrier that has emerged as a result of the strong competitive pressures that has driven product innovation through flexibility and greater levels of guarantees etc. is that providers product margins have fallen. This is making it increasingly difficult for providers to reach target returns on capital which could in turn be deterring some prospective new entrants109. A further negative consequence of this economic constraint could be heightened consumer risk in terms of pressure to reduce expensive selling time or improve low conversion ratios via shortcuts in the advice process or pressure on sales teams to sell business where it is not needed110.

The relative mobility of the UK population (though perhaps this is less at old age) and relative ease and low cost associated with housing transactions compared to elsewhere in the EU, means that selling the house is always a viable option offering an alternative to homeowners.

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108 See Section containing country report for Malta below (on p.128).
110 See (fn 109).
Other economic barriers are linked to development in the risk assumptions which providers are making. Alongside factors such as base mortality and mortality improvements over time, projections for long-term care and forecasts for early redemptions will also be important. Any false assumption by a provider may affect them differently depending on their circumstances. For example, it is generally acknowledged that if the product is sold through a broker based sales channel, there is likely to be more risk of early repayment as intermediaries are generally more proactive in stimulating re-mortgaging than direct or controlled distribution channels\(^{111}\). Almost all providers in the UK calculate early repayment charges (also referred to as early redemption fees or prepayment penalties) for early termination of the contract based on a backward sliding scale where the percentage of the product value decreases over time, one major provider has in fact suggested a different method based on the market interest rate prevalent at the time. This last method is said to be fairer (more closely reflecting the actual true cost of adjustment) but often perceived by consumers as more complicated to understand. Although one method penalises everybody, it is transparent\(^{112}\).

c) Cultural barriers

The typical cultural barriers that apply for other EU countries do not for the UK. Attitudes to indebtedness and the familiarity with the idea of extracting money from the value of your home are favourable to ERS and it is thus no surprise that the UK is by far the most developed market in the EU.

There is conflicting information on consumer awareness of SHIP. Some consumers say they look out for SHIP and the logo, others do not recognise it. The Logo is supposed to serve as a seal of quality and is currently being rebranded\(^{113}\). The media portrayal of ERS as expensive and inflexible is judged by providers in the UK as unfair. Interest rate differentials with other credit products are around 1% only and the recent innovation in flexibility of product features is not being recognised by the press\(^{114}\).

The extent to which ERS can be the preferred solution to a consumer wanting to extract cash from the value of his home is an issue which has been quite confrontational in the UK. This is mainly because the main consumer organisation in the UK, Which?, has been rather clear with its opinion that ERS (irrespective of whether they are a Loan or Sale Model ERS) generally belong as the option of last resort\(^{115}\). Critics of this view often deride this ‘Nanny State’ approach, while many will just want to see the product sold fairly, uninterested in whether the funds released are used to pay for fundamentals or necessities as opposed to enabling an improved lifestyle.

Although home reversions represent a much smaller share of ERS in the UK, the prospects for further distribution of these Sale Model ERS remain fairly strong. Consumer mentalities and familiarity with the concepts, will lead to preferences for one type over another.

\(^{111}\) See (fn 109).

\(^{112}\) Opinions of consumer associations on the issue of early repayment fees is also mentioned in Section 2 a) above (on p.12).

\(^{113}\) Based on interviews with SHIP during a visit in September 2008.

\(^{114}\) SHIP the trade association has had to work at correcting information that has often been based on old biased views. However, recent media views are showing that this is changing over the last year. SHIP is active in promoting the use of ERS as a logical decumulation of wealth against the opinion that it is a last resort option for people.

\(^{115}\) The tension stems primarily from several articles by Which? that either suggested ERS should be an option of last resort (e.g. in January 2006 http://www.money-advice.net/media.php?id=3162) or stressed that alternatives to ERS such as downsizing are superior (e.g. in September 2007 http://www.money-advice.net/media.php?id=3161). Furthermore, in September 2008, SHIP issued an open criticism following the use of the term ‘last resort’ by Which? again in a two page section covering ERS in its Guide on health care funding for the elderly (http://www.ship-ltd.org/bm~doc/22-sep-08.pdf and http://www.money-advice.net/media.php?id=3253 respectively).
the other. The variety of preferences does however mean that the different propositions will cater for different consumer psyches. One argument could even go to say that the current environment in 2008 and general distrust for financial services as a result of the banking crisis, will support the Sale Model vis-à-vis the Loan Model which is more associated with the financial services people are familiar with.

7. Risks and benefits

a) For providers

Market growth so far has been attributable to specialist lenders and insurers. Mainstream banks are yet to enter the market. Several have nevertheless led pilot programmes investigating the feasibility for them in entering the market\textsuperscript{116}, but despite this, they still remain tentative for reputational reasons. Providers can also benefit from the psychological shift in the attitude of most Britons towards considering ERS. This is in a large part driven by the realisation by elderly homeowners that their own children do not actually need all the money which they have accumulated in the value of their home (largely due to the sustained growth in house prices over past years).

Risks for UK providers are similar to those that apply to all providers generally so we would refer to the general section of the report in Part I. Though some big equity release providers (Northern Rock and Bradford & Bingley) have had difficulties as a result of reliance on securitisation, equity release providers do not apparently need to resort to these forms of funding and thus are not more vulnerable to the credit crisis than other lenders. Along with the different funding methods, their attitudes to risk are different too. As mentioned already, the current climate in the UK and resulting lack of confidence in financial services generally, will undoubtedly have some impact on potential consumers avoiding the product over the short-term\textsuperscript{117}.

b) For consumers

(1) Benefits for consumers

Experience from advisers testifies to greater demand from pensioners for information on equity release with an emphasis in many cases on avoiding an increased tax bill as a result of asset price inflation over recent decades\textsuperscript{118}. One of the problems that is less common now as a result of more flexibility in the ability to drawdown a more appropriate amount of money, is the practice of advisers receiving a double commission as a result of them selling an ERS and jointly selling an investment product with the lump sum the consumer received\textsuperscript{119}.

As described in the product section, a considerable benefit which certain schemes contain today, and which are almost unique to the market in the UK, is that a consumer is able to leave a proportion of the equity totally protected, thereby ensuring that not all the potential inheritance is used up during later years. There is also some interest for more government involvement with ERS in the UK and this is particularly centred around the area of social care funding\textsuperscript{120}.

\textsuperscript{116} E.g. HSBC.
\textsuperscript{117} Based on conversations with UK stakeholders during a research team visit to the UK.
\textsuperscript{118} From conversations with members of the UK Financial Services Consumer Panel.
\textsuperscript{119} See (fn 117).
\textsuperscript{120} Examples can be found in the following publications: Caring Choices, The Future of Care Funding - Time for a change, 2008 (http://www.money-advice.net/media.php?id=3299), King, Nigel, Berry, Diane and Pannell, Jenny, Rainy days and silver linings: using equity to support the delivery of housing or services for older and
(2) Risks for consumers

The FSA regulation of the market has been good and it would appear that the regulator feels that what it previously formally referred to as a high risk product is now better under control. However, the vulnerability of the customer base will mean that this market will always be supervised as having a high risk of consumer detriment. The level of consumer protection has improved significantly in a large part due to the broad extension of the no negative equity guarantee to almost all product offerings. This is largely due to the code of conduct drawn by the Safe Home Income Plan and the continuous growth in providers which became members of the trade association over time.121

(A) Advice

Key to avoid the risks of inappropriate products being sold to consumers is the level and quality of pre-contractual advice or information that has been given to the consumer. The UK has detailed information on this and it is presented under the legal section above 122. One element of risk in the field of advice is that some see as possibly detrimental to the consumer that ERS can still be sold directly without the input of an independent financial adviser. Mandatory financial advice may be an option with extra costs for both providers and ultimately the consumers but these will be outweighed with the knowledge that advice was received before purchase of an ERS. Lessons could be taken from the US experience, which would help improve the clarity and comparability of the products available on the market. Generally, this disadvantage in terms of clarity and ease of choice is the flip side to all the innovation that the UK market has witnessed especially in terms of the different product features and flexible catering to the customer’s preferences.

A further comment raised by respondents on the subject of advice, was related to ‘dabblers’, i.e. financial advisers that were involved in the sale of ERS but without real conviction and professionalism. This leads on to a more general suggestion to make the market safer, and thus more prepared to grow, by improving the general level of quality in advice (by both prohibiting certain uncertified advisers and improving necessary qualification level). The FSA has nevertheless made its expectations very clear with regards to bad advice in the sale of ERS, and the two mystery shopping exercises appear to have helped deal with certain element of mis-selling.123

Stakeholder responses also point to the desire to see a more regulated advice procedure, whereby distributors of the product should make sure that the family of the consumer is systematically included into the process, or that this should officially be recognised as

121 This added benefit (or safety mechanism) is judged to be so important that we were told in conversations with Which? and other consumer representatives that they would rather see the existing products with this guarantee than much cheaper products without it. The suspicion that competing providers offering a product without the no negative equity guarantee might be able to consequently offer more price competitive products was not confirmed by any of the respondents that we met.

122 See Section 5.9)3 on advice and information provision above (on p.21).

123 Links to work by the FSA include: a 2005 press release discovering that consumers were not being properly advised on equity release (http://www.fsa.gov.uk/pages/Library/Communication/PR/2005/054.shtml); A 2006 report containing mystery shopping results in the sale of lifetime mortgages (http://www.fsa.gov.uk/pubs/consumer-research/crpr53.pdf); and a 2008 Mortgage effectiveness review on lifetime mortgages including sub-prime loans (http://www.money-advice.net/media.php?id=3307).
best practice. The implications of ERS on social benefits, etc. is an area where providers should be better able to advise on.\(^\text{124}\)

**B) Complaints**

One in every ten people who intended on taking out ERS will end up actually taking one. This shows that information is allowing selection to take place. Furthermore, there are no registered complaints that refer to someone not having wanted the product. Most complaints are about early repayment charges. Home reversion has not received a single complaint though the FOS does contain case studies with mostly complaints made by the heirs of those having concluded contracts (children but also siblings)\(^\text{125}\).

**C) Valuation of the property**

A specific risk factor with regards to Sale Model ERS in the UK in terms of consumer detriment is with regards to property valuation. Although the law concerning home reversions clearly states that the valuer is the agent of the consumer, there appears to have been a significant drift in actual practice as this is reported to be no longer the case. This is strongly attributed to the fact that regulation of Loan Model products do not have this same requirement and therefore providers are all too content to select the valuer they are used to do business with. The argument is that a valuer selected by the consumer himself may be a better objective judge of the property’s worth (an especially key component for the Sale Model since it involves a sale).

**D) Low income earners**

A potential ERS customer needs to consider many things before buying an ERS. In the UK, the customer will need to take special advice, from suitably qualified advisers, about not only the potential effect of ERS on their estate (which is important for all ERS products in whatever country), but also about the implications or not on any state benefits which the person is or may be entitled to. This level of complication in terms of the suitability of this product for persons on very low incomes is specific to the UK market.

**E) International**

A phenomenon that has been gradually taking place over the years in the UK, is that a growing number of British citizens, motivated by both economic (e.g. lower cost of living) and non-economic factors (e.g. a warmer continental climate), have been buying properties abroad (mainly France and Spain) either as holiday homes or as homes to live in during retirement. These expatriates (former UK consumers) are increasingly finding themselves in financial difficulties due to the recent economic environment (e.g. falling house prices in Spain, low pensions, exchange rate changes etc.) and considering an ERS with the property they own in their adoptive country\(^\text{126}\). Though UK customers may be

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\(^{124}\) The Council of Mortgage Lenders makes information available to assist its members in discharging their advising responsibilities. This is described in detail in the report *Equity Release and the impact on benefits/tax* (available at http://www.cml.org.uk/cml/filegrab/ER&theimpactonbenefits&taxApril2006.pdf?ref =3510). Ferret Information Systems is the co-developer (with the CML) of the FINTAL software package that is intended to help advisers with the calculations of benefits/tax implications.

\(^{125}\) See Financial Ombudsman Service website under http://www.financial-ombudsman.org.uk.

\(^{126}\) See (fn 118). There have also been media reports such as Hanrahan, Brian: *UK expats face Spanish troubles*, May 14, 2008 under http://news.bbc.co.uk/2/hi/business/7400846.stm. (Note that according to the Institute of Public Policy Research, more than 3.3 million British pensioners are likely to be living abroad by 2050, and statistics from the Association of British Insurers show that expats save even less than the third of Britons who are not saving any money at all for their later years, and that a third surveyed said they intended to invest mainly in property to fund their retirement.)
culturally used to the practice of equity release, they are however in a different situation when they find themselves abroad with very little idea about the regulation in their new country of residence. A question which regulators will feel an increasing need to answer, is the question of the FSA’s duty to advise and general obligation to provide the same standard of services to UK citizens everywhere including those living abroad.

(F) Other products and contagion of negative press

There are many products that may appear similar to ERS, however, despite certain characteristics in common with the schemes investigated in this research study, they are in fact distinctly different for various reasons. To name just two examples, the design of new mortgage products with lower monthly payments for the consumer (e.g. interest-only mortgages or longer term mortgages) and the appearance of sale and rent back arrangements, do not meet the criteria of repayment from sale of the housing asset (as distinct from repayment from a future expected income stream) and long-term housing security respectively\textsuperscript{127}. In the UK, as outlined above in the Product section on page 7, there has been growing activity by firms offering to buy the housing asset from indebted persons in the form of a ‘quick fix’ that may not be in the long-term best interest of the homeowner. These offers are often associated by the homeowner as equivalent to an ERS when in fact it is not. The UK Office of Fair Trading report from October 2008\textsuperscript{128} has suggested that industry should promote self-regulation, because it expects that it will take a long time for any regulation of the sale and rent back market is decided, and put within the remit of the FSA. In the meantime, there is a risk that ERS could be tainted by these very different and as yet unregulated products. The unfamiliar and highly pressurised situations that these people find themselves in may leave them particularly vulnerable to misleading statements or valuations from sale and rent back firms looking to make a deal. Even those customers for whom sale and rent back might be the best option could be unaware they are currently bearing almost of all the risks.

\textsuperscript{127} The definition of an Equity Release scheme and the delimitation of the scope of this research is explained in Section A of Part I: General Report.

\textsuperscript{128} The OFT report on “Sale and rent back schemes” can be found under: http://www.money-advice.net/media.php?id=3302.
II. Spain

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Spain</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>86.3</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>13.0</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>22.4</td>
<td>20.6</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>646.7</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>13.1</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>61.6</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>14510</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>84.5</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>75.6</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>2296</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>45.3</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>17.1</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>24.2</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>16.6</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>21</td>
<td></td>
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</tbody>
</table>
| ERS Market?                                        | Developed ERS market |}

Spanish population lies in the region of 46 million inhabitants, with a 17.8% of over 65 year olds in the population\textsuperscript{129}, a percentage which is expected to increase rapidly in the future\textsuperscript{130}.

The development of ERS in Spain is linked to growing longevity, progressive ‘dismantling’ of the traditional family structure that looks after elderly people, and the need to supplement public pension schemes.

The Spanish public system of pensions is a ‘pay as you go’ contribution system. Contributions to Social Security pension schemes are paid both by workers and by employers and they serve the aim of funding ‘contributive’ pensions to retired population. Following the passing of Law 24/1997 of 15 July that reinforced transparency in relation to sources of funding, it is now possible to gather more accurate data on what

\textsuperscript{129} Data taken from official INE (Instituto Nacional de Estadísticas) sources.

\textsuperscript{130} See below, in particular (fn 135).
percentage of this public pension is paid for by the contributions of the existing workforce\textsuperscript{131}. It is only at the end of 2007 that income received from contributions covered the total amount being allocated to these pensions. Non-contributory pensions, those received by persons that did not pay up contributions for the number of years required by law, are funded by the General State’s Budget\textsuperscript{132}. Additionally, in Spain, pensions and public expenditure to cover social care for old age and dependency are decentralised to the finances of the Autonomous regions, giving way to a lack of uniformity throughout the country and which will be much dependent on policy options chosen by each community.

In Spain, there has been a long standing tradition of home ownership and little debt. Though this trend towards home ownership is continuing, the past 15 years has seen this ownership being strongly supported by borrowing rather than through savings (e.g. the Bank of Spain reports a 90% homeownership rate as an average for the last 8 years). The home is traditionally considered to be the main asset for the extended family. Home ownership, public pension schemes, personal savings and family support have all allowed for the taking care of the needs of the elderly people. Most persons over 65 are owners of a home that now has significant value in Spain. Real estate by way of homes are considered as a source and sign of wellbeing, and it has not been a tradition to use this wealth to obtain liquidity during one’s old age\textsuperscript{133}. The family house is usually a material part of the deceased’s total estate left to his or her heirs and heiresses. Furthermore, it combines around it the idea of being a mixture of an asset kept for ‘caution reasons’ and an asset to be left to future generations, in a certain altruistic fashion. There is even a deep rooted tradition that the family member that “stays” with his/her elderly parents will then receive the home by way of a kind of “consideration”\textsuperscript{134}.

However, evolution in living conditions, and the fact that it is nowadays becoming increasingly frequent for the ‘carer of the elderly’ to not actually be a family member but a third person recruited form the labour market, means that traditions change over time.

In recent years, the Spanish population shows a clear ageing trend. Greater ageing of society is a fact known and affecting economies the world over. In Spain, a lower than world average birth rate, and a long and growing life expectancy will put considerable strain on existing levels of pension provision. Sociological changes such as mono-parental families, high rate of divorces, immigration etc. are also adding to this, with the result that these changes together are leading to an increasing awareness that public protection plans and family support may not suffice\textsuperscript{135}.

Given all the above circumstances, Spanish governments have proposed several measures related to dependency over the past 5 years. More recently still, a reform of

\textsuperscript{133} See OECD report Ageing, Housing and Urban Development (2003).
\textsuperscript{135} For a summary comment of this situation see the following within Generalitat de Cataluña, Directorate of Economy site. http://www.invenia.es/oai:dialnet.unirioja.es:ART0000079249. By way of example, it is expected that by year 2020 a 6,2 % of Spanish population will be over 80 years of age and by 13,3% between 65 and 79; and by year 2050 a 19,1% of Spanish population will be between 65 and 79 years of age and 9,1 % of Spanish population will be over 80 years of age, see IMSERSO (2005). Las personas mayores en España. Informe 2004 y INE: INEBASE: Proyecciones de la población de España.
the Mortgage Law (Law 41/2007) related to the Personal Tax law has been passed to regulate ERS, by way of linking certain tax benefits to those schemes, as described in the Law. Among the measures introduced, there were some tax benefits and fee exemptions granted to users of reverse mortgages (the name for Loan Model ERS in Spain). These reverse mortgages by the way they are regulated in Spain are a product with narrow and detailed requirements compared to the previous product called by the same name that some credit institutions had been already offering before the law was passed. Provisions approved by Parliament should have been further developed by the Government (Ministry of Economy), but this currently continues to be behind schedule as of November 2008. When completed, these reforms could lead to an increase in future market size for Loan Model ERS, particularly if this there is a corresponding reversal in the current difficult mortgage market.

2. Products

The modalities of products in terms of function and parameters such as the duration of the income perceived differ. The reverse mortgage can have a credit line format (the most usual and typical option offered and chosen) or a lump sum. If a one lump sum is used, in almost all cases an insurance contract is also signed. This is done in order to have an insurance policy providing a life annuity perceived as a monthly income which is then used to credit the interests that are generated by the loan.

a) Loan Model ERS

The Loan Model scheme known in Spain is that of a financial operation carried out normally with a bank, although theoretically it could be operated privately. The owner of the house – which does not necessarily need to be his/her place of residence - creates a charge (normally a mortgage) and thus receives capital or monthly advances from a sum of capital for an agreed period of time (either an agreed fixed period or for lifetime). The owner maintains ownership and use and in case that he/she wants to receive a life annuity he/she can (should) contract a life insurance policy with part of the capital received from the provider. This scheme is then usually (though not necessarily) linked to a life insurance contract (Policy insurance for a life pension or Seguro de Rentas Vitalicias), which according to Spanish insurance regulations must be contracted with an insurance company which offers the insured a periodic amount, typically monthly, for his or her life.

The following is the standard operating system in Spain for this type of product. The credit institution carries out a valuation of the real estate asset (used to calculate the maximum loan amount), and makes calculations taking into account the age of the applicant or applicants including statistics on life expectancy (which serves to define the period for recurrent advances, ‘period of disposition’ for disbursement of funds to the applicant). When the maximum loan amount (which includes all expenses, as well as

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136 Additional Disposition 4, of Law 41/2007 referring to art 51 of Law 35/2006 of the 28th of November of the Law on Personal taxation (Impuesto sobre la Renta de las Personas Físicas). To this aim, annuities perceived are subject to the same treatment as that received by retirement plans as contained in point 3-b of art 51 of the said Law, which is tax exemption after 10 years of receipt of the first annuity payment.


138 See Jubilarse en Casa, point 3 f.

139 Percentages of maximum indebtedness to calculate available rents to customers are in a region between 40% and 100% (Jubilarse en Casa, point 3 h).

140 When the mortgage is contracted by a couple the age of the wife is set as a reference (Jubilarse en Casa, point 3 f).
interest) and period of disposition\textsuperscript{141} are calculated, the provider will then set a maximum monthly payment amount.

Customers’ financial reward is received either by way of a monthly payment paid at the beginning of the month (a fixed constant amount, or an amount which increases over time, depending on the terms of the contract); or by way of a lump sum received upon completion of the agreement. This later modality allows the customer to better face expenditure on big ticket items such as home refurbishing, repayment of previous existing mortgage debt, etc.

Providers recover the total amount (credit plus interests and costs) upon either the date of expiry (when the Loan Model ERS is one with a fixed term); or upon the death of the applicant or the death of the last beneficiary. At this time, in accordance with Law 41/2007 art 1 point 7, the heirs can implement a number of options. Firstly, they can choose to repay the loan (i.e. cancel the credit) in which case no penalty can be imposed on them with respect to the said cancellation. Secondly, the heirs may decide to obtain a fully new credit agreement with the provider, in which case this possibility is left entirely up to the wishes of the parties to the new credit contract (i.e. the heirs when they become the new owners and the credit provider). Lastly, the heirs may decide to let the financial institution simply repossess the home (i.e. allow for the implementation of the provider’s rights under the mortgage deed). If heirs follow this later option, all schemes that were concluded in accordance with the Loan Model subtype of Law 41/2007, benefit from a certain ‘cap’ on the amounts to be recovered by the credit provider. Additional Disposition, art 1.6, of that Law sets that the provider can seize the mortgaged property and the estate of the deceased, but the provider’s recovery action cannot reach the heirs estate. This implies that the deceased’s estate is the limit to recovery by credit providers. Legal experts have pointed out that this limit could be interpreted as affecting only Loan Model ERS that follow the subtype of Law 41/2007\textsuperscript{142}.

When reverse mortgages are contracted on a lifetime basis, an insurance policy is also subscribed to. The initial disbursement received by the customer can be used to pay the insurance premium. The terms and conditions of these policies can vary from one provider to another.

For those having contracted with a lump sum option, the returns from the associated insurance product vary. This is usually the main element of differentiation between the various proposals of the providers. Depending on the performance of this life annuity, one with additional benefits will affect the debt differently (from no effect on the debt and thus rolling up, to coverage of the interest payment on the debt, to repayment of the loan)\textsuperscript{143}.

In terms of the costs to the consumer of the Loan Model ERS in Spain, as of September 2008, fixed interest rates were between 5.75% and 7.89%, whereas variable interest rates vary between Euribor +0.75 and +2.00.

b) Sale Model ERS

Sale Model ERS (created around a sale contract) are also schemes to obtain liquidity from immovable assets, namely from residential property. They operate by way of a contract whereby the owner transmits the ownership of the fixed housing asset while maintaining

\textsuperscript{141} Most providers agree on a fix interest rate during the “disposition period”, but the interest becomes variable rated afterwards, if the agreement is completed for a longer period that the one in the “disposition period”.

\textsuperscript{142} This situation has been heavily criticised because it introduces particular risks for the heirs in cases of Loan Model ERS that are contracted outside the frame of the precise model of Law 41/2007. See JA Miquel Silvestre ‘Hipoteca inversa, algunas hipótesis de conflicto’, in Diario la ley n. 6924, 14 April 2008, ref D-116.

\textsuperscript{143} Jubilarse en Casa.
the lifetime right over its use and the right to receive a life annuity pension. Its basic regulation can be partially found in articles 1802 to 1808 of the Spanish Civil Code *Renta Vitalicia* (Life Rent), although this lifetime ‘rent’ is combined either with a tenancy contract or a usufructo (right to use and rent).

By transferring ownership, the vendor is released from encumbrances such as payments of local taxation (IBI), and maintenance of communal areas. Monthly payments receive a beneficial regime under tax law.

Furthermore, there are some recent samples of regulated private law contracts which serve to the effect of ensuring life care for elderly people on exchange for the handing over to the rent/care provider of a property. This property (which does not need to be a private residence, or even an immovable) can be transferred either by the recipient or by a third person (Law 2/2006 of Civil Law of The Autonomous Region of Galicia).

### 3. Providers

21 providers are selling a Loan Model ERS in Spain. These are the Caixa Kutxa, Ibercaja, Bancaja, BBVA, Caixa Terrassa, Caja Vital, Caja Inmaculada, Cajasol, Catalanian West, Caixa Manresa, BBK, La Caixa, Caja Duero, Caixa Sabadell, Caja Navarra, Caixa Galicia, Caixa Girona, Caixa Penedés, Sa Nostra, Caja de Ingenieros, Caja Castilla la Mancha.144

Spanish providers typically offer their reverse mortgage products through their own sales network, though sales via intermediaries do exist.

In relation to Sale Model ERS, they where offered some 10 years ago, but we are not aware of this product being commercially available at present. Among the providers which were active in the past we are told by stakeholders from the supervisory authorities that major banks such as BBVA were previously involved in their sale.

### 4. Market

The term ‘Equity Release scheme’ as such is not known in Spain. Providers explain that the term reverse mortgage is better known but that they themselves prefer to avoid using the term ‘mortgage’ for this type of product.145 However, there are various types of products known in the Spanish market which comply with the ERS definition as provided earlier in this report.

For Loan Model products (mortgage type of product), some credit institutions have been known to offer these reverse mortgages since 2001.

The market has been stimulated by recent legislation (Law 41/2007) that regulates some requirements146 and attaches exemptions on some Tax (Stamp duty), Notary and Registrar fees with regard to Reverse Mortgages that are contracted within those requirements. Until the passing of Law 41/2007, not all financial Institutions offered Loan Model products and today’s credit and real estate crisis does not seem to be the best environment for its development. However, a number of providers are introducing their own reverse mortgages. These include the BBVA Group, Banco Santander and a number

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144 The names of the providers actively involved in marketing ERS in Spain have come from various sources but were most recently updated by Optima Mayores in their 2008 report analysing the ERS Market in Spain (3 extra providers were identified in this contribution: http://www.money-advice.net/media.php?id=3257).

145 Ley 41/2007 de 7 de diciembre por la que se modifica la Ley 2/1981 de 25 de marzo, de Regulación del Mercado Hipotecario y otras normas del sistema hipotecario y financiero, de regulación de las hipotecas inversas y el seguro de dependencia y por la que se establece determinada norma tributaria. Boletín Oficial del Estado, 294, 8th December 2007, pp.50593-50614.
of “Cajas” (or savings banks) such as: Iber Caja, La Caixa, Caja Madrid, Caixa Girona, Bilbao Bizkaia Kutxa (BBK), Caixa Galicia, etc.\(^\text{147}\)

Following the passing to Law 41/2007, it was expected that most of Spanish Financial Services, Credit and Insurance Providers would enter this relatively young market, whose level of development and success is still relatively unknown. A recent study on awareness and potential demand for Loan Model ERS in Spain by one of the providers\(^\text{148}\) provides an indication of the potential market. The results include: 74% of those surveyed and needing care would prefer to live their old age at home (52% with family assistance while the other 22% with external assistance); 57% of those polled had heard of reverse mortgages (33.3% said they believed that this product is ‘very interesting’ or ‘quite interesting’, compared to 45% saying they would never be interested in such a product and 37% said they would do it in case of economic difficulty). Many would prefer to complement their pension by resorting to their own savings (29%), turning to family aid (22%), or selling their property outright (18%).\(^\text{149}\)

The Spanish market for ERS has only a limited number of transactions to date despite the first product having entered the market a number of years ago. The estimated number of contracts today reaches 6,500. Figures from the last two years suggest a growing trend, 3,800 contracts in 2007 following from 1600 in 2006. However, uncertainty over the immediate future of this trend looms as a result of the current economic environment affecting the Spanish economy and housing market more specifically. Although the market currently does not allow for economies of scale for the providers and the fixed costs of their operations, there is a shift in the attitudes towards inheritance (as mentioned above).\(^\text{150}\)

For Sale Model schemes, \textit{Vivienda Pension or Home Pension Schemes} are known in Spain. These schemes are based on Articles 1802 to 1808 of Spanish Civil Coded of 1889. Commercially, this type of product was sold 20 years ago but we have found no data to show that it is sold nowadays. Stakeholders, consumer experts and private lawyers explain that this type of contract is organised privately, usually among family relations.

In terms of data or information, there is no single public official register for reverse mortgages. Theoretically, institutions that could provide these data include the AHE (Spanish Mortgage Association), the College of Registrars of the Property or the Ministry of Economy, however, as was seen during this research study, the current data is only really supplied directly by the providers concerned.\(^\text{151}\)

\section*{5. Legal situation}

a) Loan Model ERS

Given the possibilities and externalities that ERS generate, incentives have been put into place to cover or guarantee one particular type of scheme. Advantages and protection is

\footnotesize{\textsuperscript{147} Among the more active providers we find savings banks (\textit{Cajas de ahorros}): La Caixa, Caixa Terrasa, Caixa Manresa, Caixa Sabadell, Caixa Girona, Caixa Penedés, Kutxa, Caja Vidal, Caja Navarra, Ibercaja, Caja Inmaculada, Cajasol, Caja Duero, Caixa Galicia; But banks are also offering this product, in particular BBVA, and other Financial Institutions such as Catalana Occidente (Jubilarse en Casa, point 3 c).

\textsuperscript{148} Surveys carried out whose results are published in the study "The wealth real estate agency: An ATM" for the older people", XX prize Dr. Rogeli Ducastella of the Foundation The Caixa (provided to us by Jubilarse en Casa).

\textsuperscript{149} From contribution from Jubilarse en Casa.

\textsuperscript{150} From contribution from Jubilarse en Casa.

\textsuperscript{151} Only 4 of the 18 providers directly cooperated with our study and helped contribute a completed questionnaire.}
offered to potential consumers of these schemes (i.e. tax and fee reductions), their beneficiaries (i.e. by impeding that the provider charge cancellation fees on heirs wishing to repay the loan upon the death of the applicant) and to financial institutions (because the Law provides benefits to only a particular scheme for which financial institutions and/or insurance firms need to be authorised to operate in Spain). This also allows the development of specific mechanisms to increase transparency and consumer protection. Those incentives are linked in Spain to a particular form of Loan Model ERS (reverse mortgage) that fulfils a number of prerequisites.

Various subtypes of the Loan Model agreements are possible under private law. There are many contractual situations capable of existing under general Spanish law. However, only those fulfilling all requirements set in Law 41/2007 are linked to the tax incentives introduced by the law. Loan Model ERS, as regulated in Law 41/2007, apply to a credit contract guaranteed by a mortgage. Moreover, this credit must be provided by a financial institution that fulfils the requirements of any other mortgage provider in Spain, and must be signed before a public Notary and registered as a charge upon the real estate in the Land Registry. Following general mortgage law, upon personal bankruptcy of the debtor, the mortgagor holds a priority claim over the mortgaged asset. These hipotecas inversas (inverted or reverse mortgages) are contracted following requirements that are listed in Additional Dispositions 1 and 4 of Spanish Law 41/2007 of 7 December. These schemes benefit from a special legal regime.

The legal definition of Hipoteca Inversa to qualify for this special regime is: "Reverse mortgage is a loan or credit warranted with a mortgage over an immovable asset".

The following conditions have to be met in order to qualify for the benefits of Law 41/2007:

- **Home**: The mortgaged property must be the permanent residence of the applicant. This home must be insured against damages. Spanish law 41/2007 includes some references to heirs and beneficiaries. However, no mention is made in the law to any prior information rights of potential legal heirs, other beneficiaries, or third persons that may live in the property together with the applicant. Providers inform us that heirs or other dwellers of the mortgaged property are not asked to fill in any form, nor declaration etc., and that they are not consulted nor informed by the provider.

- **Provider**: Providers must be credit entities and insurers authorised to operate in Spain.

- **Advice**: In accordance with Law 41/2007 on reverse mortgages (of the type which is described in that law), credit providers must grant independent information to consumers. Point 4 of art 1 of the said Law imposes upon the Spanish Ministry of Economy, the duty to draft specific information procedures. This secondary legislation is still pending as of November 2008. Law 41/2007 establishes that providers are under the obligation to give applicants, independent advice, taking into account the applicant’s financial situation as well as risks associated with this product. The said advice is to follow regulations to be

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154 Additional provision 1.10 of Law 41/2007 acknowledges that Reverse Mortgages can be completed over other immovables, although in those cases the scheme does not benefit from the beneficial regime created under that Law.
155 Terms of this Insurance is established in Arts 7 and 8 of Law 2/1981 on the Regulation of Mortgage Markets.
156 Additional Disposition 1, Art 1, point 5 of Law 41/2007 prohibits that providers charge cancellation fees when heirs wish to repay the loan.
established by the Ministry of Economy. Seeing as these supplementary regulatory measures have not been passed yet, providers consulted report that customers are given a written brochure with all due information. Providers also inform that heirs, or potential heirs, are not given specific information, nor are they made to sign applications or other type of documents.

- **Applicants:** The applicants/debtors must be 65 years of age or more, and/or be affected by severe dependency or great dependency (this term is defined by Spanish Laws and in particular Ley 39/2006, for the Promotion of Personal Autonomy and care of persons with a dependency).

- **Payment:** Credit can consist of funds accessed either as a lump sum of money or through various instalments.

- **Termination:** The credit is usually completed on a lifetime (lifelong) basis. However, it can be cancelled under various circumstances. Firstly, upon the wishes of the mortgagee, who must in this event, satisfy the provider with a refund of capital plus interest. Secondly, upon the sale of the property (this situation is expressly provided for in Additional Disposition 1 of Law 41/2007), in which case the provider can ‘call in the loan’ unless a substitutive guarantee is provided (sic).

- **Debt recovery:** Upon the death of the mortgagee, or upon the death of the last beneficiary, the provider ‘calls in’ the credit. In this later situation, the creditor can recover the value of the loan plus interest against the mortgaged property and against the deceased’s estate. It is implicit in the Law that heirs could repay the loan and free the asset.

- **Benefits:** Schemes which fulfil the above indicated terms – as per Law 41/2007, benefit from a reduction on the Taxation of Public documents Drafting (notarial documents) (Tax on Actos jurídicos documentados, similar to Stamp Duty). There is also a reduction on Notary and Registrar fees. For such schemes the Law allows that the lump sum or the instalments received by the applicant and/or by the beneficiaries of the reverse mortgage scheme be invested totally or partially to contract another retirement plan (as described in Art 51.3 Law 35/2006 on Personal Taxation). These payments are assimilated to those from retirement funds (art 51.3.b of Law 35/2006) and have a beneficial Tax regime. As in other mortgage schemes, mortgage law imposes upon the credit provider that the mortgagee has a right of early repayment (amortisation). When the mortgage has been created over a home by a natural person, the bank cannot charge any commission or penalty for early amortisation in accordance with Art 7 of Law 41/2007. In other situations (Law 2/1981), those commissions for early repayment cannot exceed: i) 0.5% of the early repaid capital when the early repayment is done within the first five years of the life of the credit or loan; or ii) 0.25% of the early repaid capital when the early repayment is done at a time after that indicated in the previous point.

- **Costs:** Notwithstanding the benefits referred to above, there are some charges linked to the formalisation of the mortgage: property valuation (which is usually

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157 Art 26.3 of Law 39/2006 defines ‘Gran Dependencia’ as that of persons than need assistance to carry out basic acts of life several times per day; or persons that have lost personal autonomy (mental, intellectual, physical, etc) and are in need of daily support.

158 Some experts interpret the limitation to the deceased’s estate as confined to schemes contracted under Law 41/2007. See JA Miquel Silvestre *Hipoteca inversa, algunas hipótesis de conflicto*, in Diario la ley n. 6924, 14 April 2008, ref D-116.

159 Beneficial regime on the constitution, subrogation, novation and cancelation of reverse mortgages with fulfil the criteria established in law 41/2007. There are also exemptions with respect to notary and registrar fees.
carried out by the expert agents selected and used by the credit provider); notary fees and property registry fees. These charges are in the region of a 7% of the value of the real estate property.

- **Interest**: Informational flyers, brochures, leaflets from providers show that these products are offered on variable interest rates related to Euribor.

b) Sale Model ERS

Spanish personal tax Law (IRPF) declares an exemption from the payment of personal gains tax the increases in the value of residences by persons over 65, and reduction in notary fees. The same Law creates a beneficial regime for periodic rents received by persons over 65 (this is the same regime as seen for reverse mortgages).

It can be concluded in a number of different ways: among private persons, through an estate agent acting as the intermediary for an insurer, directly with an insurer, or otherwise. The various subtypes have the sale of a house in common. The contract is not typified by law, and can therefore be completed with different contents. Generally, the sale contract contains a reversion clause in such a way that the vendor would recover property should the acquirer breach the contract by way of not paying the amounts agreed. There exist different modalities.

Although this is not a typified contract, its basic regulation can be partially found in articles 1802 to 1808 of the Spanish Civil Code under ‘renta vitalicia’ (life rent/pension), combined either with a tenancy contract or a ‘usufructo’ (right to use and rent). Also, there are some recent samples of regulated private law contracts that can sometimes be assimilated to this type of Sale Model ERS. They serve to the effect of ensuring life care for elderly people in exchange for the handing over of a property to the rent/care provider. This property (which does not need to be a private residence, or even an immovable) can be transferred either by the recipient or by a third person (Law 2/2006 of Civil Law of The Autonomous Region of Galicia). Among the features of this contract, designed specifically by the regional administrative authority of this particular autonomous region, one notices that it introduces a speciality which makes it different from the renta vitalicia of the Spanish Civil Code. If Sale Model ERS are interpreted in accordance with renta vitalicia, the vendor has no right to recover ownership of the property even if the provider breaches its obligations for a life annuity payment. Instead, Law 2/2006 of Galicia, allows for ownership recovery in case of a breach. This Galician Law aims for the acquirer to provide for care, or for a pension, to the property transferor in his or her old age. However, because this provision can be implemented directly or indirectly, we consider that it includes the possibility for the acquirer to contract an annuity or a similar instrument for the benefit of the transferor.

In general, under Sale Model ERS, the homeowner gives ownership of the real estate and receives a consideration either for himself/herself or for the benefit of a third party referred to in the contract. This consideration can take the form of: an advanced lump sum and a monthly income for life; or a life annuity usually paid in monthly installments; or services (for instance in health care received in the home). The beneficiary maintains the use for life, this is, the right to use, rent etc the house for his or her lifetime. The beneficiary receives a pension payment with periodic increases as agreed (usually independent from changes in the market). The main risk for the provider of this payment is longevity.

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Another subtype is such that the owner sells the house and loses possession in exchange for a place and care in a retired person home.

Sale Model products can also be used by couples or a group of persons. In this situation, the life annuity payment is calculated on the basis of the youngest person. Upon the death of one of the beneficiaries the other continues receiving the use of the house in exchange for the same monthly payment.

Finally, it is possible in Spain to sell or to maintain possession by way of the owner becoming a tenant. Lawyers consulted point at the fact that this is arranged privately, usually within family relations. Providers and stakeholders report that this was commercially introduced in Spain over 20 years ago.

6. Reasons for lack of further development of the markets

a) Legal barriers:

There do not seem to be clear legal barriers to the development of ERS in Spain. Requirements to qualify for tax exemptions cannot be considered barriers. Loan Model ERS, are complex financial services and as such have an associated insurance product. The policy issuer must be a registered insurance company. Lenders must be registered credit institutions or registered insurance companies in order to qualify for benefits under Law 41/2007161.

Experts have nevertheless criticised ERS pointing at various facts. On the one hand, they underline, particularly in relation to Loan Model ERS, that the nature of the contract is so different from that of a ‘normal’ mortgage, that it can become unfeasible to apply common Mortgage Law to reverse mortgages. This holds true even under circumstances where the legal system does not provide for a specific solution to a given conflict related to reverse mortgages. On the other hand, legal experts tell us that the limited scope to Law 41/2007 leaves many potential contractual situations outside its regulation, thus leaving many questions unanswered. For instance, comments have been made along the lines that no provision is in place in order to cater for situations that are becoming known such as in cases relating to the ‘disappearance of elderly people’. In Spain, a time lapse of 10 years is needed to obtain a formal declaration of ‘disappearance’ for people over 65, (the equivalent time period is 5 years in cases of persons over 70). This formal declaration allows the opening of the way to inheritance procedures. However, nothing is foreseen in relation with the interim period162.

In relation to Sale Model ERS, the lack of clear regulation does appear to be a barrier. As stated above, in such a contract the transaction is construed following the Civil Law of Spain, and the vendor does not have a real remedy against breach on the side of the provider (apart from a damages remedy, which in any case, could be heavily encumbered by the event of the provider’s bankruptcy for instance). Modern, but geographically limited regulations such as Law 2/2006 of Galicia introduces the possibility for the vendor to recover ownership, but its scope of application is limited and it does not only refer to the sale of immovables but to the transfer of any property.

b) Economic barriers

ERS in a wide sense have existed for a number of years. However, their introduction as a standard financial product is relatively new. The current fluctuations in real estate values

161 See Section 3 a) above on Legal situation in Spain (on p.44).
also have consequences on the development of ERS, with the current domestic housing market and bank preoccupation on capitalisation and liquidity not facilitating the introduction of new ERS schemes in the immediate short-term. The present financial crisis together with the specific Spanish crisis affecting its real estate sector has affected those factors, but as explained in the next section on benefits, the medium-term outlook does not constitute an overwhelming barrier.

The current economic situation aside, a more specific economic barrier is that economic amounts to which the applicants are entitled to, are not highly attractive to potential consumers considering to enter this type of transaction, unless there is a grave necessity for them to do so. For example, providers point out that a property value of EUR 100,000 allows for a regular (monthly) income of EUR 56; property value of EUR 300,000 allows for a regular (monthly) income of EUR 270.

c) Consumer barriers

ERS are considered to be complex products that could collide with consumers cultural and sociological attitudes in Spain. As previously stated, homes have been considered as the backbone asset to the enlarged Spanish family. ERS and in particular the Loan Model ERS (reverse mortgages), are also heavily related to Inheritance Law and tenant Law. However, the Law does not provide for information to be given to potential heirs (the Spanish Civil Code establishes that certain family relations such as sons and daughters are entitled to a percentage of the deceased estate, unless certain hard and proven situations occur). Providers consulted explained to us that they do not inform legal heirs about the mortgage. Spouses and other persons dwelling in the home with the mortgagee may have a residual right to maintain it use (i.e.: to continue living in the home) after the applicant dies, should the property be free of charges. Consumer organisations consulted pointed at the fact that whilst inheritance law and tenant law are not a direct legal barrier, they may create uncertainty, and can be seen as a reason for not concluding this type of product.

Additional Disposition 1-4 of Law 41/2007 announces that this law is to be developed by secondary legislation that would regulate the obligation of reverse mortgage providers to inform customers and to offer independent advice. This secondary regulation has to date not been passed. Lack of information is perceived as a barrier to consumers.

d) Cultural Barriers

Spain is still a close-family society, particularly in rural areas. The house is seen as a heritage within the family and should not be burdened with debt.

7. Risks and benefits

According to those providers who replied to our questionnaire addressed to them, there are a number of risks associated with ERS. These include longevity risk, risks related to market risk and valuation, and interest rate fluctuations. Among these, the present market conditions with falling house prices, may have contributed to ‘property valuation’ being considered by providers as the major risk.

During the past few months but particularly throughout 2008, Spain has seen a significant rise in public awareness on the use of homes to obtain funds to complement pension plans or allow for homes to be adapted to cater for the increased disability of the old. This has also been helped by Spanish banks that have launched Loan Model ERS this year. The example of BBVA announcing in major main street newspapers in January 2008

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that the Bank aims to achieve 25% share of the market for ERS in Spain, demonstrates the future market growth that is expected over the medium to long-term. Despite the decline in the Spanish real estate sector (housing prices fell by 3.2% in 2008) and severe negative ramifications on the general economy (e.g. rising unemployment and falling tax revenues due to construction and related industries accounting for up to 20% of GDP), this annual fall should be put into perspective as the first such drop in 15 years. The reversal of the domestic housing boom will reduce the size of previous housing equity levels, but allow for a moderation in prices more closely reflecting the fundamental drivers of house prices, which will be beneficial for potential sustainable growth of ERS in the future. It is highly probable that new market entries, such as that from BBVA, are related to the passing of Law 41/2007 that is giving incentives to Loan Model ERS (under fulfilment of conditions). Although the lending environment will be tight, it is important to make the distinction between conventional mortgage loans that are subject to both solvency and liquidity risks and reverse mortgage loans (Loan Model ERS) where the stability of the future borrower’s income stream is irrelevant.

However, from April 2008 onwards, reverse mortgages have become a higher risk product given the lack of credit liquidity and diminishing real estate prices in Spain. It is understandable that providers are worried about property valuation the most, and this is particularly the case because the risk of negative equity is particularly evident in Spain at present. There is a general mistrust on how properties effectively act as collateral to credit from how they have been valued (overvalued) in recent years in Spain.

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164 House prices have seen strong annual growth rates throughout those 15 years, with prices having risen by as much as 18.5% in 2003 alone. A chapter dedicated to housing markets in the IMF’s 2008 World Economic Outlook explained the serious “price gap” across many developed economies (defined as the percent increase in housing prices above what can be explained by interest rates or increases in homeowner wealth). The countries that experienced the largest unexplained increases in house prices were Ireland, the Netherlands, and the UK (30% higher than justified by fundamentals) with Spain 20% higher (similar to France and Australia). The same report also mentions that if the ratio of residential investment to total output is used as a measure of the direct exposure of the economy to a weakening housing market, Spain (along with Ireland) is a notable exception with a ratio of 9% of GDP at the end of 2007 (versus an average of 6.5% for advanced economies). As an illustration, Spain built 700,000 new homes in 2006 i.e. more than Germany, France and the UK combined. See: http://www.imf.org/external/pubs/ft/weo/2008/01/pdf/c3.pdf.
III. Ireland

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Ireland</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>74.5</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>8.4</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>21.2</td>
<td>20.6</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>139.8</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>13.4</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>75.3</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>32200</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>38.5</td>
<td>72.9</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>18590</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>4.4</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>37.2</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>16.3</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>11.2</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>27</td>
<td></td>
</tr>
<tr>
<td>ERS Market?</td>
<td>Developed ERS market</td>
<td></td>
</tr>
</tbody>
</table>

ERS have existed for some time in Ireland, where the financial services industry is now relatively mature in terms of making funds available for homeowners who may not have the future income stream traditionally required for mortgage loans. The sustained rise in house prices over the past decade, currently still readjusting downwards, has without doubt played a major role encouraging innovative lenders to take the risk of granting equity release products to a steadily growing group of customers which had benefited from an increase in their asset wealth without a corresponding improvement in their income position. Ireland has also built up its market in recent years on the back of years of experience with ERS, albeit on a small scale, together with close monitoring of developments and lessons from mistakes and advances in its neighbour, the UK.

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165 Based on the permanent tsb House Price Index, the average price paid for a house nationally in October 2008 was EUR 265,364 (compared to EUR 287,887 in December 2007). Having averaged over EUR 300,000 throughout 2007 (when valued at EUR 145,902 in January 2000), year on year rates of growth in average national prices to October 2008 were down by 10.2% (following a decline of 4.7% recorded in the 12 months to October 2007). E.g. http://www.esri.ie/irish_economy/permanent_tsbesri_house_p/.
2. Markets and products

Very little quantitative data has been available concerning the markets for these products, but these are perceived by stakeholders who responded to the questionnaire to be still small in the scheme of things. It may be expected that, following regulation of these products this year (see details on the legal situation set out in Section 4 below), a greater knowledge of the market will emerge to the regulators over time, in spite of the current economic conjuncture, which is heavily affecting Irish financial service providers in the housing market. Indeed, one provider interviewed has discontinued sales of its ERS as a result (as shown by the following message on the Shared Home Investment Plan Ltd (S.H.I.P. Ireland) website on 25.07.2008: “Due to the ongoing difficulties in the wholesale banking and the mortgage markets, S.H.I.P. has temporarily withdrawn its Lifetime Mortgage products from the Irish market. This of course will have no impact on our existing customers who will continue to be serviced as before. We expect to be in a position to reintroduce the products when normal credit conditions return and the current “credit crunch” problems have been resolved.”)

It is noteworthy, however, that despite the limited size of the equity release market, if a wider definition of ‘equity release’ is taken and the market size for more general mortgage-based credit products is reported, then data does become available167. In fact, top-up lending typically accounts for approximately 1/3 of new mortgage loans in Ireland, and around 13-14% of value. The significance of this form of secured lending means that, from a consumer protection and regulatory perspective, these loans are treated as mortgage loans. With ERS now being specifically regulated, stakeholders ranging from the regulators themselves to industry or academia hope that statistics on the lending and sale transactions of the market will soon become available to policy makers.

3. Providers

There are a number of providers of equity release products, typically marketed to elderly people, in the Irish market but, with one exception, they are not usually banks. These providers are either retail credit companies (non-deposit taking lenders) or are specialist home reversion firms. Both of these categories were brought within the regulatory framework in early 2008, which means that the provisions of the consumer protection code now apply to them as well. At first sight, the market appears buoyant with 27 providers actively supplying the market with mainly Loan Model ERS (25 of them) but also Sale Model ERS (two providers only), however because the level of intermediation is very high, not all of these firms are actually designers or originators of these schemes. 4 of these 27 providers are credit institutions (all banks) and of all the others only 3 bodies are specifically listed on the Financial Regulators website as home reversion/retail credit firms (namely, Springboard Mortgages Limited, Shared Home Investment Plan Limited, and Seniors Finance Ireland Limited). Only seven are thus true originators as opposed to intermediaries (or facilitators).

166 See http://www.shipireland.ie/index.html.
167 Source of data on the “top-up” type of mortgage lending is available from the IBF Mortgage Market Profile indicating the volume and value of new mortgage lending each quarter. For example, see the website at http://www.ibf.ie/pdfs/IBF%20PwC%20mortgage%20stats%20web.xls.
168 Retail Credit Firms and Home Reversion Firms are entities authorised under Part V of the Central Bank Act, 1997, as amended by the Central Bank and Financial Services Authority of Ireland Act 2004, to carry out retail credit firm and home reversion firm business. Again, many of the bodies as providers are just intermediaries, e.g. Blue Cube Personal Loans http://www.bluecubeloans.ie/about.asp.
4. Legal situation

The provisions of the Consumer Credit Act apply to the banking (or credit)-type product. Retail Credit Firms and Home Reversion Firms other than banks are authorised in the Republic of Ireland and listed under Part V of the Central Bank Act, 1997, as amended by the Central Bank and Financial Services Authority of Ireland Act 2004, to carry out retail credit firm and home reversion firm business.

a) Definitions

(1) Loan Model ERS

Lifetime Mortgages are provided by credit institutions (e.g. banks and building societies) and retail credit firms. Lifetime mortgages are not defined in legislation but are defined in the Irish Financial Regulator's statutory Consumer Protection Code, which applies to the activities of entities in Ireland regulated by the Irish Financial Regulator, including home reversion firms and retail credit firms. ‘Lifetime mortgage’ is defined as a loan secured on a borrower's home where:

a) interest payments are rolled up on top of the capital throughout the term of the loan;

b) the loan is repaid from the proceeds of the sale of the property; and

c) the borrower retains ownership of their home whilst living in it.

(2) Sale Model ERS

Home reversion agreements are sold by home reversion firms and both concepts are now defined in legislation. Section 28 of the Central Bank Act 1997 as amended by the Markets in Financial Instruments Miscellaneous Provisions Act 2007 contains the following definitions.

A ‘home reversion agreement’ means an agreement between a vendor and a home reversion firm that provides:

• for the conveyance by the vendor to the home reversion firm of an estate or interest in land (which includes the principal residence of the vendor or of the vendor's dependants) for a discounted sum or an income (or both), and

• for the vendor to retain the right to live in the residence until the occurrence of one or more events specified in the agreement,

A ‘home reversion firm’ means a person carrying on a business of entering into home reversion agreements.

b) Authorisation

The Central Bank Act 1997 also sets out a definition of ‘retail credit firm’ as:

"a person prescribed for the purposes of paragraph (g) of the definition of "credit institution" in section 3 of the Consumer Credit Act 1995, or any other person who holds itself out as carrying on a business of, and whose business consists wholly or partly of, providing credit directly to relevant persons, but does not include - a) a person who is a regulated financial service provider, b) a person who is an authorised credit intermediary under Part XI of the Consumer Credit Act 1995, or c) in relation to credit that was originally provided by another person, a person to whom all or any part of that other person's interest in the credit is directly or indirectly assigned or otherwise disposed of, or d) a person who provides credit on a once only or occasional basis, but only if the provision of the credit does not involve a representation, or create an impression (whether in advertising, marketing or otherwise), that the credit would be offered to
other persons on the same or substantially similar terms, or e) a person who is exempted, or who belongs to a class or persons that is exempted, under S29A of being required to hold an authorisation as a retail credit firm."169

This legislation only came into effect in February 2008, so it is too early to comment on whether it will make any difference to the broader position.

Bodies involved in the sale of equity release must be authorised under the Central Bank Act, 1997, as amended, to carry out business as a credit institution, retail credit firm and/or home reversion firm. As of end November 2008, only two home reversion firms and four retail credit firms are shown as registered on the website of the Financial Regulator.170 However, a number of banks and building societies are also involved in the sale of ERS.

c) Marketing

The Financial Regulator’s amended Consumer Protection Code contains specific provisions concerning marketing of equity release products. In particular, it requires that a regulated entity must advise the consumer of the consequences of equity release products including details of the total costs involved, including all interest, charges and the effect on the existing mortgage, if any. It must also ensure that consumers are made aware of the importance of seeking independent legal advice and include a warning on any information document, application form or any other document given to the consumer in connection with an equity release product that purchasing this product may negatively impact on one’s ability to fund future needs. In addition, any advertisement for an equity release product must contain the same warning.

The Regulator also requires ‘minimum competency requirements’ of firms involved in the sale of equity release products.171

d) Taxation and welfare issues

Information about the taxation implications of ERS is not readily available on the website of the Revenue Commissioners (nor the Financial Regulator or other public agencies). However, the position would appear to be that the following. In the case of a home reversion agreement, any money received is tax free, providing the property involved is the person’s principal private residence. If not, capital gains tax may apply. Income tax should not apply as any money received is capital. With the lifetime mortgage as the money is being borrowed, no capital gains tax should apply.

However, money received under either form of ERS would appear to be potentially taken into account for the purposes of entitlement to a means-tested State pension.172 In Ireland, many persons (particularly older persons and formerly self-employed persons) would not have an entitlement to a contributory pension and would be subject to a means test.

169 This quote is based on a 2007 amendment which is not available in the on-line version of the Central Bank Act 1997 which is not yet amended: http://www.irishstatutebook.ie/1997/en/act/pub/0008/print.html.
170 The latest up to date list of ‘Retail Credit Firms and Home Reversion Firms Authorised in the State’ is located on p.3 of the ‘Regulated firms’ subsection of the regulator’s website: http://www.financialregulator.ie/.
172 Guidelines on the website of the relevant agency state that: ‘If you sell all or part of your home to a financial institution or to another party, e.g. under an equity release agreement, and you are permitted as part of this arrangement to continue to reside in your home, the amount you receive from this sale will be fully taken into account in calculating your means for pension purposes.’
Public health care entitlements for those up to 70 are also subject to a means-test. Persons over 70 currently receive full public health care without a means test but the government has recently proposed to reintroduce means-testing for such persons.

Thus using equity release could have serious implications for persons who require means-tested welfare or health care.

e) Subsidies

There is no promotion of or subsidies for equity release (other than general mortgage interest relief if applicable). As outlined in the preceding paragraphs, several government policies in the welfare area would have the effect of penalising the use of equity release.

For completeness, it should be mentioned that the government has recently announced a type of public ‘equity release’ scheme for nursing home care whereby such care will be provided by the public system subject to contributions based on a person’s income and 5% of any savings in excess of the asset disregard per annum.173 If the assets include land and property, the 5% contribution based on such assets can be deferred (deferred contribution). This means it does not have to be paid during a person’s lifetime and may be collected from their estate. In the case of the principal residence only, the deferred contribution will be capped at 15%, i.e. after three years of care a person will not be liable for any further deferred contribution based on their main residence. The legislation concerned has been published, but it is not known when it may come into force.

5. Reasons for lack of further development of the markets

a) Legal barriers

The main barriers in relation to the development of the Irish equity release market do not arise from legal barriers imposed in legislation (or indeed the lack of a legal framework), but rather by contractual barriers imposed by companies. Unfortunately, due to no quantitative data being available, it is currently difficult to say how prevalent the different practices are as outlined below.

The Law Society of Ireland (the governing and regulatory body of the solicitors’ profession) has been extremely critical of equity release products and, in a number of cases, has told solicitors not to be involved with specific products. It currently advises Solicitors ‘to exercise extreme caution when advising clients with regard to ERS’ However, the Society’s objections have tended to relate to specific aspects of the schemes involved and not to the overall legal framework (or lack thereof). For example, a submission from the Law Society174 raised a number of issues including:

The obligation on a borrower to make a will as a condition of the loan175. The Society argued that this was not necessary or reasonable and is, accordingly, an unjustifiable intrusion into the private affairs of the borrower. Neither is it possible to know with certainty whether or not a will has been revoked at any time by making a further will or otherwise.

173 The Irish Department of Health argues that it is not equity release stating that ‘there will be no need for people to draw down value in their house during their lifetimes’ (although this would appear to be precisely what people will be doing).

174 Proposed Regulation of Home Reversions and Lifetime Mortgages, 2007. Note that these requirements vary from scheme to scheme and do not apply to all.

175 As mentioned in the previous paragraph, these obligations are contractual barriers rather than legal ones.
The requirement that the executor of a will sign a form, as a condition of the loan being granted, undertaking to co-operate with the lender on the death of the borrower. The Society stated that “In reality, an executor cannot undertake to do anything other than to administer the estate in accordance with law. If this means bringing an action against the bank in the interest of the estate, the executor is obliged to do so regardless of what undertaking he or she has signed. In the ordinary course of events, the executor will be obliged to discharge the lawful debts of the deceased, and this applies whether or not he or she has signed an undertaking to co-operate with the bank...”.

The requirement that a borrower agrees that the lender may discuss the borrower’s affairs with his or her executors and beneficiaries during the borrower’s lifetime. The Society states: “The borrower should not be subjected to the possibility that his or her affairs will be discussed with an executor or with a beneficiary during the lifetime of the borrower. By definition, neither an executor nor a beneficiary can claim to be such until the death of the borrower, and the borrower at all times will wish to retain the right to change the name of either an executor or a beneficiary without making them aware that they had been originally nominated. Any assurance that discussions will not be held with the executor or the beneficiary unless it is considered by the bank to be necessary is of no comfort to the borrower. The bank will clearly put its own interests first, as it has amply demonstrated. The borrower should not be obliged to give a blanket consent in advance to any matter.”

The requirement of the homeowner to maintain and repair the house. The submission pointed out that the homeowner is “solely liable for the cost of doing so, but if the house is sold, the proceeds are apportioned in accordance with the interests of the co-owners - the homeowner and the home reversion company”. It stated that “While it may be considered reasonable for the homeowner who occupies the house to be liable for day-to-day maintenance and decoration, the homeowner should not be solely liable for structural repairs (such as a new roof), the cost of which should be shared proportionately by the co-owners.”

A requirement in the one home reversion contract for a surviving spouse who remarries to notify the company before his or her new spouse moves into the home. If there are some instances where a homeowner who remarries may not be allowed to bring his or her new spouse into the house of which a company is part-owner, the submission argued that “the question arises as to whether this is contrary to public policy regarding the position of marriage in the [Irish] constitution”.

Thus rather than the potential legal barriers identified in the study questionnaire, the legal barriers identified in practice have related to the specific terms imposed by companies in the market.

b) Cultural barriers

First, there are cultural barriers in that Irish people, as shown by the rather high home ownership rate, are attached to their property and generally wish to be able to pass it on to their children, something which is obviously may be called into question by the use of equity release. More generally, equity release is a victim of its unsuccess in that people are not familiar with it and therefore do not wish to ‘experiment’ with the option.

176 The quotes in this section are from the document Proposed Regulation of Home Reversions and Lifetime Mortgages, 2007 which is available only under the member’s area of the Law Society of Ireland under http://www.lawsociety.ie. A summary of the document is however available in the Law Society Gazette, their house journal from March 2007: http://www.money-advice.net/media.php?id=3268.

177 These comments are based on the personal experience of the expert in this area.
Second, the general tone of comments from public bodies such as the Financial Regulator, the Law Society, and financial commentators is quite critical and suggests that the products currently on offer are not particularly good value for money. Although, it is difficult to establish this from a financial perspective, there is certainly a perception that equity release is not necessarily a good option for many older persons.

Third, as outlined above, there is a lack of co-ordinated government support for equity release and in many cases, equity release would simply not be an option for persons as availing of equity release could lead to a loss of welfare benefits and (if means-testing of health care for older people is re-introduced) to the loss of public health care entitlements.

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179 The Society, for example, stated that equity release schemes should be used only as a last resort where, for example, the need for money is compelling and there is no other financial option open to the house owner.

180 See Section 4.d) on the legal situation in Ireland (on p.54).
Group 2: Member States with less developed Loan Model ERS markets

IV. France

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>France</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>56.5</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>11.9</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>21.8</td>
<td>20.6</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>651.1</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>12.7</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>34.9</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>10170</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>63.1</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>50.1</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>1870</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>61.9</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>11.5</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>25.3</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>16.5</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>ERS Market?</td>
<td></td>
<td>Loan Model less developed</td>
</tr>
</tbody>
</table>

France currently has a population of 61.9 million. This is expected to rise to 69 million by 2035, helped largely by a birth rate that is higher than that of most other EU countries. 16.5% of the population are aged 65+ in 2008 (with 5% over 80), which leaves the country with an old age dependency ratio of 25.3%.

57% of France’s population are homeowners, a figure that has grown with policies encouraging this form of housing status as well as sustained average house price growth of more than 10% p.a. from 2000-2006. The French housing market is a dynamic market with a sizeable shortage of housing supply that has resulted in some pressure on prices. The market has however cooled off in 2008 after several years of strong growth.
72% of French people over the age of 70 are owners of their main residence\textsuperscript{181}. The ratio within this group falls however in higher age groups, but this seems more attributable to a generation effect (one that experienced the absence of long term credit offers\textsuperscript{182} and disincentive owing to the law of 1948\textsuperscript{183}) than to a decision by older people to return to rental status through the sale of their main residence. Although this change in the tenure status only significantly occurs for persons of 80 years of age or more, there is however a more and more frequent reselling of property other than the home of main residence at higher ages. This is something which is especially true concerning secondary residences, and can be explained through financial (e.g. costs are incurred without the property yielding any return) as well as practical reasons (e.g. difficulties in travelling).

Lending for house purchases has been robust and growth in mortgage debt was 14.7% in 2006 resulting in a stock of residential mortgage debt of 32.3% of GDP (or EUR 9 200 per capita) in 2006\textsuperscript{184}. More generally, the French are relatively less indebted compared to other European countries. One factor behind this is a strong fear of overindebtedness\textsuperscript{185}, but another explanation for the relatively low level of mortgage debt is that the French do not practice mortgage equity withdrawal as is prevalent elsewhere in Europe\textsuperscript{186}.

In terms of the situation for state pensions, compared to those countries where voluntary occupational pension plans are well developed (e.g. Ireland, the UK, or even Belgium and Germany), France stands out by having less than 10% covered by private plans. However, despite France having a mandatory gross replacement rate below the OECD average, it has the smallest retirement savings gap of the 11 countries analysed in an OECD study (7.5% versus an average of 18.2%)\textsuperscript{187}. Despite pension reform in past years, the system does however suffer from the length of time over which pension is paid, as France has a normal retirement age of 60 and a life expectancy above the OECD average, which together, increase the required contribution rate compared with countries with normal retirement at 65 or more.

2. Products

a) Loan Model

One product, defined as a \textit{Prêt viager hypothécaire}, has existed in France since June 2007 and goes under the commercial name “Foncier reversimmo” given to it by the Crédit foncier de France. It is a banking product, a Loan Model ERS. The Credit foncier de France, the oldest French mortgage bank, is the sole provider of ERS in France so far. The product is a direct result of recent changes made to the legal framework to purposefully enable the existence of ERS in France. As explained in detail in the legal section\textsuperscript{188}, a ruling in March 2006\textsuperscript{189} reformed the way mortgage guarantees function in

\textsuperscript{181} See INSEE (French official statistics office) at http://www.insee.fr.
\textsuperscript{182} The introduction since end 2007 of a product using a guarantee, called the prêt hypothécaire cautionné, may well change this difficulty as Taffin and Vorms suggest in their 2007 report: http://www.anil.org/fileadmin/ANIL/publications/Etudes/6510.pdf.
\textsuperscript{183} Though the intention of the Law of 1948 was to regulate changes in rental prices, rents of existing housing stock were effectively being frozen in practice. This disincentive to rent out property was later corrected and now no longer constitutes a problem.
\textsuperscript{184} Source for data is the European Mortgage Federation.
\textsuperscript{185} Response from Questionnaire SQ2.
\textsuperscript{186} The wider phenomenon of mortgage equity withdrawal, and the recent legal changes in France surrounding such mechanisms of \textit{extraction hypothécaire} are explained in Section 6 b) below.
\textsuperscript{187} These observations are taken from the part of the OECD report \textit{Pensions at a Glance – 2007} that looked at voluntary private pension provision (i.e. plans not mandatory by employers or individuals). See OECD: \textit{Private Pensions - A growing role, 2007} at http://www.oecd.org/dataoecd/35/17/38717744.pdf.
\textsuperscript{188} The legal situation in France is described in section 5 below, while the EU legal frameworks for Equity Release schemes in general are described in Section E of Part I: General Report.
France, and thus allowed the introduction of the “reverse mortgage”, known as “prêt viager hypothécaire” (translated as lifetime mortgage loan).

As in other countries where similar products exist, Foncier Reversimmo is a loan for older people where the minimum age established by the provider was set at 65 (this is in the absence of a legal minimum age in the articles concerning this product). No repayment is due until the borrower dies. If, as a result of longevity or house price fluctuations, the debt exceeds the value of the property, the loss is not borne by the borrower’s estate but by the bank (or its insurer). This no negative equity guarantee for the consumer is defined by law and is not a product feature which a provider can choose whether or not to include.

The sole existing product disburses the funds released from the loan to the consumer only as a one-off cash lump sum as the product does not offer monthly payments as an option. Though offering regular income payments is allowed, offering a drawdown option is not. This is because offering an open credit line is strictly not possible at the time of writing (something which is expected to change with the law on the modernisation of the economy and its reference to the prêt viager hypothécaire). The product in France has a clear goal of facilitating access to credit for older people and can only be granted to a physical person. This product is to be a loan on a property that has to be used exclusively for residential purposes and must be located in France. Unlike in other countries, the property need not be the main residence of the borrower; it can be a second home or a rental property. The average amount of funds disbursed to a customer through this product is about EUR 90 000. The product is strictly reserved for non-commercial use and it was never sold in combination with an investment product in France.

b) Sale Model

Sale Model ERS do not exist in France. There is no institutionalised commercial activity of the sort to date and the “sell and stay” alternative is exclusively conducted by private individuals. This life annuity agreement between individuals was significantly successful in the past, however, it suffers from its reputation and the number of contracts signed is in continuous decline. This will be referred to again in a further section, but several respondents explained the “vente en viager”, which is a transaction between two physical persons, where an estimated third of these transactions are actually concluded between two members of the same family. One even qualified this private transaction as “the main mechanism to mobilise one’s residential asset whereas the prêt viager hypothécaire has a much harder time with finding its place.” Though this private form of sale and lease back was not investigated by the study, as opposed to the Loan Model ERS characteristics outlined above as they stand today, the transactions do result in a rente viagère or lifetime annuity, which is generally transferred monthly.

In terms of alternative products, alongside these private sale and lease back agreements, secured lending by banks based on the value of collateral does exist as confirmed by the respondent from the main banking association and has been directly encouraged by

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190 For details on this Modernisation law: see http://www.senat.fr/rap/l07-413-1/l07-413-15.html.
191 This is explained by one respondent as due to the lack of State involvement. Because Loan Model ERS in question are free of government intervention and have no social vocation, the State has concentrated itself on securing the product in terms of high consumer protection standards. Without any financial commitments at stake or guarantees from the State, it was not deemed necessary to restrict the use of ERS to only the primary residence.
192 See article L 314-2 of the consumer code.
193 Response from Questionnaire SQ16.
194 Response from Questionnaire SQ35.
recent changes to the law on sureties. Nevertheless, as of end 2008, these legal changes enabling the hypothèque rechargeable have had only little noticeable impact on the supply of these forms of second charge mortgages in France\(^{196}\). In France, although mortgage-based treasury loans are offered by the main French banking networks, these are not widely used and are constructed within a personalised offer (montage personnalisé) without being defined as a ‘product’. Furthermore, jurisprudence from the Cour de Cassation does not allow a lender to extend credits using the value of the good without taking into account the repayment capacity of the client\(^{196}\).

Compared to the prêt viager hypothécaire, the private sale and lease back arrangement contains a confrontation between two physical persons which is very inconvenient in the sense that one has a financial interest in the death of the other. As mentioned in the general section of the report, though these equivalent contracts may provide the customer with a greater sum of money, the occupant does forgo any claim on the future capital gain or appreciation in value of the home he/she no longer owns.\(^{197}\)

### 3. Providers

A provider must be authorised and be registered. Only a bank can distribute Loan Model ERS products. Currently, only one provider does so. It is the Crédit Foncier de France (CFF)\(^{198}\). Regular controls are exerted by the Commission Bancaire which controls French banks in all their activities.

The CFF does 100% of its business through its direct marketing channel in terms of distribution. This direct sales also includes business brought to it through other financial institutions that are part of the CFF’s bank grouping, in this case the groupe Caisse d’Epargne.\(^{199}\)

Although the sole existing provider is said to be “very soft” in the advertising of its product (probably because it does not need to advertise, seeing as demand currently outstrips supply and that no other providers have entered the market), restrictions on advertising of ERS do exist.\(^{200}\)

### 4. Markets

The market is only just one year old but some data is available already. New contracts in 2007 are quoted by one source as totalling 200 with a total value of EUR 20 million (though a second source reported 588 contracts worth EUR 60.7 million). In terms of outstanding credit, this is 199 (implying one has repaid) and EUR 21 million of credit is outstanding. Over one year of activity (from June 2007 to July 2008), 4 400 loans have been authorised, which means EUR 380 million of which 175 million had been disbursed as of July 2008.

\(^{195}\) This new mortgage and its concomitant impossibility of re-evaluation of the surety are discussed below under Section 6.b) on the economic barriers to ERS in France (on p.66).


\(^{197}\) Response from Questionnaire SQ16.

\(^{198}\) There is only one provider as of October 2008. There is a provider that has launched a product with a similar sounding name, the Crédit Immobilier de France with its prêt hypothécaire cautionné however although aimed at seniors, it is a traditional loan but constructed so as not to require the over 60 year old to need to take out an insurance.

\(^{199}\) Response from Questionnaire SQ32.

\(^{200}\) These are described below on p.63 and can be found under art L 314-3 du code de la consommation http://www.legifrance.gouv.fr/affichCode.do;?idSectionTA=LEGISCTA000006161881&cidTexte=LEGITEXT000006069565&dateTexte=20080922.
Though information is currently lacking on the characteristics of the users in France, the provider confirmed that the main reason consumers were turning to their ERS product was due to a problem of cash to cover current household expenditure. The typical user of this product was described by the sole provider as a couple with an average age of 76 at the point of subscription to the credit. According to one source, women are a significantly more frequent clientele, representing 65% of all customers.\textsuperscript{201}

With regards to the importance of the private sale and lease back equivalent to the Loan Model ERS, their number has been estimated at around 4,000 new contracts per year in the whole of France according to professionals (based mainly on statistics in the Paris region, Ile-de-France, which generally averaged 400 p.a. between 1997 and 2003). The limited sample size from housing surveys conducted by INSEE, the statistics office, would suggest that this product and practice has become much less frequent over the last 20 years, while the average age for these ‘customers’ (who are actually the sellers of their home, and not the purchasers) is estimated at 77 years old. There is no official government source for data and statistics on ERS, and excluding certain reports published by different arms of the state such as that of the \textit{Agence National d’Information sur le Logement (ANIL)}\textsuperscript{202}, the only other source for some information would be to consult the land registry or \textit{registre foncier}.

In terms of information on ERS more generally, documentation is low because only one provider has published material on the subject. However, as mentioned reports were done by the government around the time the law was drafted and we are aware that several French banks have undertaken market research studies as well as more technical ones from a more internal point of view.

With 70% of retired 75 year olds currently outright owners of their property, the prospect for development of the market may at first seem very bright. However, compared to other methods of guaranteeing a home loan, the higher cost of the mortgage surety remains a serious deterrent to a strong take-off of the market in France\textsuperscript{203}. Some respondents stressed that the size of the investment required to develop business for a product serving a niche market constitutes an excessive burden to potential providers. One solution suggested by two of the authors of the report that preceded the legal changes enabling the existence of Loan Model ERS, was to use a State guarantee system for homeowners on modest incomes inspired by the set-up in the USA whereby a ceiling on the collateral value of the housing asset is calculated\textsuperscript{204}.

\section*{5. Legal situation}

Supervision by the banking authority, the Commission Bancaire, is the same for Loan Model ERS products as for any other credit. Before commencing their activities, credit institutions must obtain approval from the Credit Institutions and Investment Firms Committee (\textit{agrément du Comité des établissements de crédit et des entreprises d’investissement}).

\textsuperscript{201} Though another source said about 50% are women.


\textsuperscript{203} See Section 6.b) on economic barriers for explanations on the different forms of Home Loans in France (on p.66).

\textsuperscript{204} This suggestion of State involvement is elaborated on in section 6.b) on economic barriers.
a) Advertising

The relevant articles from the code on consumer law referring to this product are articles 314-1 to 314-19. Below are a few of the important details in place to protect the consumer.

Articles L 314-3 and L 314-4 frame the commercial practices concerning the activity of equity release using Loan Model ERS. Article 314-3 provides that all advertising on lifetime mortgages (whether made, received, or perceived), irrespective of its form, has to be true and informative (loyale et informative). This means that the advertisement must mention:

- The identity of the lender, the nature of the operation being offered, its cost and the Annual percentage rate of charge (APR) as sole rate allowed to be displayed, and which is supposed to be calculated for all distinct periods of 5 years, and lastly all fees (perceptions forfaitaires) must be identified.

- The modalities of the term of the offered product. The first two subparagraphs of article L. 314-7 apply. These refer to the ten days cooling off period and subsequent notarial certification; and the rule saying that until the offer has been accepted by the borrower, no payment in any form whatsoever can be undertaken by either the lender or borrower.

When the advertisement is in the written form, no matter the medium, the relevant information to the business (e.g. calculation methods behind the APR, promotional rate if applicable, and time frame over which these rates apply) must be visible with a character size at least as big as the font size used to indicate all other information regarding the financing details, and must be inserted in the main body of the publicity material in question. Forbidden in all advertisements are:

- Mentioning that a loan can be extended without the information that would allow an evaluation of the customer’s financial or wealth situation; and

- Indicating the additional funds obtained from the loan if this same indication is not accompanied by an information describing the modalities of the product characteristics as provided under articles L. 314-13 et L. 314-14. The preliminary credit offer (offre préalable) must be separate from any material or other advertising material.

b) Information and advice

The specific pre-contractual advice or information that has to be provided is given under art L 314-3 du code de la consommation. Especially noteworthy under the framework governing the French market for ERS is the mandatory consultation with a notary. The notary will thus exercise a duty of advice, which the consumer will receive after having benefited from information communicated to him by his banker. Specific measures were introduced into the consumer code to protect the elderly people for whom this product is targeted, and who may sometimes be in position of vulnerability. Among these is a forbidding of doorstep selling. No cold calling or aggressive marketing strategies are thus

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205 In France, an usury ceiling (interest rate cap) applies to credit, the interest rate of which must not exceed more than 30% of the average rate of transactions of the same category or type of credit. The Loan Model ERS (prêt viager hypothécaire) is a separate product and is in a category of its own with regards to calculation of the usury ceiling.


allowed. Article 314-4 of the consumer code stipulates that a lifetime mortgage cannot be sold via door-to-door selling practices. According to articles L 314-3 and L 314-4, the competition authorities, the consumer protection department and the authorities against fraud are empowered to identify any insufficiencies and non-respect of information obligations towards the borrower, which is punishable by fines. If the lender does not comply with the formalities required in the presentation of the credit offer, the judge may impose a partial or total loss of entitlement to interest.

An additional specific measure includes a specific ceiling on the fees imposed in the case of early repayment of the loan and clear guidelines with regards to early termination of the contract. On the one hand, the early repayment charges are clearly defined. On the other hand, if upon the sale of the home the value of the property is less than the total sum of the outstanding debt, this difference will not be transferred to the beneficiaries of the inheritance (and because of the no negative equity guarantee, if the value of the debt exceeds the value of the property, the bank will not be able to claim recourse to additional funds).

c) Restrictions on the use of the mortgage

Several specific provisions restrict certain uses of the lifetime mortgage and confer some important obligations on both parties. Firstly, in terms of the use to which the funds are put, the lifetime mortgage cannot be used to finance a professional activity. Secondly, the use made of the home must remain private and according to article L314-8 of the consumer code, "the borrower must bring to the mortgaged property all the care and attention of a good head of household". As stipulated in article 1188 of the French civil code, the debtor can no longer claim any right to any surplus upon termination of the contract when, from his own action or non-action, he/she has diminished the value of the surety which he gave through the contract to the creditor. The debtor also loses all claims to any surplus value when he/she has either:

- changed the use made of the mortgaged property, typically restricting the use one makes of the housing asset (i.e. must remain residential); or
- refused access to the mortgaged property to the creditor when the creditor wants to control the good state of maintenance and conservation of his surety.

There is thus an obligation of maintenance of the property by the customer.

6. Reasons for undeveloped markets

The legal changes mentioned above have caused the legal barriers that existed only 2 years ago to disappear. As such, the legal impediments for Loan Model ERS no longer exist. The first scheme in France was sold only very recently and the growth in the numbers of schemes sold took off at a much faster rate than had been expected by most observers. Nevertheless, with 4 400 loans authorised by July 2008 and as yet no second entrant to the market, there are several reasons for a slower expected rate of development of the market. These range from providers suffering from competing alternatives to a mortgage loan and strong social scepticism towards ‘uncontrollable’ indebtedness (in the sense that the level of indebtedness is not known from the outset due to the compounding of interest and an undetermined life expectancy).

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208 The maximum compensation for early redemption to the provider is fixed by decree by art. R. 314-2 of the consumer code.
209 In French: "L'emprunteur doit apporter à l'immeuble hypothéqué tous les soins d'un bon père de famille". The term "good father of the family" is an interesting definition which would deserve deeper investigation.
210 Response from Questionnaire SQ32.
211 Response from Questionnaire PQ21.
a) Legal barriers

Contract Law, Bank Law and Housing Law are all relevant to the marketing of this product in France. These texts have recently undergone changes as a result of necessary legal modifications to consumer credit law (loi sur le crédit à la consommation), bank law (code monétaire et financier), and the civil law (code civil). These reforms were implemented in order to enable the Loan Model product to exist and as such no longer represent a barrier.

The main reform was contained in the Ordonnance no 2006-346 of 23 March 2006 relating to Sureties. In this text, the prêt viager hypothécaire was defined as the contract by which a credit institution consents a loan to a physical person, which is guaranteed by a mortgage claim on a property of the borrower which is exclusively used as a place of residence, and the repayment of which can only be demanded when the borrower either dies or leaves the property vacant. The total amount to be repaid is fixed at a ceiling, which is the price of the property at either death or sale of the housing asset. The main obstacle that the reform removed concerned the length of time for which a mortgage registration was valid. Alongside extending the validity of the mortgage, the Ordonnance also relaxed certain rigidities regarding foreclosure on a property (main-levée). The consumer protection measures brought about by the reform are outlined above, and were mainly motivated by the desire to see strong protection rules for the debtor.

Although intermediaries are not involved in the sale of this product so far, the legal requirements any such entity would need to meet before being able to provide the product is to have a recognised status as an IOB (Intermédiaire en Opération de Banque). In France, an intermediary acts by virtue of a power of attorney granted by that institution. The said power of attorney indicates the types of transactions that the intermediary is empowered to carry out, and the conditions applicable thereto.

There is no Tax Law relevant to this product in France. Neither are there codes of conduct or recommendations.

One legal uncertainty that remains in terms of preventing a full development of the market in terms of product offerings of the type that are observed in other more developed markets, is based on consumer protection laws as they currently stand. There is a lack of flexibility in the Loan Model product that is sold in France. This is because it is proposed mainly as a lump sum capital output, i.e. in the shape of a single payment. Though monthly payments are possible, these must be planned from the outset and do not allow for drawdown products where money is received based on need. A reform is however currently being suggested which, if successful, would help providers offer this flexible feature and thus perhaps encourage more competition from new entrants to the market. The Modernisation Law aims to clarify the treatment of compounded interest and will help remove certain legal uncertainties which banks have put forward to explain the ‘wait and see’ approach which potential providers are currently following.

The private sale and lease back arrangements (vente en viager) are governed by contract law (the part of the civil code dealing with aleatory contracts) and are analysed as a classic sale transaction with specific payment modalities attached to it. Although certain real estate agents specialise in the purchase and sale of private sale and lease back transactions as broker between two private parties, as already mentioned, products offering a lifelong annuity payment are not currently sold commercially by corporate entities in France and there is no specific regulation of such activities. These Sale Model

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212 See Section 5 on legal situation (on p.62).

213 Response from Questionnaire SQ40.

214 The Law on Modernisation and suggestions made by the Senate committee are available under: http://www.senat.fr/rap/l07-413-1/l07-413-15.html.
ERS would however nevertheless be regulated by contract law as the legal framework stands.

b) Economic barriers

In France, a large and almost dominant proportion of all home loans (i.e. more than half) are not secured by a personal mortgage claim over the property but by a third party guarantee provided by a specialised institution\textsuperscript{215}. This system is unknown in most other EU countries, and is one where the mortgage is not registered but where instead the provider of a “\textit{caution mutuelle}”\textsuperscript{216} guarantees that in the event of a default there is no priority claim on the property. This guarantee provides an alternative to a mortgage and, as such, constitutes an additional constraint to the development of the market. This is because it narrows down the potential target group of customers for whom granting of a first charge mortgage on their property is something they are comfortable or familiar with. A prerequisite for a Loan Model ERS is the more a homeowner (outright or not) is likely to envisage an external claim by way of a mortgage surety, the greater the chances he/she will do so again in old age once the process of acquiring 100% equity has been completed. In France, arguments in favour of this guarantee system include a lower cost than a mortgage, encouraging voluntary settlement with the borrower in the event of default, providing banks with a second opinion on the credit risk, and allowing outsourcing of recovery process in the event of default. A more simple administrative procedure (shorter and more straightforward) also means that the guarantee has a competitive advantage.

A significant barrier to equity release products for consumers is the cost. This may be to some part attributable to the fact that the sole lifetime mortgage product being offered is still in an experimental phase, because of which costs (placement fees) are high and correspondingly the proposed loan to value ratio, i.e. the ratio between the loan amount and the housing value, is very low (34% at 75 years). This may be due to a very cautious calculation from the provider, which may or may not be excessive considering all the risks which are contained in supplying such a product.\textsuperscript{217} The cost of this product, as measured by the ratio of interest payments to the value of the property, is nevertheless dissuasive, and although the sole provider in France is breaking new ground for others to follow, the lack of competition to date is definitely one reason for such high costs. Because only one provider exists since 2007, volumes of sales of Loan Model ERS are still very low. There is a clear interest on the part of consumers for this product but both the level of interest rates and the actual sum of money that can be released have disappointed potential consumers to date. This however, is seen as necessary to cover the longevity risk and complexity of the product generally\textsuperscript{218}. The consumers may have been a little harsh in judging this product because in fact, the loan-to-value ratios currently offered are close to those offered in other countries, but with the additional advantage from the consumer's perspective, that products sold in France have enhanced consumer protection features than some of the products found elsewhere in Europe.

\textsuperscript{215}This paper from 2002 explains the differences between the French mortgage and the \textit{caution} (defined as a commitment made by a third party in place of the borrower, making him liable for any payment default by the borrower): http://www.anil.org/fileadmin/ANIL/publications/Etudes/3080.pdf.

\textsuperscript{216}A decade ago, mortgage registration was previously almost always required for any housing loan whenever the amount or the duration was significant. But because it was expensive (high cost to register and to lift it) many lenders accepted another form of guarantee called ‘\textit{caution mutuelle}’. In such a system, the risks are mutualised, i.e. the price to pay is higher than a mortgage registration but a large part of it is returned in the end. Of course, participants are strictly scored. The guarantees are provided by two types of organisations: mutual guarantee companies or insurance companies (the biggest player being Crédit Logement). This mutual guarantee should be distinguished from ‘\textit{caution personelle}’, a guarantee brought by a natural person.

\textsuperscript{217}See Part I: General Report section D.III.2.a) for more detail on risks for providers.

\textsuperscript{218}Response from Questionnaire SQ40.
The lack of economies of scale is also a contributing factor to the lack of enthusiasm to date, as well as the fact that the reverse mortgage is seen by banks as a niche product. What may change this significantly in a number of years to come, though still limited by the probable continued relatively low French appetite for indebtedness, is the demographic trend ahead. Like elsewhere, the drivers behind any future emergence of the ERS market in France will be the high homeownership rate, the forecasted growth in persons at pension age (what the French refer to as the "Papy boum") and the rising need to compensate for a less generous state pension in the future associated with a greater financing need for the increasing dependency on costly health and care.

Discussions over the role which the State could play in helping providers enter the market with affordable products are taking place, and revolve around finding ways in which a public entity could assume some of the risks inherent in this Loan Model ERS such as setting up a public insurance mechanism.\(^{219}\) The example of the US structured system has been considered by several agencies in France to help develop the market. Certain structures already exist in France that would make a similar system potentially workable. The State, for example, has through the intermediary of the \textit{Fond de garantie de l'accession sociale à la propriété} (FGAS)\(^ {220}\), the possibility of precisely defining the characteristics of the lifetime mortgage: cap rates, placement fees, flexibility norms, and marketing conditions. In the case of pension output, it should be exempted from tax. One possible outcome would be to have the State guaranteed lifetime mortgage coexist with an absolutely free market offering as it stands today.\(^ {221}\)

The law introduced in 2006 created a regime for lifetime loans that is comparatively favourable for French consumers. This may limit the harm to the reputation of the product market through negative incidences over the long-term, but may cause certain potential providers to take their time in considering the business incentive to offer a product on the market. Some respondents have confirmed that banks are interested in developing these Loan Model products but are not rushing to enter the ERS market just yet. One reason put forward for delaying entry was referred to in the legal section above, namely that legal uncertainties still remain\(^ {222}\). This however, is likely to change following recent policy orientation by the government indicated in its law on modernisation (Loi LME) which could, if the recommendations are followed, significantly improve the chances of growth of the ERS market\(^ {223}\). Other respondents have indicated that in France, providers do not seem particularly interested in developing such an innovative product for the market. One reason for this is that another new product may be more attractive to the banking profession: the rechargeable mortgage.

Significant changes to the legal framework have also allowed a new bigger market to develop. Alongside the reform of mortgages that enabled the ERS Loan Model product to exist, was the changes enabling the creation of the rechargeable mortgage. This, along with the lengthening to 50 years of the maximum duration of mortgages, marked a significant step in the modernising of the mortgage system in France. Under the name of \textit{"hypothèque rechargeable"} (translated as refillable mortgage), this newly created mortgage is aimed at allowing borrowers to tap into the mechanism of mortgage equity withdrawal, which has helped boost consumption in some of its European neighbouring countries. The rechargeable equity release mortgage enables the guarantee already

\(^{219}\) Response from Questionnaire SQ2.

\(^{220}\) Set up in 1992, the FGAS, Fond de garantie de l’accession sociale à la propriété (assisted home-ownership guarantee fund), is similar the Federal Housing Association set up in the USA.

\(^{221}\) This suggested solution could thus resemble the ERS market observed in the USA, where a federally sponsored system dominates but coexists with a limited number of offerings outside that insurance system. The following link to the U.S. Department of Housing and Urban Development (HUD) website gives more detail on the reverse mortgage program run by the Federal Housing Administration (FHA), called the Home Equity Conversion Mortgage (HECM): http://www.hud.gov/offices/hsg/sfh/hecm/hecмhome.cfm.

\(^{222}\) See Section 6.a) on Legal barriers above (on p.65).

\(^{223}\) Response from Questionnaire SQ2. Again, see Section 6.a) on Legal barriers above (on p.65).
taken on the property to be reused for other loans. This is basically a second charge mortgage, however the French legislator has added an extra level of consumer protection by stating that the maximum amount of the mortgage be fixed from the moment the initial mortgage loan is registered.

It is also worth clarifying a general confusion that exists when the two new products are mentioned. Fundamental technical characteristics as well as micro and macro risks differentiate the two products. Repeating the distinction made in the general part of the report, the hypothèque rechargeable is aimed primarily at consumers who are partial homeowners, and whom will face a prolonged length of time indebted as a result of the product. This product can thus lead to excessive indebtedness, whereas the prêt viager hypothécaire does not. This is because it is not intended to be repaid by the borrower.

c) Cultural barriers

As mentioned already, the French are relatively less indebted compared to their European peers. This is especially noticeable when figures on consumer credit are compared. Attitudes to indebtedness for housing purposes are not particularly different but because the nature of the lifetime loan is to accumulate debt to spend rather than to take out debt to acquire an asset, the underlying characteristic of the product is similar to a credit taken out for consumption purposes. This French mistrust of credit is a significant barrier for consumers, and constitutes an unfavourable social attitude towards indebtedness and risk. While some societies such as the US encourage broad access to credit (and fighting against practices such as redlining\(^\text{224}\)), consumer associations in France on the other hand generally call for stricter preventative measures against overindebtedness\(^\text{225}\). The French tradition being relatively paternalistic and often about protecting the consumer from himself. One respondent to the survey undertaken for this study noted however, that in terms of ERS, the equity, or net housing asset, held by the owner in his home, has a vocation to be used. This is totally coherent with the macroeconomic data that tells us that many households in Europe are extracting equity from their homes through a mortgage. The ratio in the table above for outstanding mortgage credit as a % of GDP shows that in that regard France has a lot of ‘catching up’ to do when the figure of 32% is compared with that for other countries like Spain (59%), Ireland (70%), the UK (83%), the Netherlands (98%) or Denmark (100%).

There is considerable stigmatism associated with the status of overindebtedness in France and as a result, people remain conscious of the dangers of excessive indebtedness and how this may affect them socially. Reactions and general negative attitude by the consumer organisations in France\(^\text{226}\) towards this product (a factor which

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\(^{224}\) In the 1960s and 70s, banks in the USA would redline neighbourhoods (i.e. draw a redline enveloping certain neighbourhoods on a map) which meant that for those that lived within the redlined areas, regardless of their income, credit score, assets, debt servicing ability, they could not qualify for a mortgage. This practice was made illegal by the Fair Housing Act of 1968, but because it still surreptitiously continued, the Community Reinvestment Act of 1977 was drawn up to help combat this form of exclusion.

\(^{225}\) Recent examples include the views expressed by UFC Que Choisir and CLCV in response to the law proposed by Senator Marini (see either http://www.credit-responsable.net/index.php?id=1981&viewid=42097 or http://www.conso.net/page/bases.1_actualites.1_inc_hebdo.283_inc_hebdo_n_1497./Item-itm_ccc_admin_20081127122834_122834_Centrelesurendettementune.txt), or those of UNAF, the union representing French families, shared with the Minister of Justice in November 2008 (http://www.unaf.fr/article.php3?id_article=7954). The views of UNAF (p.71) and the preoccupations of the group ConsoFrance (p.188) are also presented in the 2007 report on household overindebtedness by the French social and economic council (‘Surendettement des particuliers’, Conseil Économique et Social, 2007 at: http://www.unaf.fr/article.php3?id_article=7954). The views of UNAF (p.71) and the preoccupations of the group ConsoFrance (p.188) are also presented in the 2007 report on household overindebtedness by the French social and economic council (‘Surendettement des particuliers’, Conseil Économique et Social, 2007 at: http://www.unaf.fr/article.php3?id_article=7954). Furthermore, a report on discussions on overindebtedness between French stakeholders in 2007 and promoted by the European Coalition for Responsible Credit is available on the website of INC, the national consumer institute, under http://www.conso.net/incdoc/1451-cr_colloque_383.pdf.

\(^{226}\) The following press release by consumer organisation UFC Que Choisir serves as an example: not only is the one sided nature of the risk of the ERS (the consumer can lose everything) overstated but the prêt viager hypothécaire is almost always commented on together with the other product enabled by the changes in the
was mentioned by stakeholders as hindering the chances of having this type of product accepted by the public and thus favouring the launching of new products by other banks) testify to this. The lifetime mortgage as sold in France constitutes an opportunity available to older persons already homeowners, and which is completely without any payment default risk whatsoever\footnote{Another example of this aversion is the media reaction to the launching of the \textit{prêt à taux zéro} (0\% loan designed for persons with low income to help them acquire a main residence with no financial cost and even postponement of repayment of principal for up to 18 years).}. Again, the popularity of the home loan guarantees which are specific to the French market can be used to suggest this aversion of the French towards having a third party with a claim on their home. These guarantees are precisely preferred because they overcome the distrust felt by French people towards mortgages, which they see as a restriction of their ownership.

It is also difficult to quantify any exceptional French characteristics with regards to socio-economic preferences with regards to attitudes towards leaving an inheritance, importance of family traditions, or even trends with regards to family structures etc.

With regards to the private equivalent version of Sale Model ERS, though the old “viager” system has existed for a long time, the moral dimension of the transaction whereby a buyer bets on the seller’s early death has meant that it has lost considerable appeal over the years. This incidentally, is something that can be avoided should the transaction be carried by a business instead of an individual. French mentalities are generally aware of the sale and lease back concept but media reporting on extreme cases will have served as a warning for prospective home reversion providers. The famous case of Jeanne Calment, a French woman who lived to 121 years of age and survived her buyer is now world famous. Though these occurrences are extremely rare, the added fact that she also smoked a pack of cigarettes a day, reinforces the unpredictability and uncertainty which potential providers of this Sale Model product have to deal with.

7. Risks and benefits

a) For providers

When asked for what benefits they could see for providers expecting from entering this niche market, French stakeholders (provider associations, consumers, and regulators) agreed that a high profit was the most important motivator in their eyes. Only two other factors were mentioned as being equally important, namely the aim of increasing market share in the mortgage loan market generally, and (according to one industry participant) the reputation of being a bank that serves the full spectrum of the population (though admittedly, the counteracting risk of a negative incident harming the firm’s image may outweigh this benefit).

Property valuation risk was judged to be of greatest concern by providers of ERS, followed by the high risk factor associated with longevity risk and reputational risk. Neither interest rate risk nor the risk of facing difficulties in the maturity mismatch were seen as important issues. The potentially damaging effects of moral hazard whilst acknowledged by the sole provider as a risk factor, were not deemed to be particularly significant generally.

b) For consumers

The provider response to the survey also highlighted that benefits to the consumer were of average importance in terms of tax efficiency or in terms of helping them to become
independent from other family members. However, above all, providers viewed the lifetime right to stay as conferring the main benefit of the product, even above the benefits associated with providing the consumer with more liquid funds.

As mentioned, mandatory legal advice is a benefit to consumers in the sense that it will ensure that at least one entity is involved in the process to judge the suitability or not of the product. It is thus important for the notarial profession to be well informed and well able to pass judgement on the respective merits of different alternatives open to the consumer. Independent financial advice on the other hand is not guaranteed to French consumers under the existing system. Other than a consultation with a legal advisor in the form of a notary being compulsory by the client, the only other source of advice or information on the product is the general media as well as some more specific publishing companies aimed at seniors. The agencies for housing (agences départementales d’information sur le logement) and wealth management companies may also be of assistance on the subject.

An additional benefit is the lack of controls in place over the use a consumer makes of the money received, except that it cannot be spent on professional use (i.e. a business).

With regards to the disadvantages of equity release products, our research has identified some areas for improvement for the consumer. Firstly, the only provider, Credit Foncier, has been overwhelmed with requests for their new product and appears cautious about taking on too many new customers too quickly. There is also evidence to suggest that applicants have been disappointed with the actual amount of funds they are able to release. Another disadvantage for consumers is that the Loan Model schemes are relatively expensive because they require an appraisal of the property, an insurance against fire and damages by the provider, and detailed information of the borrower and his future heirs.

Regulation of the product in France does not contain any special provisions with regards to inheritors being included into the sales or advice procedure. They may perhaps be informed by the senior consumer himself (e.g. most often in the case of a couple vis-à-vis their children) but there is no obligation to do so. This is however not the case, when the heirs are full owners of the property without any other claim (nus propriétaires), in which case the elderly consumer will be obliged to get the agreement of the owners (often the case for widows and their children).

No special complaints procedure has been set up to deal with any problems with Loan Model products specifically and the same procedures apply as with any loan.

One area worth mentioning is the acknowledged need to fund the costs of dependency. In France, attention has been brought on to the issue of old age funding requirements. The Gisserot report puts at 1% the annual average growth rate of the number of dependent senior citizens up to 2040, mainly through two accelerations, corresponding to the baby-booms which followed both world wars, between 2005 and 2020 then between

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228 Advice could be given by ANIL (national housing information board), but as mentioned, information is in fact given by the lender and by the notary. See provider source under: http://www.creditfoncier.fr/editorial/Pret_Viager_Hypothecaire/pret_viager_hypothecaire.htm.

229 Response from Questionnaire SQ40.

230 This opinion is based on anecdotal evidence and blog websites, rather than from the provider himself.

231 This may however be more related to unfulfilled expectations in this regard because the size of the funds released in terms of Loan to Value ratios do not seem too different to those ratios offered by providers in other countries such as even the UK (see general section of the report).

232 Response from Questionnaire PQ9.

233 Financial perspectives of the dependency of senior citizens by 2025: forecasts and choice margins, report to Mr. Philippe Bas, Minister for social security, senior citizens, the handicapped and family affairs.
2030 and 2040. Based on projections by the Direction de la recherche, des études, de l'évaluation et des statistiques (DREES) at the Ministry for Health and Solidarity, the number of dependent senior citizens will touch the 1.2 million mark by 2040 (a number to be treated with caution because of the uncertainties with the very old and dementia etc..), and correspondingly, the scenario retained by the public authorities within the framework of the Old Age Solidarity Scheme makes a particular provision for the promotion of home care and increased expenditures on staff which this implies (i.e. 85% of the additional costs).234

Dependency related expenditures are of different types: Works on adaptation of housing (usually one-off), and services to individuals (which will involve recurring expenses that will increase with the degree of dependency, or housing in an institution). In France, there would seem to be a trend towards a situation where expectation of people and community interest combine to favour maintenance at home.235 Other than State health insurance, the funding of dependency in France comes from three types of sources: public finances (in the shape of APA/Personalized Allowance for Autonomy, CNSA/national solidarity fund for autonomy, and tax aids); private insurance; or the household itself. The State funding of the schemes is problematic because they have a low level of redistribution (with higher income groups potentially benefiting when they less need it). APA is paid by the Département to a million dependent senior citizens, at an annual cost of about EUR 4 billion (the average APA cover is EUR 400 which leaves a large additional funding gap when one considers the average cost of dependency is estimated at EUR 1 400 per month.236


235 ANAH funds 70% of the works related to accessibility and adaptation of houses and buildings up to a limit of EUR 8 000 for owner-occupants whose resources are lesser than the upper limits said to be grossed up (for example EUR 21 022 of reference fiscal revenue in Ile-de-France and EUR 16 795 in the provinces for a single person). The funding circuits for dependency, services to individuals or housing in institutions, are complex in nature. Health insurance accounts for more than 60% of the total of the expenses, which is a clear pointer to the fact that efforts at clarifying the boundaries between health insurance and dependency are necessary in order to bring out what is known as the "fifth pillar" of social protection.

236 More detail is available on the ANIL website at www.anil.org.
V. Hungary

1. General information

<table>
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<tr>
<th>Category</th>
<th>Hungary</th>
<th>EU Median</th>
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<tr>
<td>Owner occupation (% of households, latest)</td>
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<td>75.0</td>
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<td>House prices (average annual % change 2003-2007)</td>
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<td>Number of transactions per 1000 homeowner (2007)</td>
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<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
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<td>Growth in mortgage debt (% 2007)</td>
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<td>Residential mortgage debt (% of GDP, 2007)</td>
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<td>Per Capita Mortgage debt (EUR)</td>
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<td>Net replacement rates on mandatory pension programmes (%)</td>
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<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
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<td>Old age dependency ratio (% 2008)</td>
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<td>65+ (% of total population)</td>
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<td>ERS Market?</td>
<td>Loan &amp; Sale Model less developed</td>
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</table>

Hungary has a relatively high ownership rate. This is however combined with a relatively low mortgage penetration. Seniors are not considered bankable, therefore they have to look for alternative ways to obtain liquidity. In Hungary, a life annuity contract is a legal basis for exchange of ownership, even if no funds are transferred.

But there is also a noticeable and widespread need for funds during retirement, as most pensioners’ monthly income does not reach the average income level of the adult population and more than 25% live on income equal to or less than minimum wage. Furthermore, there is a high proportion of mortgage-free homeownership (it is estimated that 90% of properties owned by pensioners are unencumbered by mortgages).

237 See EMF Mortgage Info No. 2 February, 2008, p.3.
Furthermore, mobility in Hungary is low, and the typical pensioner in Hungary has lived several decades in their own homes and wants to continue living the rest of their life in their own homes.

### 2. Markets and products

In Hungary, there are currently both types of ERS. These have been specifically developed for elderly consumers. The most recent of the products is a reverse mortgage or Loan Model type, and was only introduced into the market a year ago. The commercial (product) names of the two types are as follows:

- **Loan Model ERS:** Old-age mortgage annuity (Időskori jelzálog járadék);
- **Sale Model ERS:** eternal annuity (Örökjáradék) or, originated and based on a traditional private contract explicitly named and regulated in the Hungarian Civil Code, lifetime annuity (életjáradék).

Hungary is a country that already has a number of ERS for elderly consumers. In Hungary, the existence of these products is no surprise given the factors specific to the country, such as high unencumbered home ownership by the elderly and low pension income. An additional reason supporting the past development of ERS in Hungary is that these schemes are presently the sole option available to homeowners for extracting equity for purposes other than buying or repairing owner-occupied homes. Mortgage-based sureties as they are known elsewhere in the EU and the appearance of second charge mortgage claims, will, however, undoubtedly emerge soon, as they have done in other EU accession countries, enabling older people, and others, to access the equity in their home by means other than ERS, selling the property or moving, as is currently the case.

On signature of a Loan Model ERS contract (reverse mortgage contract), the credit institution assumes the obligation to disburse the loan and to register the mortgage and its priority interest with the land registry. As with certain other ERS, the original borrowers are not liable for repaying the loan. The characteristics of the Loan Model product on the market include flexibility in disbursement of the funds as either a single lump sum or in equal monthly instalments, and in whether the payments should start immediately, or at a later date where lump sum of a minimum of HUF 1 million (approx. EUR 4 300) is also paid. The maximum amount of the lump sum is determined by the lender on the basis of the expected market value of the property and other criteria, which means that the borrower can choose the amount of the lump sum between a given maximum and minimum. The level of monthly instalments will be dependent on the size of the lump sum and the output from internal calculations, taking account of factors such as those outlined in the general section of this report.

Because the Loan Model ERS are designed specifically so that the borrowers are not liable to make repayments in their lifetime, the duration of these loans is not predetermined as it sometimes is for schemes sold in other EU markets. The loan terminates exactly one year after the death of all borrowers who were party to the contract, at which point the repayment of the loan in full falls due. Methods for repayment can vary; three alternatives are offered to the heirs named in the certificate of inheritance. They may repay the full amount in one lump sum, they may enter into a new loan agreement subject to agreed instalments and term, or they may sell the property themselves and repay the loan from the proceeds of sale. Where the heirs fail to cooperate in repaying the loan, the bank may exercise its rights under the mortgage to force a sale and recover the amount due from the proceeds.

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238 As reported by the Hungarian financial authorities and one of the leading providers of ERS on the Hungarian market.
The home reversion type products (Sale Model ERS) available in Hungary are referred to as ‘life annuity programs’, which involve purchase of an annuity in exchange for ownership of the customer’s home. Three companies currently offer this type of product, which was first introduced to the market in 2005, and sales have been showing rapid growth recently. By the end of 2007, an estimated total of 3 000 contracts had been signed. As with similar products elsewhere, the originator assumes the obligation to pay an annuity, as well as ensuring that both the lifelong right of occupation of the property (an ‘annuity right’) and its own priority rights are registered at the land registry. On conclusion of the contract, ownership of the property is transferred to the lender, but the consumer retains security in terms of rights of occupation.

The customer may choose whether to receive a single lump sum or monthly annuity payments; the lump sum is usually capped at a maximum of 33 % of sale value of the property; the monthly payments (which may be either fixed or variable) are based on the amount of the lump sum. Where fixed monthly payments are made, the monthly payment is revised annually based on the average annual consumer price index published by the Hungarian Central Statistical Office. Under the variable monthly payment option, the sum starts off lower than for the fixed option but increases annually. A specific feature of this type of ERS is that the annuity contract terminates only on the death of the borrowers. By definition, therefore, the contract cannot be terminated while the customer is alive.

3. Providers

OTP Eletjaradek is one of three providers. It offers two products, both of which are Sale Model ERS. The first has the title transferred at the signature of the contract. Furthermore, up to 45 % of advance is paid to the customer, they have usufruct right239 to the real estate for life (can also continue to occupy the real estate), and an indexed monthly annuity is paid. The second offer is one where the customer over 70 can pick an inheritance version. In this, a purchase and sale agreement is signed, client gets usufruct right. Depending on age, receives 40-45 or 50 % of real estate value and receives an additional 20-15-10 % over a predetermined number of years (depending on age). The rationale is that if client passes away before predetermined period is up, the unpaid sums will be paid to heirs. This can be done because it is a purchase and sale agreement, not an annuity contract. The other Sale Model product is offered by HILD, which is a life annuity. Upon signing of the contract, consumers receive an initial large lump sum payment coupled with lifelong monthly annuity payments. The consumer shall pay for the costs including maintenance and real estate insurance as set out in the contract in order to ensure protection of value of the real estate (serving as a collateral).

FHB Life Annuity Ltd is the sole provider (originator) offering a Loan Model ERS to date.

4. Legal situation

In terms of regulation of the ERS market in Hungary, there is no legal definition or product name for ERS in general in Hungarian law. There is also no special law for ERS in Hungarian law. Loan and Sale Model ERS are regulated under the Civil Code. In terms of supervision, whereas Loan Model products are regarded as the professional provision of loans, so that the provider and the product, as a financial service, are subject to the supervision of the Financial Supervisory Authority, Sale Model products on the contrary, are not subject to supervision.

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239 Usufruct is the legal right to use and derive profit or benefit from property that belongs to another person, as long as the property is not damaged (as opposed to legal land ownership). The English word derives from the Latin roots *usus* and *fructus*, referring to the rights of use and fruit, respectively.
The closest legal institution for Sale Model ERS is the lifetime annuity contract (életjáradéki szerződés), but on a private rather than on a professional basis, its definition can be found in Section 591 (1) Act IV of 1959 on Civil Code. According to the Civil Code, under a life-annuity contract, one of the parties shall be obliged to provide a specific sum of money - against a consideration not defined by law. The consideration may thus be (and usually is) the title of a real property. If the beneficiary transfers title of his real property to the provider in exchange for annuity support, the right of support can be (and usually is) registered in the land registry (right in rem). Even legal persons shall be entitled, as obligors, to conclude such contracts.

Regarding Loan Model products, the legal definition would be a loan agreement (see Sections 523-528 of the Civil Code) backed with a mortgage according to Sections 261-265).

There is no barrier in terms of the product payouts from Loan Model ERS being treated as income. This is because they are clearly treated as loans. Because these payments are not qualified as income, a Loan Model ERS is not subject to income tax (i.e. the product is tax neutral). For the heirs of those customers choosing the Loan Model, there may be even a tax advantage if the real property is not inherited as free-of-encumbrances, but encumbered with a mortgage. Further inheritance tax advantages may arise if the mortgage is not cleared by the heirs but they agree a sale of the real property with the bank.

However, regarding the Sale Model ERS, the selling of the real property results in income. As a general rule, the income itself is not taxable, but the profit is. There is a tax incentive regarding the taxation of profit based on the years between the acquisition and the sale (after 5 years, no profit is taxable). See Section 62 (1) and (6) of Act CLV of 1997 on Income Tax. – All this information is however rather of a theoretical nature, as the sale under an ERS scheme will definitely not result in a higher price at sale than the acquisition price.

According to Section 3 (1) and (3) of Act No. CXVII of 1996 on Credit Institutions and Financial Enterprises, the provider of a Loan Model ERS has to obtain a licence from the Hungarian Financial Supervisory Authority (PSzÁF) as a credit institution.

According to our knowledge, no licence or registration is required for the Sale Model. This is however a political issue (see joint statement of Financial Supervisory Authority and Ombudsman for Citizens’ Rights dated 26th April 2006)240 according to which there is a need for legal regulation of Sale Model products, as the present contracts cannot be clearly identified as life annuity contract or insurance contracts. There were even serious preparations to pass an act on ERS providers and products in early 2007, but from our understanding as of November 2008, the legislation project appears to have drained away, so for the time being merely a draft241 of the act prepared by the Ministry of Finance exists. To our knowledge, such a legislation project is not on the government’s short-term agenda.

5. Legal barriers

Although the two forms of ERS exist in Hungary, there are still certain foreseeable barriers which affect the products.

For Loan Model products, the sale after death (if heirs do not / cannot pay back the loans given) under the mortgage may be time and/or cost intensive, as the mortgagor has

quite a number of protection rights (information rights; bank’s obligations regarding the arrangement of an auction in order to achieve a relatively high price etc.\textsuperscript{242}

Sale Model contracts may be challenged by heirs on legal grounds of “\textit{disproportion on service and its consideration}” (in case of early death).\textsuperscript{243}

Anatocism is explicitly allowed\textsuperscript{244}, ever since the Hungarian Constitutional Court decided in 1993 that in relation to the permissibility of anatocism the distinction in the Civil Code between private persons and legal persons as lenders is unconstitutional, thus abolishing such normative distinction.

Despite no legal barriers preventing the offering ERS, cost increasing barriers do exist. For Loan Model products, there are the above cited mortgagee’s rights in case of sale of real property due to lack of agreement between bank and heirs. For Sale Model products, the land registry entries often make the real property in question useless for serving as a security (shared titles for all apartments in one house, entries regarding owners or size are not up-to-date or not accurate etc.).

According to Section 292 (2) of the Civil Code, prepayment is always possible for both Loan and Sale Models and no interest is payable for the respective subsequent period. (\textit{The obligee shall also accept performance that is provided before the deadline or prior to the initial date of the performance period; in such cases, no interest or compensation is due for the period between performance and the deadline. Any agreement between the parties concerning interest or compensation, as they are not permitted by law, shall be null and void; invalidity shall not affect other provisions of the contract.}) However, to the knowledge of iff and its expert on Hungarian Law, this legal restriction has been overcome by the bank, e.g. by imposing so-called ‘break costs’ on the debtor, i.e. payment of the bank’s additional costs arising from the obligatory refinancing of the outstanding part of loan the repayment of which was expected for a later date.

It is obligatory to maintain an insurance for the real estate against usual damages affecting the usability and the value of the real property (most commonly: bursting of gas or water pipes, flooding of walls or ceiling due to the neighbour’s water damage). The insurance is usually offered by the provider, but could also be obtained by shopping around.\textsuperscript{245}

The contracts have to be filed with the land registry (Loan Model: mortgage and prohibition of sale and encumbrance; Sale Model: sale and purchase agreement) may be countersigned and filed by an attorney-at-law, however, the providers also require the participation of a notary public (due to the possibility of direct enforceability of such so-called ‘public document’).

The mortgagee has the obligation imposed on him by law to maintain the object and its value. In case of the decrease in value, the mortgagee must, lacking other remedies, offer another mortgage.


\textsuperscript{243} See Section 201 (2) of Civil Code.

\textsuperscript{244} See Section 232 (1) of Act IV of 1959 and the correspondent ruling of the Constitutional Court No. 61/1993 (XI. 29.).

\textsuperscript{245} The Hungarian expert responded to the question whether it is obligatory to buy the insurance with the provider: “I am not aware of the business practice of the providers. There is a legal requirement neither for offering/accepting such auxiliary insurance service from the same provider nor for allowing shopping around by the provider. At usual mortgage backed bank loans, the lender has to obtain the insurance product linked to the loan by the provider (but usually offered not by the bank itself but by a cooperation insurance partner).”

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Loan Model mortgages may be (and usually are) backed with a ‘prohibition of encumbrance and sale’ registered at the Land Registry together with the mortgage itself.

Mortgages for future debt are explicitly possible\(^{246}\).

As the loan is to be used freely, no tax incentives or tax exemptions exist. However, regarding Loan Model ERS there may be a tax advantage for the heirs since it may not be subject to income tax.

In case of bankruptcy with Sale Model ERS, the debtor may file his claim at the liquidator, with the claim belonging to a preferable category (private persons’ claim)\(^{247}\).

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\(^{246}\) See Section 251 (2) of the Civil Code: “Liens may also be created for securing future or conditional claims.”

VI. Italy

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Italy</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>80.0</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>8.0</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>18.3</td>
<td>20.6</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>304.2</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>10.2</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>19.8</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>5130</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>77.9</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>67.7</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>773</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>59.5</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>4.1</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>30.5</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>20.1</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>ERS Market?</td>
<td>Loan Model less developed</td>
<td></td>
</tr>
</tbody>
</table>

With high ownership rates among the elderly (more than 90%), there is very low mobility and a lack of financial instruments designed for people over 65 years of age. Reverse mortgages are used for:

- helping sons and daughters (i.e. in the form of heritage advances to help them purchase their home following marriage. Help in case of financial difficulties, often to restructure the debt of sons and daughters)
- restructuring of debt of the elder being financed (as opposed to the restructuring of the debt of the heir of the elder as in point 1. above), utilizing the reverse mortgage to eliminate the burden of the monthly instalments on their existing debts.
- liquidity (to finance extraordinary expenses such as: a) medical expenses; b) home caring (for the disabled); c) extraordinary tax items; d) extraordinary expenses related to the property maintenance; e) increase in disposable income (reinvesting the proceeds from the reverse mortgage and utilizing it over time for day by day expenses); f) other (luxury items such as travelling and leisure)).
2. Products

In Italy, only one type of ERS is available. It is called presitito vitalizio ipotecario and is structured as a medium or long loan contract between natural persons aged more than 65 and banks, credit institutions or financial institutions under the supervision of Italian Banking Law\textsuperscript{248} secured by first rank mortgage on residential property. Under this financial product, credit can be granted with annual capitalization of interests and costs, and reimbursement in a lump sum at the termination of the contract. As such, this financial product is used in practice – however recourse to it is not yet widespread – and regulated by legislation\textsuperscript{249} – however regulation is far from being complete and satisfactory (see section 5 describing the legal situation below on page 79).

For the purposes of this research, the Italian way to ERS is qualified as a Loan Model, i.e. credit agreement. No alternative product is available until now.

The Association of Italian Banks suggests a definition of ERS equivalent to lifetime mortgages (Loan Model ERS), to which the Italian product can be assimilated\textsuperscript{250}. Lifetime mortgages are regarded as financing secured by mortgage of residential property through which enables the owner to convert into liquidity part of the economic value of the property. The purpose is to devote such liquidity to consumers’ needs. The owner continues living in the property. Reimbursement of capital plus interests and costs occurs at the termination of the contract. Interests and costs are capitalized on a periodic basis. The Association of Italian Banks also provides for a definition of the home reversion scheme\textsuperscript{251}, which is not applied in Italy. In the home reversion scheme (Sale Model ERS), the owner sells the property to the financial institution or bank, while maintaining the right to live in the house. The latter grants a lifetime annuity or a lump sum (usually amounting to 30-65 % of the property value). One of the reasons why home reversion schemes in Italy are not popular could be that – as opposed to the schemes of the lifetime mortgage – it precludes the possibility that the heirs recover the property. From a cultural point of view, Italians seem very attached to the home in which they grew up and the family has lived in their lifelong time (see below, point 6 c)\textsuperscript{252}.

3. Providers

<table>
<thead>
<tr>
<th>Provider</th>
<th>Form of Organisation</th>
<th>Launch date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deutsche Bank SpA (Prestitempo)</td>
<td>Special Branch of Deutsche Bank, active in the field of credit to families</td>
<td>April 2008</td>
</tr>
<tr>
<td>Euvis SpA</td>
<td>Financial intermediary originated from the merger of Cofide SpA, a major Italian industrial group and Merrill Lynch. Its activity focuses on financing to the elderly. It is subject to supervision according to Italian Bank Law, art. 106</td>
<td>2006</td>
</tr>
</tbody>
</table>

\textsuperscript{248} See art. 106 Legislative Decree of 1\textsuperscript{st} Sept. 1993, no. 385.

\textsuperscript{249} See Law of 2\textsuperscript{nd} Dec. 2005, no. 248, art. 11-quaterdecies, paragraph 12.


\textsuperscript{251} See (fn 250).

\textsuperscript{252} Response from Questionnaire PQ7.
4. Markets

There are no official government sources for statistical data on the Italian market of ERS. However, data by the Association of Italian Banks show the growth potential of this market. The number of elderly people is progressively increasing in Italy. While the income of people over 65 is drastically reduced, their level of wealth is constant and assessed to be at a high level. This shows that the wealth – mainly based on home ownership – could at least in theory be mobilized by way of ERS.

5. Legal situation

Legislative definition of reverse mortgages in Italy is provided by Law of 2nd Dec. 2005, no. 248, art. 11-quaterdecies, paragraph 12, which simply states the following generic definition:

“A lifetime mortgage loans (Prestito ipotecario vitalizio) is the granting by credit institutions and companies, as well as by financial intermediaries according to art. 106 of Italian Banking Law (Legislative Decree of 1st Sept. 1993, no. 385, in Gazzetta Ufficiale of 30 Sept. 1003, n. 270) of middle and long term financing with annual capitalization of interests and costs and full reimbursement in a lump sum at the termination, secured by first rank mortgage on residential properties, reserved to natural persons aging more than 65 years”.

This provision does not constitute a special regulation of this particular credit product, but is contained in a Law enacting miscellaneous rules on “urgent measures against tax evasions and provisions in tax and financial matters”.

A draft of a new regulation of lifetime mortgages in Italy was presented under the past legislature (DDL S-1644, Misure per il cittadino consumatore e per agevolare le attività' produttive e commerciali, nonché' interventi in settori di rilevanza nazionale, art. 42, paragraph 2, Disposizioni sui prestiti vitalizi ipotecari)255, but elapsed due to a change in government in April 2008.

From a legal point of view, the definition/regulation of reverse mortgages provided by Law of 2nd Dec. 2005, no. 248, art. 11-quaterdecies, paragraph 12 is almost useless, except in the part in which establishes that annual capitalization of interests and costs is possible256. On the one hand, it cannot be considered as the law allowing for this kind of products to be sold on the Italian market. No legal rule was ever enacted prohibiting these transactions. On the other hand, this definition does not specify many aspects of these financial products, which therefore remain left to the creativity of financial institutions operating in the market. This has led to the development by the banking and financial practice of a product usually entailing specific features, beyond the basic requirements codified by Law n. 248/2005. These features, which could lead to a more precise ‘social’ definition of the Italian version of ERS, are the following257.


254 "Il prestito vitalizio ipotecario ha per oggetto la concessione da parte di aziende ed istituti di credito nonche' da parte di intermediari finanziari, di cui all'articolo 106 del testo unico di cui al decreto legislativo 1° settembre 1993, n. 385, di finanziamenti a medio e lungo termine con capitalizzazione annuale di interessi e spese, e rimborso integrale in unica soluzione alla scadenza, assistiti da ipoteca di primo grado su immobilii residenziali, riservati a persone fisiche con età superiore ai 65 anni compiuti."

255 Emendamenti sostitutivi 42.2 e 42.3 al Disegno di Legge S. 1644.

256 In fact, an act by the Comitato Interministeriale per il Credito ed il Risparmio of 2000 (art. 3) allows this capitalization for financing that are reimbursed by instalments.

257 The features set out in text are mainly those developed by the provider Euvis SpA and made public in the following brochures: Product brochure (http://www.money-advice.net/media.php?id=3255), information
Provider: Which entities can be providers of ERS is almost the only point made clear by Law n. 248/2005. This Law dictates that providers of ERS can be “credit institutions and companies, as well as by financial intermediaries according to art. 106 of Italian Banking Law”. This means that not only banks, but also qualified non-banking institutions can offer these products in the market.

‘Credit institutions’ are basically banks, whereas ‘non-credit institutions’ are other institutions which are called, in Italy, ‘financial institutions’ that can provide loans of any type (art. 106 Banking Law), but which are not banks. Banks are subject to special supervisory regulations, but also non-credit institutions are subject to regulation and supervision by the Bank of Italy, exactly as defined in the information of the EU-Study\(^\text{258}\) (e.g. bigger financial institutions are regulated similarly than banks).

In Italy, it is not necessary for credit providers to be registered as credit institutions (i.e. banks) in order to provide residential mortgage loans. Non-credit institutions called “financial intermediaries” can provide mortgage loans. Insurance companies cannot provide mortgage loans in Italy because Title V of the 1993 Banking Law restricts the granting of loans on a public basis to financial intermediaries (non-credit institutions). Non-credit institutions (financial intermediaries) are registered, authorised and supervised by the Bank of Italy. Non-credit institutions are entered onto a "general register" maintained by the Bank of Italy (The 1993 Banking Law, article 106), but they must also be entered onto a "special register", provided some further standards are given, testifying a particular extension of their business (Banking Law, art. 107)\(^\text{259}\).

The Banking Law confers authority to the Bank of Italy to supervise non-credit institutions entered on both the general and special registers (article 106 and 107 respectively of the Banking Law). Non-credit institutions entered on the special register are subject to higher levels of regulation and supervision as compared to those on the general register (articles 107 – 114 of the Banking Law)\(^\text{260}\). “Banks” under Italian Banking Law must be authorised and registered by the Bank of Italy to undertake banking activities. The Banking Law provides for the general regulatory framework concerning “bank activity”. The Bank of Italy supervises credit institutions (“banks”) and the supervisory instructions for credit institutions are contained within the Bank of Italy Circular 229. Further, articles 53 and 67 of Banking Law confer regulatory powers in regard to prudential regulation to the CICR and the Bank of Italy, and these powers are further specified in Circular 263, "New regulations on the prudential supervision of banks”\(^\text{261}\).

The problem with Italy might be that Italian “banking” law contains also a special regulation for a special type of mortgage loans, i.e. mortgage loans which must have the following requirements: medium or long term, secured by a first mortgage granted by banks (credito fondiario). But this regime operates only if the credit provider is a bank (and the other requirements are given) and increases the creditor’s rights if compared to the normal rules of the civil code regarding mortgage and mortgage enforcement. The major part of Italian home loans (loans for the acquisition of a dwelling) are granted by such banks, according to this special regulation of credito fondiario.
The problem of the applicability of this special regime to ERS where the credit provider is a bank has not been dealt with in literature. However, the Association of Italian Banks report states that as it is uncertain in an ERS whether the duration of the contract will be short or medium or long (depending on longevity of the borrower), the applicability of this special regime could be hindered. In the absence of additional rules on ERS, this uncertainty causes risks for both financing providers and borrowers.

This does not mean that financing (especially ERS) is limited to banks in Italy. On the contrary, financing of any type is allowed only for financial institutions (regulated and supervised) and - as you see from the stakeholders answers to the Questionnaire - the main providers of ERS in Italy are non-banking institutions.

**Property:** First rank mortgages can be created over all kinds of residential properties. Excluded are:

- Real estate with less than a certain value, e.g. EUR 75 000 or EUR 100 000, agricultural real estates and commercial properties;
- Real estate that is situated in an earthquake-danger zone, except for cases where specific insurance applies to the property;
- Real estate that belongs to the artistic heritage, or have environmental restrictions or have not received planning permission;
- Real estate that has been built on zones which have been granted by municipalities according to Law no. 167/1962;
- Already mortgaged real estates, except for cases where the previous mortgage has been paid back.

**Amount:** The amount of financing granted to the borrower depends on his/her age and the home value. The minimal amount is EUR 20 000 and the maximum is EUR 350 000 and the corresponding limits in terms of loan-to-value lie within 20% and 50% of the home value.

**Repayment:** The loan has to be repaid within 10 months after the borrower’s death by the heirs. Otherwise, the estate will be sold within 12 months and if the sales proceeds exceed the amount due on the reverse mortgage, the surplus will be assigned to the heirs.

**Duties of the Borrower:**

- to send an annual communication with the information that the provider requires;
- not to sell or rent the property, except for the case where the full sum is repaid to the creditor;
- to keep the estate in good conditions.

**Purpose:** The purpose of financing granted by way of prestito vitalizio ipotecario is usually not specified. This means that the borrower is free to use the credit as he/she chooses, with the exception that applies for the following purposes: acquisition or renovation of residential property, financing of productive or professional activities carried out by the borrower, financial investments\(^{262}\).

The contract between the borrower and the bank or financial institution has a duration of 30 years. However, termination (usually) occurs earlier, with the death of the borrower.

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\(^{262}\) See Euvis Brochure Information sheet (http://www.money-advice.net/media.php?id=3254).
or the surviving spouse and the credit must then be reimbursed within the subsequent 10 months\textsuperscript{263}.

The giver of the security (usually the borrower himself/herself) confers the power to sell the property in case of maturity of the reimbursement obligation to the creditor. This power can be exercised only one year and one day after maturity of the reimbursement obligation. The creditor has the duty to account on the proceeds of the sale and can get direct satisfaction of its credit from the same proceeds (the legal qualification of these powers according to Italian law is \textit{mandato irrevocabile a vendere con rappresentanza}, arts. 1704 and 1723 para. 2 civil code)\textsuperscript{264}.

If the proceeds from the sale are insufficient to satisfy the creditor’s rights, the debt is remitted, according to art. 1236 Italian civil code, therefore the obligation on the borrower or borrower’s heirs’ is extinguished\textsuperscript{265}.

In case of default by the debtor (the debtor being typically the borrower’s heirs at that point) on the reimbursement obligation, the creditor can enforce the mortgage over the property\textsuperscript{266}.

Moreover, in practice, this product is sold together with an insurance of the property against fire and other damages. This insurance is mandatory: without insurance, no lifetime mortgage can be contracted\textsuperscript{267}.

It must be specified that the legal regulation of lifetime mortgages remains rudimentary and contains no provisions on the subject of tax treatment of lifetime mortgages. The legal definition of the product, however, stating that it is a financing secured by first rank mortgage, implies that it should be regarded as a financing secured by real estate, and not as an income. This means that articles 15 ff. Decree of the President of the Republic 29 Sept. 1973, n. 601 should apply, whereby these financing are subject to a substitutive tax of 0.25% of the financing granted. In certain situations (e.g. when the financing is not devoted to buy the ‘first home’), however, the tax amounts to the 2% of the financing granted. It seems that the lifetime mortgage should fall in this second category, subject to the 2% tax.

There is no special regulation and/or supervision of the credit institutions which are allowed to sell lifetime mortgages on the market. These institutions are subject to the general rules on banking activity, enacted by Italian Banking Law (Legislative Decree of 1\textsuperscript{st} Sept. 1993, no. 385, in Gazzetta Ufficiale of 30 Sept. 1003, n. 270).

Italian Banking Law regulates the relationships between a bank, or similar credit institution, and its clients, and grants important information and form duties. Title VI of this Law, on transparency of contract clauses between banks and clients (arts. 115-120) establishes a series of transparency duties on banks and credit institutions, amongst which the following can be mentioned:

- The bank/credit institution shall make publicly known the costs of the offered products, including interests and penalties (art. 116);
- Contracts shall be stipulated in written form and a copy shall be handed out to the client (art. 117 para 1); the absence of written form the contract is void (or can be set aside) (art. 117 para 3);

\textsuperscript{263} See (fn 262).
\textsuperscript{264} See (fn 262).
\textsuperscript{265} See (fn 262).
\textsuperscript{266} See (fn 262).
\textsuperscript{267} See (fn 262).
• Unilateral modifications to contract conditions shall be expressly set out in the contract and notified to the client with at least 30 days notice. The client can withdraw the contract within 60 days from notification of the unilateral modifications, without bearing any costs (art. 118);

• At least once a year the credit provider shall notify in writing the client on the development of the contractual relationship (art. 119).

The rights conferred to clients by this legislation can be derogated from only in favour of the client (art. 127 para 1) and whenever the sanction of nullity (or voidness) is imposed (e.g. for the omission of the bank to stipulate a written contract and hand out a copy of it to the client, art. 117 para 3), this voidness/nullity can be claimed only by the client, not by the bank or other third parties (art. 127 para 2).

Moreover, the Bank of Italy has powers of control of compliance with banking legislation and repeated violations of those rules may lead to suspension of the bank's activities for no more than thirty days (art. 128 para 5).

What is here worth stressing is that the major provider of lifetime mortgages in the Italian market, i.e. Euvis, respects these duties in its brochures. However, the absence of specific regulation regarding banks duties in case of lifetime mortgages can produce some disadvantageous risks to the elderly, since they are not normal bank clients, but rather a particular class of consumers, needing even more protection than the latter.

6. Reasons for undeveloped markets

a) Legal barriers

Legal barriers to the development of lifetime mortgages in Italy are, first of all, the lack of a complete legislative regulation of this product. This leads to uncertainty and doubts in practice, which hinder a positive opinion on such products by the public.

For instance, Law no. 248/2005 regulating Italian lifetime mortgages (art. 11-quaterdecies, para. 12) does not specify the situations in which the contract can be terminated. For example, is the death of the borrower sufficient? Can the contract continue in favour of the surviving spouse? Can the contract continue in favour of the surviving partner (in case of not married couples) living in the mortgaged house? Is the contract terminated, if the borrower sells the mortgaged property? And what happens if the borrower sells a limited real right on the property, while retaining ownership? There are thus potential risks of consumer detriment due to these uncertainties including future banking practices268.

Moreover, in case of termination of the contract, the modalities of realising the property are unclear. For example, can the power to sell the mortgaged property be conferred upon the creditor? This situation can cause many legal problems under Italian law, since this power to sell could be considered as a prohibited forfeiture clause (according to art. 2744 Italian c.c.). At least an exemption of such situation from the scope of art. 2744 c.c. should be established by legislation269.

Furthermore, the creditor could be considered over-secured, since the power to sell should be the way to realise the property on default. In such a case, what would be the relation between power to sell and mortgage, two different devices serving the same purpose, i.e. securing the creditor's rights?

268 See (fn 250).
269 See (fn 250).
Other legal problems arise from the fact that the duration of the contract depends on the life of the borrower. Is the borrower dies 6 months after the stipulation of the contract, the financing would not be "a medium or long financing" as the Law no. 248/2005 requires. This could also jeopardise the applicability of the rules on real estate credit secured by first rank mortgage (credito fondiario) established by Banking Law, arts. 38 ff., with consequential detriment to both the creditor's and the debtor's interests. With respect to the common rules set out in the civil code for mortgages and mortgage loans, these rules provide for a stronger protection of the secured creditor whenever a series of requirements are given: the mortgage loan is a medium or long term contract; the creditor is a bank; the security is a first-rank mortgage. Even if the provider of an ERS was a bank institution, lacking the requirement of "medium or long term contract" the applicability of the regime of arts. 38 ff. Banking Law could be doubted. Also, tax law aspects should be, of course, made clear.

It has been suggested that a code of conduct between consumers associations and the Association of Italian Banks could be a fair way to assure uniform standards by the credit providers active on the Italian market. For instance, this code could establish that advice and assistance by a friend/advisor of the borrower should be required, together with an involvement of the borrower's heirs in the pre-contractual phase.

b) Economic barriers

The most significant barrier for (potential) consumers of lifetime mortgages could be the high cost of such products in Italy. If a total calculation of the many costs burdening the borrower is made, according to the brochure of the main Italian provider of ERS, the result is that lifetime mortgages in Italy are currently an expensive product if compared to traditional mortgage loans, that most sensible persons should avoid buying, except in cases of desperate need of quick money (this is likely to concern only a few people). Indeed, with respect to traditional mortgage loans, the high costs of this product also on the side of the creditor (due to the risk profile connected to it) makes it difficult for the borrower to get a tangible sum of money to add to his/her pension as a source of extra income.

Despite the absence of Sale Model ERS in Italy, the existing Loan Model ERS (or lifetime mortgages) are not the only way to monetise property because a private equivalent to the Sale Model has existed for a long time. This traditional option available to elderly persons (often widows) involving selling the bare ownership of the dwelling while retaining an usufruct, is the current less expensive way followed in Italy to monetise part

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270 For instance, in case of insolvency of the security giver, the security can be avoided in the insolvency only in a shorter "suspect period" than that established for normal mortgages, i.e. only if created within 10 days before the opening of the insolvency (art. 39 para 4 of Banking Law).
271 See (fn 250). The special rules provided by Italian Banking Law for credito fondiario (arts. 38-41).
272 See (fn 250).
273 See (fn 250).
275 Interest rates and credit provider’s charges are higher in ERS than in traditional mortgage loans: See (fn 250) p.3.
276 The most important risks for ERS providers are longevity of the borrowers higher than the average; interest rate variations; oscillations in the value of the property which is the only security for reimbursement: ABI (Association of Italian Banks), Sviluppo del prestito ipotecario vitalizio in Italia, p.3, and Adiconsum, Responses to the Questionnaire, item 6.1, for whch also reputational risk is very important. See also the inquiry by Assessorato Tutela dei Consumatori e Semplificazione amministrativa della Regione Lazio, pointing out that ERS in Italy produces a multiplication of the borrower’s debt: http://www.portaleconsumatore.it/consumatore/inchiestedettaglio.php?id=247.
of the value of the home. These private contracts are not however found in a commercialised way\textsuperscript{277}.

Alongside monetising too little money for the borrower, the relatively poor value for money that existing Loan Model ERS constitute for elderly people, means that according to one academic respondent of the questionnaire, the widespread recourse to the sale of bare ownership with retention of usufruct is realistically a more economic solution in many cases.

The existence of public programs of aid to elderly care in some Regions of Italy (like South Tirol, Lombardia, Veneto, Liguria)\textsuperscript{278} could be a further obstacle to the expansion of lifetime mortgages, whenever these devices are chosen by the elderly in order to get the necessary liquidity to pay for care.

Although questionnaire responses received from Italian stakeholders was rather low, from the risk factors from a provider perspective, longevity risk and reputational considerations were those considered most important for the supply-side of the market. The ability and accessibility to the valuation of house prices, though important was not seen as the crucial risk factor, perhaps because certain reliable indices already exist\textsuperscript{279}. However, because collection of data concerning house prices does not prevent market variations in the prices themselves, according to the Association of Italian Banks, this remains an important risk for providers.

c) Cultural barriers

Cultural barriers to the spreading of lifetime mortgages in the Italian market can surely be found. Italians are very attached to their homes. This proves to be particularly true for elderly people who are not keen to sell the home where the children grew up and which is connected to dear family memories. Furthermore, the home is the major asset which is expected to descend to the heirs (i.e. children) on the death of the elderly. This expectation of inheritance is so strong that recourse to lifetime mortgages – if any – must be seen by Italians as the \textit{extrema ratio}\textsuperscript{280}.

\begin{itemize}
\item \textsuperscript{277} See Part I: General Report for the explanation as to why this research has excluded private sale and lease back transactions from its definition of ERS.
\item \textsuperscript{279} Prices for housing are regularly collected by Nomisma (an economic think-tank that publishes semi-annual national index of house prices); Il Consulente Immobiliare (an industry-related review edited by Il Sole 24 Ore media group); Bank of Italy; and Agenzia del Territorio.
\item \textsuperscript{280} See Adiconsum responses to the Questionnaire, question 7.4.
\end{itemize}
VII. Finland

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Finland</th>
<th>EU Median</th>
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</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
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<td>House prices (average annual % change 2003-2007)</td>
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<td>Number of transactions per 1000 homeowner (2007)</td>
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<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
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<td>61.7</td>
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<td>Growth in mortgage debt (% 2007)</td>
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<td>Residential mortgage debt (% of GDP, 2007)</td>
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<td>Per Capita Mortgage debt (EUR)</td>
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<td>Net replacement rates on mandatory pension programmes (%)</td>
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<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
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<td>Population growth (% 2008-2035)</td>
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<td>Old age dependency ratio (% 2008)</td>
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<td>24.2</td>
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<td>65+ (% of total population, 2008)</td>
<td>16.5</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>2</td>
<td></td>
</tr>
</tbody>
</table>

ERS Market?          | Loan Model less developed |

With a population of 5.2 million, Finland has an owner-occupancy ratio around 60%. In 2007, 23% of all individuals had housing loans and the average amount of housing loan was approximately EUR 49 000. This amount is higher for younger people from 20 to 39 year-olds (an average of over EUR 60 000). The amount of housing loan per person with a housing loan has grown by approximately 60% since 2002. The total market for housing loans is in the region of EUR 65 billion. All the above is evidence that indebtedness has increased in Finland quite rapidly. The total amount of debts has grown by 86% since 2002 and the amount of housing loans has more than doubled. In Finland, there is a relatively well-functioning old-age pension system and therefore the need for ERS is rather limited. Applicants for this type of scheme find themselves in the lower to middle classes.

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282 Responses from Questionnaire SQ8 and SQ9 to item 3.2 on user profiles.
2. Products

In Finland, both reverse mortgages (Loan Model ERS or Käänteinen laina) and home reversions (Sale Model ERS or Käänteinen asuntokauppa) are offered. These products are mainly tailored to suit customer needs, although this is done within a commercial framework.

The main equity release product in Finland is offered by the OP-Pohjola Group. It is called Käänteinen laina. It was introduced in 2007 and is offered for older homeowners in order to improve their liquidity. The property is used as collateral, with no other solvency requirements. This product operates as follows: the bank transfers to the customer’s current account a certain agreed sum of money once a month. Within this general framework, two 'sub types' have been described by the providers.

- **Reverse mortgage for “lifetime”**. Payment and the maximum loan amount are defined in such a way that the loan does not go over a certain percentage of the home value. This percentage varies accordingly with the customer’s age, and the limit is calculated in a way that, should the agreement cover a long life, the percentage would be of 70% at the customer’s age of 95\(^284\). In real contractual terms, the agreements are concluded for 10 years. On expiration, the situation is revised and the agreement can be renewed. The customer is not bound to make regular payments, on the contrary, interest is added on the principal and the loan becomes due for payment at the end of the loan period. **The loan limit for the first ten years is about EUR 12 300 with monthly payments to the customer typically calculated at about EUR 75.**

- **Reverse mortgage for a limited period.** It operates similarly to the above described sub-type, except that there is a fixed term associated with the scheme and that the loan limits will vary, i.e. the limit of the loan (maximum loan amount) for 5 years is EUR 50 000, with a correspondingly higher monthly payment amount to the consumer of about EUR 715.

Certain observations on the products are listed below:

- With a limited number of providers, the market is relatively new, which makes it difficult to assess potential future restrictions.

- Charged rates of interest are variable\(^285\).

- Interests are accrued to the principal, and are to be reimbursed at the end of the loan period (reimbursed, or included as the subject of a renewed agreement or subject to an amortisation plan). Although no great details are available about how interests are construed, there is no ground to assume the existence of risk of anatocism during maturity. The main risk of anatocism would occur at the time of renewal.

- ERS described for this market are not directly linked to amortisation programmes. In the case of Loan Model products by Nordea, upon expiry the client that decides not to renovate and not to pay back the full amount to the loan can negotiate an amortisation plan.

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\(^283\) Although the product is called "life time", from a contractual standpoint it appears to be rather a long-term Loan Model ERS with a roll on or renewable facility extending the term.

\(^284\) Notwithstanding the above (70% of the home value at 95 years of age), this provider specified that the common percentage is situated on a 50% of the home valuation. It is to be taken into account that agreements are concluded for a number of years with a “roll on” or renewable facility. Interests accrue the principal loan amount and both become due at the end of each period.

\(^285\) As indicated above: Nordea (September 2008) had a nominal interest of Nordea prime (4.50) + 1.40, and upfront fee of EUR 400. The OP-Pohjola Group APR June 2008, 6.25, plus handling fee of EUR 50.
Risk evaluation has been described by both providers and stakeholders as similar to evaluations of any other risks. However, lack of data for risk evaluation is a factor.

Transfer of Title takes place on expiry. Providers report that this is a decision of the customer, although, in real terms the decision would be dependant on the customer’s financial capacity to reimburse the loan and interests accrued.

No data has been provided in relation to transfer of sureties for this type of credit product.

Another product known in the Finnish market is called HomeFlex. It was launched in 2005 by the Nordea Bank Finland. It consists of a combination of loan and current account. This product operates as follows: if the customer owns a home with free equity, he can be granted a loan up to 75 % loan-to-value, using the home as collateral. In combination with the loan, customer obtains the facility of a current account. The loan is a balloon loan with 10 years’ maturity, whereby, the customer only pays the interest. After 10 years, the loan can be renewed, paid back or an amortisation scheme can be made. Customers can also pay the loan back any time before expiry without extra cost. Customers pay an up-front fee for the product. Interest rate for both the loan and the current account is the reference rate (Nordea Prime rate) + a customer margin. If the amount on the current account exceeds the amount of the loan, the customer is not paid any interest on the exceeding amount. Tax at source is deducted from the interest paid on the account.

Also outside the frame of the narrow definition used for our survey, are products like those mentioned above which are tailored for the same purpose and target group but are based on ordinary mortgages. For instance, the OP-Pohjola Group banks have used traditional secured lending products for releasing equity (ordinary line of credits and bullet loans). However, statistically these loans are considered to be ordinary consumer loans and thus could not be separated from normal consumer credit. We have however, made sure that their comments concerned only the specific Loan Model ERS (Käänteinen laina).

Sale Model ERS have been reported to exist by some respondents to the survey, but only little information on this product was provided. Features of the product include a fixed term during which the consumer will receive the proceeds of the house he has sold (typically ten years), and the need for the consumer to deduct payment of a rent of the property from the bank.


Special note must be taken that this product, based alone on its description, does not strictly qualify as an Equity Release scheme according to our definition (see Part I: General Report, Section A). Though the response from the provider in question for the Homeflex product has been taken into account for the report, caution should be taken with interpretation of any data referring to the overall size of the ERS market.

The provider in question is part of the Hypo Group, known as Hypoteekkiyhdistys, with operations including work of the Mortgage Society of Finland and the special deposit bank Suomen Asun托hypopankki Oy. The following media reports from 2006 are examples of their product:

http://www.asuntotieto.com/10000i_ASUNTOMARKKINATIETO/10000i_kaant-askauppa.html and
http://www.hs.fi/asuminen/artikkeli/Myisink%C3%B6+asuntoni+pankille/HA20061210SI1FA03emi.
3. Providers

There are only two financial services institutions active in the equity release market.

The first is the OP-Pohjola Group, a financial services group amalgamating over 200 co-operative banks whose core business areas are asset management, lending devices, payment services, and non-life Insurance. This Group offers only reverse mortgages (Käänteinen laina).

The second provider identified is the commercial bank Mortgage Society of Finland (Suomen AsuntoHypoPankki) operates in the Finnish equity release market offering both Loan Model ERS (Käänteinen asuntolaina) and Sale Model ERS (Käänteinen asuntokauppa).

<table>
<thead>
<tr>
<th>Provider</th>
<th>Form of Organisation</th>
<th>Launch date</th>
<th>ERS Type</th>
<th>Payments, Liquidity</th>
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<tr>
<td>OP-Pohjola Group</td>
<td>Financial Services Group</td>
<td>2007</td>
<td>Loan Model</td>
<td>monthly or as agreed</td>
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<td>Mortgage Society of Finland</td>
<td>Credit institution</td>
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<td>Loan and Sale Model</td>
<td>n.a.</td>
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</table>

4. Markets

The target group for ERS are middle-aged/older home-owners with relatively little debt, dwelling in the home located mainly in non metropolitan areas. Contracts are concluded mainly by customers aged over 60 who may be low-income but are owners of some real estate property.

Deposit-taking banks play a significant role as intermediaries of finance. The bulk of households’ borrowings are made up of home loans, which are nearly all granted by deposit-taking banks in Finland.

ERS are offered mainly to customers aged over 60 who may have a low-income but have some equity invested in their homes. The age for contracting ERS is estimated by experts to be in the region of 50-60, and the average age for termination at 75-90. Providers explain that they have not marketed or sold the product very actively, and that as the total amount of contracts still remains too low in their eyes, they have been unable to more accurately define a user or contract profile.

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289 Various providers and stakeholders were contacted. Two providers were among those that provided more complete information alongside an industry trade association, along with a senior adviser at the Ministry of Justice. More superficial consultation (through web pages) was carried out with Consumer Protection bodies Consumer Disputes Board and Advisory Office for Bank Customers.

290 Excluding Nordea Bank Finland and its mortgage product for the reasons outlined in the previous Product section above.

291 Details of the provider come from the company website only: http://www.hypo.fi/kaanteinen_asuntokauppa.

292 According to a survey made in 2006 by the OP-Pohjola Group most users are retired, male, married and live outside the Metropolitan area.

293 From Questionnaire responses SQ8 and SQ9 to item 3.2 on user profiles.
Respondents described no automatic exclusion. On the contrary, applications, valuations and liquidity inquiries follow the same procedure as in any loan reliant on the guarantee provided by collateral (real estate), and on a case-by-case basis.

There are no Government Statistics specifically related to equity release products.

5. Legal situation

There is no well-established definition of an ERS in Finland and though the market has an established number of contracts, it is still quite new and small. No product specific legislative initiatives are expected. Academia is not very active in respect of this type of financial product.

However, as general regulation on the consumer credit also widely covers loans where the home is used as collateral, implementation of the Consumer Credit Directive will cause some regulatory changes, because in the case of Finland these EU rules will probably be applied to home loans and Loan Model ERS too.

With regards to Sale Model ERS, such products are regulated following sales regulations. These regulations cover all purchases of real estate and have the typical requirements of notary involvement etc. Beyond there are consumer rights as laid down in the EU Directive on consumer sales.294 Below are observations based on the legal situation surrounding Loan Model ERS:

Prudential regulation:

- There are no specific supervisory requirements regarding providers of ERS in Finland. However, since ERS are in practice offered only by credit institutions, they are supervised by the Financial Supervisory Authority. In this respect, a licence or permission to operate banking business is sufficient.

Private Law:

- No restrictions as to a maximum age for mortgages were described. The minimum average age, decided by the ERS provider, would seem to be 60 judging from questionnaire responses;
- No automatic exclusion has been described;
- No compulsory involvement of an insurer has been described as a specific requirement over and above any other loan having real estate as either main guarantee or collateral;
- The home is sold at termination of the contract. It is the consumer’s own decision;
- Applications are signed by owners who bear the risk of the contract themselves. However, providers comment that they advise applicants to invite potential inheritors to attend the negotiations.

Consumer protection

- There are no specific rules on pre-contractual advice or information relating to ERS. General rules relating to credits offered to consumers (in Loan Model ERS) and the sale of real estate (Sale Model ERS) are applicable.

- In particular, in relation to reverse mortgages (Loan Model ERS), before conclusion of the contract, the consumer shall be notified of the contract terms and any other information referred to in section 11 Consumer Credit Act Chapter 7, in addition to which he/she shall be provided with an opportunity to peruse them in writing.

- There are two bodies competent to deal with disputes and queries. None are specific to ERS, but common to consumer protection issues (Consumer Disputes Board, at www.kuluttajariita.fi), that issues recommendations concerning disputes involving consumer and housing transactions; or to Banks customers (Advisory Office for Bank Customers, at www.pankkiasia akkaat.fi).

Tax Law

- No tax exemptions through deductibility of interest, or in any other form have been described by those consulted or found elsewhere by the research team.

Bankruptcy Law

- Compared with other private pensions, such as special pension funds that guarantee the total amount of the invested sum, and compared with public pension, ERS provide less security and homeowners may fear to lose their house and pension.

- Regarding the risk that the financial institution faces financial difficulties leading to bankruptcy, no special provisions are set in relation with either ERS.

Insurance Law

- ERS in the Finnish markets are construed as other loans that use real estate as collateral and no special insurance obligations or practices have been described or pointed out as being special.

Property Law

- No property law barriers have been described by respondents to our enquiries, neither from the stakeholder side nor the provider side.

- However, some property related features have been underlined during our enquiry and may limit the eligibility or attractiveness of certain houses for the providers of a scheme (e.g. geographical area or non-use for permanent dwelling):
  
  - During the negotiations, customer’s liquidity is assessed, although the decision on whether to grant the loan is based on valuation of the home;
  - According to the OP-Pohjola Group, if the property is located at an outlying area, it is subject to a more strict appraisal. Properties in non-built areas obtain lesser valuations. This together with data signalling that the average applicant is a dweller in non-metropolitan areas, could amount to a barrier;
  - Providers advise that potential inheritors attend pre-contractual negotiations, and that, co-owners of the home acquire the scheme together, under the same contract (particularly for Loan Model ERS).

295 Statement received from Questionnaire response PQ14.
In terms of the potential providers of Loan Model ERS, as stated in a recent European Commission study on mortgage lending by non-banks\(^{296}\), institutions (or anyone) that provide residential mortgage loans (or any loans in general) do not need to be registered or have any license if they don't take deposits or other repayable funds from the general public. This means that insurance companies could theoretically also market these schemes, even though none of the regulators and stakeholders contacted during our research were aware of any case in which insurance companies or other institutions than banks have provided mortgages in Finland\(^{297}\).

6. Reasons for undeveloped markets

a) Economic barriers

Reliable social security pension schemes in the public sector, and limits set by providers (average rate of loan is set at 50% of home valuation at an average age of 60) may deter the expansion of ERS. However, growing percentages of home ownership may be a positive factor for future development.

b) Cultural barriers

Finland has a relatively relaxed attitude to traditional family structures. This has increased the tendency to use borrowing facilities with a real estate as a guarantee. Second charge mortgages do exist in Finland but are not the dominating form of lending. There are no great cultural barriers to ERS in this country, whether deriving from family or attitudes towards overindebtedness. There is however, a certain reliance on public sector pensions, which to the extent that the level may be difficult to politically reduce, could mean that the necessity to complement smaller state pensions in retirement is unlikely to be the driver for growth in the ERS market in Finland.

7. Risks and benefits

a) For providers

Providers have described two main risks: longevity (as the main risk), together with complexity of product. Both may be grounded on the fact that this market is operated by providers who have only recently entered the market. It is the view of the iff research team, that the way in which ERS are currently contracted in Finland, i.e. for 5 or 10 year periods (although renewable), means that in actual fact longevity risk is not such a real threat in Finnish markets as it may actually be for providers selling their products in other EU Member States where the original agreements are signed for a ‘lifetime’.

b) For consumers

There is a small market, and there are no active consumer organisations specifically involved with ERS. The risks for consumers seem to be mainly related to the longevity of agreements, which are not explicitly contracted for very long. Although agreements are theoretically designed to be renewed and thus can be expected to last a lifetime (all extensions added together), this will be subject to revision, and as such could lead to lending policies changing based on both the value of the collateral and interest rates (which may vary during the loan period). The product is however, flexible (especially for the provider).

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\(^{297}\) See (fn 296).
VIII. Sweden

1. General information

<table>
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<tr>
<th>Category</th>
<th>Sweden</th>
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<td>House prices (average annual % change 2003-2007)</td>
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<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
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<td>Per capita private pension fund assets (EUR)</td>
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<td>Population growth (%, 2008-2035)</td>
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<td>Old age dependency ratio (%, 2008)</td>
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<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>17.5</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>ERS Market?</td>
<td>Loan Model less developed</td>
<td></td>
</tr>
</tbody>
</table>

Sweden has a population of 9.2 million, a population of 60+ of 2.1 million, an owner occupancy rate of 50%298, and an average number of persons in the household of 1.35. The number of qualifying households stands at 1.05 million and the average Swedish house value lies at about EUR 175 000. In 2007, interest rate subsidies and investment grants for housing were abolished. Household debt has nevertheless continued to increase with the majority of these loans being obtained for house purchases and more than 85% of the loan stock is using property as collateral299. Most of the loans are

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298 Although Sweden has a homeownership rate of 67% according to some statistics dependent on the treatment of housing association’s and cooperative ownership (e.g. owner flats are not legally possible in Sweden as reported in the EMF’s Hypostat 2007, November 2008 (http://www.money-advice.net/media.php?id=3288)).

provided by mortgage institutions, while a few of the loans are provided by banks in the form of second mortgage loans and other growing types such as interest-only loans.

2. Markets, products and providers

There is only one provider of ERS in Sweden to date named Svenska Hypotekspension. The company has taken the name that exists to describe Loan Model ERS in Swedish as its brand name: Hypotekspension®. There are no Sale Model products offered anywhere in Sweden.

The Loan Model was defined by one respondent to the survey as "a reverse mortgage, either paid directly or in the form of ten years annual life insurance repayments". What this means is that either a consumer can get the mortgage loan as a lump sum at once or in form of a life annuity paid monthly or annually. The latter option of a regular income payment however can only be received for a period of ten years (though the debt can remain outstanding until the house is sold). This is one restrictive feature that does not exist when compared to other products available in Europe. The Hypotekspension® also contains a no negative equity guarantee.

With Svenska Hypotekspension currently the sole provider of ERS in Sweden, such schemes are new and represent a limited share of the mortgage market. Although a number of banks offer other mortgage based loans to people over 60 and the retired, these products do not qualify as ERS as defined by this study. The Swedish National Bank confirmed that due to the insignificant number of companies offering ERS, the marketing of ERS is very limited and is solely provided via direct marketing. No intermediaries are thus currently operating in this very small field. The products are however promoted by banks.

A Sale Model ERS (i.e. home reversions where a homeowner sells his house but keeps the right to reside in the property) does not exist on an institutionalised and commercialised basis between a moral person and an individual. The private non-commercial equivalent to Sale Model products is not unusual within the family. An elderly person may give or sell her house to her children under the condition that she may live there as long as she wishes. But such an arrangement on a strictly commercial basis, although not illegal, is more or less non-existent.

No subsidies or governmental promotion of ERS exist. No legislative initiatives are planned.

3. Legal situation

In Sweden, providers must obtain a license through the Swedish FSA to offer equity release products. Act (1992:1610) that regulated the licensing has been replaced by the law (2004:297). The Swedish expert told the research team that a company to offer ERS must be a credit institution and be registered as such, (2004:297) chapter 1, 4th and 5th paragraphs together with chapter 2 first paragraph. According to her the exceptions given in the law seem not to apply. Consequently, also 'Svensk hypotekspension' on their website write that they have permission from the Swedish Financial Supervisory Authority. The Banking and Finance Business Act, chapter 2 first paragraph. To approve a credit the provider has to control if it is due cause to believe the borrower will fulfill the loan obligation, according to the Banking and Finance Business Act chapter eighth paragraph. Since the year 2002 a credit institution could prove the borrowers repayment

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300 Though Svenska Hypotekspension is the only company offering ERS at the moment, several banks offer regular mortgage loans to finance but have not been included in this survey due to their time-limited offers.

301 A request to clarify this has been made to the Swedish Financial Supervisory Authority but had not been answered until December 2008 when this report was terminated.
ability both from income and assets according to a statement from the Swedish Financial Supervisory Authority, earlier the borrower had to prove any kind of income to pay back the loan.

The specific pre-contractual advice or information provision requirements are stipulated under the consumer credit law (1992:830), while advertising restrictions are stimulated in Art 6-8 consumer credit Law (1992:830). There is a lack of specific procedure rules for ERS. Legal problems on ERS are handled as ordinary civil cases.

Sale Model ERS, as mentioned above, are not forbidden by law in Sweden, but the recognition of the surrounding civil law is uncertain. If the leasing agreement includes a repurchase option in real property for the seller, the agreement may not be valid according to the Chapter 4, Sections 3.1 and 4 of the Code of Land Laws (Jordabalken 4:3 and 4:4). An important point in considering these matters is whether the repurchase option can be regarded as a condition of the ‘completion or existence in force’ of the initial purchase. To be valid, a condition is that the repurchase document must be included in the purchase documents. It does not matter if the transaction is between two physical persons or if a business entity is involved.

4. Risks and benefits

We have contacted the Ministry of Finance, the Swedish Nationalbank (Sveriges Riksbank), the Swedish Financial Supervisory Authority (Finansinspektionen), the Swedish Council of Mortgage Lenders and the Swedish Consumers Association, yet not all of the questioned institutions have answered until now. Also contacted has been one provider (ERS are rather new in Sweden and have only a very limited share of the mortgage market. The Swedish Consumers’ Association has therefore not taken any views on the risks and benefits of ERS schemes.

The Swedish National Bank reports that concerns for a potential provider would include the property valuation as well as their own reputation. Significant risks for the consumers would be displayed by possible family disputes over the heritage. Access to credit in old age and consequently more liquidity was nevertheless reported by stakeholder responses as likely to bring benefits to consumers on a low pension during retirement.
IX. Germany

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Germany</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>43.2</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>-0.5</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>9.9</td>
<td>20.6</td>
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<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>1155.7</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>-2.4</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>47.7</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>14050</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>58.0</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>36.9</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>1114</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>82.2</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>-3.7</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>30.3</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>20.1</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>2</td>
<td></td>
</tr>
</tbody>
</table>

ERS Market?  

<table>
<thead>
<tr>
<th>Loan &amp; Sale Model less developed</th>
</tr>
</thead>
</table>

The iff received eight answers from providers, among them four filled out questionnaires. Three provider associations also contributed, as well as a notary association and the federal regulator (BaFin) answered as stakeholders.

Germany has a population of 82 million and demographics that include low fertility rates and thus a shrinking population according to official forecasts over the coming decades. Outstanding residential mortgages in Germany amount to EUR 1 184 billion (2006), house prices have been stagnant or slightly negative from 2000 and the rate of homeownership which is 54% on some accounts, is actually even lower at 43% when

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measured in terms of owner occupancy (2002). The average house price is EUR 224,000 in West Germany and EUR 183,000 in East Germany. The amount of new houses and apartments for private use per year has increased over the years. The German housing market is characterised by a market for rented flats that is traditionally very strong, partly a legacy of past housing policies that favoured rental to generate affordable housing quickly. Compared to most other EU countries, there is also little 'trading up' by homeowners in Germany, which may also explain lower house transaction figures.

A number of banks in Germany set up ERS in about the year 2000. There was however no market launch at that time. Products were announced and then withdrawn. Nevertheless, a discussion started which was revitalised in 2006 alongside discussion on private pension subsidies, where politicians announced that investment in the home should form part of pension provision. This led to the 'Riester Home Subsidy' in 2008, in which the incorporation of ERS was discussed.

2. Providers and products

Germany had a system of life annuities (Leibrente) for a century, which was regulated by the civil code (§§ 759 ff. BGB). These annuities were arranged between private individuals and gradually fell out of use. When they were used, this occurred mainly between family members. HVB Bank has occasionally acted as broker for such annuities in the Munich region in recent years. In general, these schemes do not form part of mainstream financial services.

In October 2008, there were two providers of ERS in Germany. The Friedenau Foundation reported that in total only 12 agreements had been concluded to date based on a Sale Model ERS. Its product therefore has no significance to the German market as a whole, even though it was not subject to any regional restrictions. The second provider (Hannoversche Lebensversicherung) has offered a Loan Model ERS since the beginning of 2008. This Rentenhypothek product offers an ordinary mortgage product designed for retired people, who pay monthly interest but no amortisation is required until death or departure from the property.

305 E.g. Dresdner Bausparkasse (Provider), Frankfurter Allgemeine Zeitung from 22.10.2000.
309 Knowledge gathered from previous research was used as a basis for this report. In addition, six (potential) providers of Equity Release schemes were contacted (Deutsche Bank, Dresdner Bank, Commerzbank, Investitionsbank Schleswig-Holstein, Stiftung Liebenau, Hannoversche Lebensversicherung). German experts who had recently published in this area were contacted, specifically the European Economic Research Center, ZEW in Mannheim (Interviews were held with Wolfgang von Nostitz (Lawyer) and Gunnar Lang (Economist)).
310 Interview with Attorney at Law von Nostitz, Munich.
311 From a questionnaire completed by the German Chamber of Notaries: “ERS as defined by the scope of this study are not common in Germany and - to our knowledge - are not provided so far. People ask more for private pension agreements especially among family members like e.g. life annuity (Leibrente, Dauernde Last) or usufruct/right of residence (Nießbrauch/Wohnungsrecht) or rather tend to sell and move house when they need liquidity.”
312 Information based on the Questionnaire filed out by the provider in July 2008.
Two other providers, one government-owned bank (Investitionsbank Schleswig-Holstein) and an intermediary (Immokasse) planned to start their own ERS at the end of 2008 or at the beginning of 2009. These products have not yet been launched. Several other providers, among them leading commercial banks, are considering a market launch of ERS in Germany.

<table>
<thead>
<tr>
<th>Provider</th>
<th>Organisation</th>
<th>Launch Date</th>
<th>ERS Type</th>
<th>Payment</th>
<th>Repayment in lifetime</th>
</tr>
</thead>
<tbody>
<tr>
<td>Friedenau Stiftung</td>
<td>Foundation</td>
<td>2004</td>
<td>Sale Model</td>
<td>Monthly</td>
<td>No</td>
</tr>
<tr>
<td>Hannoversche Leben</td>
<td>Insurance</td>
<td>2008</td>
<td>Loan Model</td>
<td>lump sum (5 times max.)</td>
<td>Monthly interest payments only</td>
</tr>
<tr>
<td>Immokasse</td>
<td>Intermediary</td>
<td>2008*</td>
<td>Loan Model</td>
<td>monthly, lump sum, line of credit</td>
<td>No</td>
</tr>
<tr>
<td>Investitionsbank SH</td>
<td>Bank</td>
<td>2009*</td>
<td>Loan Model</td>
<td>monthly</td>
<td>No</td>
</tr>
</tbody>
</table>

* = planned

The focus on fixed-rate mortgages arises from the general structure of the German mortgage market, where 98% of mortgages fall into this category. Existing and proposed products offer lifelong contracts. Funds released may take the form only of lump sums or monthly instalments.

Second mortgages are not very common in Germany. In fact there has been widespread discussion in the German media about discrimination against older people in the mainstream mortgage market.313

3. Markets

There are no official government sources for statistics and data on ERS.314 As there is presently no relevant equity release market in Germany, figures may emerge from outstanding responses but in general no data is expected. The total number of existing contracts was estimated by iff in the year 2008 at less than 100 contracts in total which represent EUR 10 million against EUR 1 184 billion in outstanding domestic mortgages in Germany (0.0008%).315

Future prospects about the market share of ERS in Germany are difficult at the moment, but information from providers shows that a market share of 7% in relation to ordinary domestic mortgages could be achieved in the future.

313 Exclusion from services (also financial services) because of age is against German anti discrimination law (AGG) based on an EU-Directive.
314 Questionnaire of the Bundesverband Öffentlicher Banken Deutschlands (Provider Association) and the Bundesanstalt für Finanzdienstleistungsaufsicht (Regulator), August 2008.
4. Legal situation

In Germany there is no specific legislation governing ERS, whether in the civil code (Bürgerliches Gesetzbuch), or in tax or other law. Payments from reverse mortgages are not a form of income and merely amount to a loan. No income tax is therefore payable. There are however no government subsidies or promotion to encourage reverse mortgage products at the moment. This has discussed at academic level in connection with private retirement pension schemes ('Riester Home Subsidy').

Legislative initiatives to facilitate ERS in Germany are unknown.

5. Reasons for undeveloped markets

a) Legal barriers

In general, German lawyers do not see any insurmountable legal barriers to reverse mortgage products. The longevity risk could, however, be taken on only by a provider licensed as an insurer (§§ 1, 5 VAG, § 1 VVG) in most Loan Model ERS. This is because monthly payments depending on an uncertain event in the future (point of death) are legally defined as an insurance business, which falls under insurance law and requires a licence as an insurer and special control mechanisms. It is therefore difficult for banks to offer ordinary reverse mortgage products without entering into a joint venture with an insurance company in Germany. One provider, the Investitionsbank Schleswig Holstein is looking for another solution with a fund which will take on the longevity risk. The other existing provider, Hannoversche Lebensversicherung, is itself an insurer.

Interest on interest (Anatocism) is forbidden by law (§§ 248, 289 BGB), which is a problem for ERS, where the payment comes only after several years on decease or departure of the borrower. However, lawyers take the view that solutions are available to this problem in Germany. For example, up front interest payments in the form of a Disagio have been seen as in conformity with the law. Keeping two separate accounts or credit contracts one of which providing for a credit that pays the interest while the other pays the credit is another way to overcome the obstacle of Art. 246 Civil Code (BGB). There is also the general opinion that current accounts with consumers are exempted from this rule according to Art. 355 Commercial Code (HGB).

b) Economic barriers

In addition, several potential providers evaluate the German market for ERS as too small to be viable.

On the one hand, restrictive planning laws in Germany do not stimulate the private housing market, and the resulting situation is very different to Spain or the UK. The moderate level of house price fluctuation means the average amount which could be secured on the house/flat in question would be much less than in other countries. Moreover, the percentage of homeowners is in Germany relatively low. Changes to fiscal laws may gradually change the tenure breakdown historically observed until now, and with it perhaps the investment practice of owning a house but choosing to rent it out and to rent a different one to live in.

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319 See (fn 316).
320 Based on interviews with Commerzbank and Dresdner Bank.
On the other hand, the group of older people (60+) not wishing to gift their home and any other assets available for consumption purposes on death would appear to be too restricted for many providers. Moreover, retirement pensions are relatively high in Germany and poverty among retirees is not widespread at present.\(^{321}\)

A third economic obstacle in Germany for potential providers appears to be the demographic factor.\(^{322}\) An additional factor is that banks operating nationally offered ERS nationwide. This was because they felt that confining their offer to houses/flats in attractive metropolitan areas, as opposed to rural areas or areas with a declining population, would put them at risk of negative publicity.

c) Cultural barriers

Specific consumer barriers have not been identified because of the limited number of products currently available. It emerged from discussions with potential providers, however, that German consumers are very interested in ERS in general, but very reticent when they learn the amount of funds the scheme could let them produce from their home.

Traditionally, Germans have paid off all borrowing in respect of their home before retiring and it is usual to aim to be completely debt-free by that time, especially in relation to their home.\(^{323}\) No research has addressed these matters specifically.

6. Risks and benefits

a) For providers

Risks for German providers are as follows, in order of importance, with the most important first:

- problems of posterior sale, realisation of the investment;
- risk of extreme longevity;
- secondary purchase of outstanding debts;
- refinancing problems;
- control problems (e.g. ongoing maintenance checks and keeping of the real estate in good condition).\(^{324}\)

b) For consumers

Risks and benefits are difficult to identify in detail at present\(^{325}\) because of the limited number of products as yet available in Germany. Recent media reports point to

\(^{321}\) See Eurostat Yearbook 2008 Europe in Figures, Living conditions and welfare chapter (2008), available at http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/KS-CD-07-001/EN/KS-CD-07-001-EN.PDF. Figure 4.2 p.222 shows a favourable income of elderly people in relation to different population groups. Table 4.1 p.223 shows that the at-risk-of poverty rate of the retired at 14% lies below the EU average and considerably lower than say the UK and Ireland figures which stand at 28% and 30% respectively. Figure 4.2 p.240 shows expenditure on pensions (all pensions in 2004) above the EU average at over 13% of GDP.

\(^{322}\) E.g. interview with Commerzbank and Dresdner Bank. Also, statistics of people per household at 2.1 in Germany is the lowest figure in the EU.


experience in other countries. In December 2007, iff pointed to the following benefits for retirees in relation to reverse mortgage products (Loan Model ERS).

- higher liquidity for retirees;
- capital for unplanned expenses (home care);
- security of lifelong payments;
- repayment at any time;
- no loss of home during lifetime.

If the suggested at the same time that an easily understandable product, transparency of prices and costs, advice before signing the contract (showing alternatives such as use of other liquid assets), clarification of risks (reduced inheritance, payment of interest on interest), security as homeowner, protection against third parties, judicial sale and flexibility where there is a change in living circumstances, are important aspects of ERS. These points also show the potential risks for consumers if they are not taken into account in new ERS or products in Germany.

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X. \textit{Austria}

1. General Information

<table>
<thead>
<tr>
<th>Category</th>
<th>Austria</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>57.0</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>1.9</td>
<td>9.2</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>65.1</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>7.1</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>23.9</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>7820</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>90.9</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>72.8</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>1430</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>8.3</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>8.9</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>25.4</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>17.2</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>ERS Market?</td>
<td>Loan Model less developed</td>
<td></td>
</tr>
</tbody>
</table>

With its population of 8.3 million, Austria lies in the middle between 12 smaller Member States and 14 larger ones measured demographically, and is also the most representative for the EU-27 as a whole regarding statistics on the age distribution of this population (whether one uses figures for today or those projected by the Eurostat in 2035 and 2060)\textsuperscript{327}. With fewer than 60\% of households in owner-occupation (a figure that rises if expatriate populations are excluded), Austria is generally associated as a ‘low’ homeownership country within the EU alongside France and Germany. A general preference to rent rather than buy is supported by a rental law that is tenant-friendly, and as a result of temporary government policies put in place during the 1990s which helped to increase the supply of rental housing.\textsuperscript{328} Though not as great as in the Netherlands, the Austrian housing market is also characterised by a rather large social

\textsuperscript{327} The 15.2\% figure for the ratio of persons 65+ in the total population in the data table for the EU is the median value calculated for the 27 Member States. The actual EU-27 ratio is 17.1\% for 2008 (rising to 25.4\% by 2035).

rented sector. As elsewhere in Europe, trends in house prices have seen provincial prices trail those in the capital, resulting in falling national house prices since 2000 in real terms. The Austrian mortgage market is smaller than the EU average and is characterised by a significant proportion of foreign-currency mortgages (similarly to say Slovenia or Denmark).

2. Providers and products

In Austria, there is an Immobilienrente (‘real estate rent’), which is a reverse mortgage with fixed interest rates for a maximum term of 15 years. There is no repayment during the term of the credit. The sole provider found in Austria is a savings bank and due to regulatory restrictions imposed on the sale of Loan Model ERS by the law governing savings banks (Bausparkassengesetz), the credit can be used only for nursing, help and medical treatment of people in need of care. This means that it is necessary to verify the need of the customer for long-term care before the provider can extend the product, therefore it is a rather selective product and is targeting a specific subset of those persons typically interested in ERS. The amount of funds released is limited by law to EUR 150 000 per person. The law provides that the loan-to-value rate must not exceed 80%. The product was launched in April 2006. It is marketed through direct marketing only. No Sale Model ERS are offered.

3. Markets

Selective evidence suggests that ERS are not offered in Austria, at least not by major banks.

Other than those customers facing care expenditures, there is no possibility for other consumers to get an ‘Immobilienrente’. For this reason, some correspondents have judged that ERS does not exist, but in our view, it technically does, however insignificant the market in Austria is at the moment.

4. Legal situation

No real legal obstacles for ERS can be identified in Austria. It is possible to conclude a contract concerning a Leibrente (§§ 1284 – 1286 ABGB) or to raise a loan (Darlehen).

Equivalents: Sale and Lease Back (Leibrente); Second Mortgage Loan (durch eine Hypothek besichertes Darlehen).

Leibrente: §§ 1284- 1286 ABGB (Allgemeines bürgerliches Gesetzbuch).

„§ 1284: Wird jemanden für Geld, oder gegen eine für Geld geschätzte Sache auf die Lebensdauer einer gewissen Person eine bestimmte jährliche Entrichtung versprochen; so ist es ein Leibrentenvertrag.


§ 1286: Weder die Gläubiger, noch die Kinder desjenigen, welcher sich eine Leibrente bedingt, sind berechtigt, den Vertrag umzustoßen. Doch steht den Erstern frey, ihre Befriedigung aus den Leibrenten zu suchen; den Letztern aber, die Hinterlegung eines entbehrlchen Theiles der Rente zu fordern, um sich den ihnen nach dem Gesetze gebührenden Unterhalt darauf versichern zu lassen.“
C2C contract. Depending on the arrangement of the contract it can be a contract of sale, a barter agreement, a donation contract, a contract for work and services or an insurance agreement. Such contracts include an aleatoric part. If the annuitant dies, the rates don’t have to be paid any longer. The Leibrente can be secured by a mortgage.

Another possibility is to raise a loan (Darlehen) and encumber your home with a mortgage (Hypothek). The regulatory framework is embodied in §§ 983 ff and § 448 ABGB (Durch eine Hypothek besichertes Darlehen).

No definition of ERS or other regulatory framework thereover can be found in Austrian law at present. Consequently no regular controls on ERS or their providers are exerted. Considering the offered product ‘Immobilienrente’ as an ERS it is partly regulated by the Bausparkassengesetz which allows for nursing, help and medical treatment of people in need of care only. It also limits the amount of funds released to EUR 150 000 per person only and provides for a LTV-ratio not higher then 80%.

5. Reasons for undeveloped market

a) Economic and cultural barriers

The Austrian Law is - like e.g. the German Law - based on the Roman Law. The legal concept of ERS is not common in Roman Law based countries. This is not especially for legal reasons, but more for financial (adequate pensions) and cultural ones. The attitude to debt in Austria (and Germany) is different to countries like the USA. Also sociological obstacles seem to be important, because in Austria you "normally" leave a bequest. People in Austria usually hand their homes down unencumbered, if it is possible. Like in Germany debts are frowned upon. People try to amortise debts or mortgages as soon as possible rather then remortgaging. It is also vital to consider economic obstacles. Due to the absence of a regulatory framework there are sizeable uncertainties concerning ERS.

It is worth noting that more and more the demographical development leads to new forms of old-age provisions. Although its effects of are difficult to predict, it may be essential that the banking sector is offering new products for elder people, so they can phase-out their real property and gain liquidity without having to abandon their residence. One of them is the Immobilienrente. Annuitäten (annuities) and Rückhypotheken (reverse mortgages) seem to be incremental segments in the future. At the moment, the public provisions for people’s old age in Austria are assured. Elder people draw a social security pension, which means that there exist several social security benefits. Austria has the second highest current pension spending in the OECD, behind only Italy. Even after recent changes to the pension system, target pensions are still expected to be the fifth highest in the OECD (The gross replacement rate – pension in retirement relative to earnings when working – is projected to be 80% of average earners in Austria, compared with 59% for the OECD as a whole and double the expected replacement rate of only 40% in Germany). Therefore, there is no great demand for innovative products like reverse mortgages or annuities. But as soon as a cutting of the benefits starts, the people will have to look for new ways to finance their living standard during retirement.

Group 3: Member States with Sale Model ERS only

XI. Romania

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Romania</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>97.6</td>
<td>75.0</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>4.3</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>86.9</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>3.5</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>200</td>
<td>7820</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>56.5</td>
<td>65.2</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>21.4</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>-8.4</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>21.3</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>14.9</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>ERS Market?</td>
<td>Sale Model less developed</td>
<td></td>
</tr>
</tbody>
</table>

Homeownership in Romania is high, whilst mobility is low. The typical pensioner has lived in their own homes for the past decades and wants to continue living the rest of their lives in their own homes. Results of our survey in Romania show how quickly the market can change. At the start of research for this study, it was clear from preliminary work that no ERS existed. However, when drafting the final report, it became apparent that a Sale Model product was being offered by a new provider in Romania.

2. Products

The new scheme, which has just entered the market in Romania, is a Sale Model ERS launched in September 2008 where the funds are made available as a regular payment, i.e. the scheme belongs to the life annuity category. In contrast, mainly because of the Romanian banking institutions themselves, Loan Model products do not exist on the Romanian banking market.

Though not ERS, equivalent products such as secondary mortgage loans, called *ipoteca de rangul II* in Romanian, could be offered by professionals such as credit institutions and

331 Research was conducted by our legal expert in Romania, and involved telephone conversations with staff from two financial institutions, email exchanges with the central bank, and consultation of websites such as that of the Association of the Finance Societies of Romania, and Association of Leasing Societies.

332 See Part I: General Report for the narrow definition of equity release for the purposes of this study on ERS.
non-banking financial institutions under the authority and the supervision of the Romanian National Bank (BNR). Based on our research, it can be concluded that such mortgage-based loans are not yet being offered and used in order to enable a consumer, belonging to the category targeted by ERS, to extract liquidity from his/her home. Through the mortgage mechanism, the customers extract liquidity from their homes, but this mechanism does not include certain features enabling the category of customers, targeted by the ERS, to use it.

Another similar product to the Sale Model ERS that exists, namely sale and lease back products for corporations, is offered in Romania by professional providers. These professionals are the leasing companies, but they offer the product exclusively in connection with corporate bodies, for example industrial equipment. Therefore, this product is not offered to extract liquidity from the consumer’s home and thus is outside the scope of this study.

### 3. Providers

In the Romanian market, there is only one provider of ERS in Romania, and because the provider specialising in Sale Model ERS is also actively selling its products in a number of other countries. We have thought it appropriate to give extensive details on the exact nature of the Romanian provider in a text box. There will be similarities in the provider characteristics and product features of HILD subsidiaries operating in those national markets.

#### The HILD Company Group

The HILD Company Group, which describes itself as a provider for financial solutions and support programs for seniors, started operating in Central and Eastern Europe in the year 2004, when it was launched in Hungary. In 2007, it extended its business to Bulgaria; in September 2008, it was launched in Romania, and it is said also to operate in Poland and the Czech Republic.

The company was established in 2004 by American businessmen, John Wirth and Geoffrey Woolley. Internationally, the HILD company group’s stockholder is the American investment bank Merrill Lynch, the second largest HILD stockholder, with 20% of the group’s stock. This institution manages the activity of HILD as member in its Board of Administrators and finances all HILD programs.

HILD Group is present in Romania through SC HILD Management Romania SRL (the company that deals with operational activities in Romania) and SC HILD Asset SA (the company that deals with contracting and managing real estate properties and supplying legal guarantees for the HILD program). Named ‘company of financial solutions’, HILD does not require for its business in the modality the company has proposed it, any authorization from the Romanian National Bank, the Mobile Assets National Commission or the Commission for Supervision of the Private Retirement

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333 From the site of BNR www.bnr.ro and of the credit institutions and of the non-banking financial institutions registered in the registers of BNR.

334 From the site of the Association of the Financial Societies from Romania, www.alb-leasing.ro and of their members; and site of the Association of the Leasing Societies from Romania www.asrl.ro, member of Leaseurope.

335 Information on the provider and the legal framework governing ERS in Romania was collected and shared by Dr. Rodica Diana Apan from North University Baia Mare in Romania. The information about the provider, its offer, procedure and guarantees, is taken from magazines, various websites or the presentation on the Company’s web site, without having access to the Company’s documents.

336 See their respective websites (not in English) under www.hild.hu and www.hild.bg.

337 See a presentation found on the internet at the time of the launch of their product in October 2008: http://www.money-advice.net/media.php?id=3314.
The financial services provided by this group are currently aimed at estate owners over 65 years of age from Bucharest or the county of Ilfov (around Bucharest). Starting next year the Company intends to extend its program nationwide. The Company estimates it will conclude contracts with 6 000 persons worth EUR 600 million in total in Romania by 2012.

a) The offer of SC HILD Asset SA

SC HILD ASSET SA (hereinafter called ‘the Company’) launched the Life Annuity Guarantor Program, through which it offers a monthly life annuity for the rest of their lives to persons over the age of 65 years (hereinafter called ‘the seniors’) and payment of a substantial advance from the actual value of the real estates owned by these seniors, and establishes the seniors’ right to continue living in their owned estates for the rest of their lives.

The Company establishes its offer based on the legal mechanism provided by the Life Annuity Contract.

The seniors automatically become members of the HILD Club (thus gaining access to various activities organized by the Company), are entitled to pay reduced amounts and have access to the services offered by the Company’s partners in the cultural, medical, home care, etc. fields. For example, partnerships have been established with Equilibre Association, which carries out caring programs at seniors’ homes and other social services for the elderly, the Pensioners’ Association from Bucharest, the ‘Princess Margaret of Romania’ Foundation, the Romanian Retired Doctors Association, SensiBlu pharmacy chain, and Generali and BRD-SocGen insurance companies.

b) The procedure followed by SC HILD Asset SA

- assessment of each real estate by an independent assessment company;
- legal advice provided for each senior by a lawyer – either employed by the Company, free of charge for the seniors, or from the public services attached to town halls, or even a lawyer selected by the respective senior;
- when calculating the monthly payment of the life annuity, the Company takes into consideration the value of each home, as well as the age and sex of each senior;
- a psychological test, which is an assessment of the senior’s sanity, is carried out, in order to get confirmation that each senior has taken the decision under his/her own responsibility, but no assessment of the senior’s physical condition;
- the contract is signed before a Notary Public and at the Company’s office;

c) The Guarantees offered by SC HILD Asset SA

- the senior is entitled to use the estate for the rest of his/her life, without any risk of being evacuated or having to pay rent to use the estate.
- in case of termination of the contract due to the Company’s failure to observe the obligations the Company has undertaken through the contract, the senior regains the right of property on the estate, without having to pay back the annuity amounts received until that moment.
- the Company undertakes to pay any costs in connection with the property of the estate, such as taxes, insurance, roof repair.
4. Markets

The size of the Sale Model ERS market will only include a handful of contracts considering that operations have only started in the last quarter of 2008. The reasons why Sale Model products have just now entered the market and why Loan Model products are not yet being offered (or being contemplated by potential providers just yet) is related to the relatively recent development of the financial market and the tradition of homeownership in Romania, as there appear to be no legal obstacles preventing development of these products.

ERS are not regulated as distinct products but, with a view to ensuring and maintaining financial stability, the Romanian Parliament has enacted legislation that regulates minimum access requirements for non-bank financial institutions to lending activity of any kind. The National Bank of Romania is the competent authority in respect of the registration process, regulation and supervision/monitoring of non-bank financial institutions. It is fair to say, therefore, that the providers of credit-based products (including lifetime mortgages and reverse mortgages) are regulated by Romanian legislation.

As already alluded to in Section 2 above on products, the equivalent product that is not ERS, namely sale and lease-back arrangements (those conducted between two private individuals as opposed to those done by leasing companies exclusively to corporate bodies) are offered in Romania. The non-commercial alternative to Sale Model ERS, transacted between private persons is known as lifelong usufruct (usufruct viager), a particular type of usufruct, consisting of the right of habitation (drept de abitatie). The life annuity contract (contract de renta viagera) also exist in the non-commercial alternative. Both alternatives are provided by the Romanian Civil Code\textsuperscript{338}. No figures exist to help estimate the importance of these contracts, however we do not expect them to be significant. Similarly, because outside the scope of this research, no figures are provided for credit with real guarantee in the form of second mortgage loans (ipoteca de rangul II). These loans are offered by commercial lenders, both credit institutions and non-banking financial institutions, with the restriction imposed by the majority of providers that the second charge loan be offered only when the first mortgage (ipoteca de rangul I) is registered in favour of the same provider.

5. Legal situation

The legal mechanism of ERS in Romania can be founded on the life annuity contract (contract de renta viagera). In Romania, no specific regulation has been adopted for the products included in the ERS for seniors\textsuperscript{339}. In Romania, no specific regulation has been adopted for the products included in the ERS, and HILD being the only provider up to this date offering such products on the Romanian market, establishes its offer based on the legal mechanism of ERS in Romania founded on the life annuity contract (de renta viagera). The sedes materiae of this contract are the provisions of the Romanian Civil Code, art. 1639-1651.

\textsuperscript{338} Both lifelong usufruct, which is a particular type of usufruct, consisting of the right of habitation (drept de abitatie), and the Life Annuity Contract (contract de renta viagera) are the non-commercial variant and are provided illo tempore by the Romanian Civil Code.

\textsuperscript{339} In this study, the analysis of the juridical effects that substantiate the ERS legally is carried out only from the legal perspective and not as a result of the analysis of the contract model that the provider proposes to the consumer, and which the research team has not investigated.
a) Landmarks of the life annuity contract in brief

The life annuity with onerous title as the contract through which a person, i.e. the Life Annuitant, alienates a property in exchange for an amount of money—once a year, trimester or month—which must be paid regularly to the Life Annuitant for the rest of his/her life, i.e. until his/her demise, by the person to whom the Life Annuitant transferred his/her property, i.e. the Life Annuity Debtor. The contract can also provide that upon its conclusion an important amount to be paid in advance by the Life Annuity Debtor, the rest of the total amount being paid in instalments, until the death of the Life Annuitant. The legal features of the Life Annuity Contract are as follows: it is aleatory, synallagmatical, bilateral, property translative, with succession execution in times.

b) The effects of the life annuity contract

The Life Annuitant’s obligations are to transfer the title of property in connection with the estate to the Life Annuity Debtor and to make sure the latter enjoys undisturbed possession of the goods, and to guarantee the Life Annuity Debtor against any hidden defects of such goods (the Life Annuitant’s obligations are in this respect identical with a Seller’s obligations in case of a Sales-Buying Contract).

The Life Annuity Debtor’s obligations are to pay an important amount of money, as well as the rental instalments until the terms stipulated by the contract and to guarantee the Life Annuitant of such payments. The parties can also stipulate that the payment should be effected in advance. The rental amount shall be paid to the Life Annuitant throughout his/her life. Based on this provision, the Life Annuitant’s heirs can follow the Life Annuity Debtor for payment of the amounts the Life Annuity Debtor should have paid to their antecessor until his/her death.

In compliance with the provisions of art. 1468 of the Romanian Civil Code, the Life Annuity Debtor can not free himself of the payment of such amounts by offering the property back to the Life Annuitant, irrespective of the length of the life of the person for whom that life annuity was established and irrespective of how onerous the rental payment would be.

c) The formal requirements ad validitatem of a life annuity contract whose subject is a real estate

When the subject of a life annuity contract is the transmission of the property right for a real estate, the requirement is that in order for the respective life annuity contract to be valid it should be in authentic form. To acquire opposability, the contract will be subjected to the real estate publicity procedure.

d) Right of habitation

Another legal mechanism that can form the grounds for ERS is the legal mechanism of the right of habitation - in Romanian drept de abitatie. Sedes materiae of this right are the provisions of the Romanian Civil Code, art. 565-574. Some of the landmarks of the right of habitation are outlined here. The right of habitation is a dismemberment of the right of private property and a particular type of usufruct. Therefore, the right of habitation is subjected to the regulations concerning the usufruct, both in what concerns its definition, and its constitution, exercise and termination. The right of usufruct is defined in art. 517 of the Romanian Civil Code as the right of a person to use the goods that are owned by another person, exactly as if they were their owner, having the

obligation of preserving the substance of these goods. The right of usufruct and therefore the right of habitation as a form of usufruct, can be formed by means of convention, namely through the transmission of the ownership without usufruct or use to another person, the initial owner of the property reserving the right of usufruct – acquirement per *deductionem*. The right of habitation can be instituted through a separate convention or through a written convention including a number of contracts. The right of habitation is always instituted in connection with a real estate, the usufructuary acquiring both possession and the right of using the estate, i.e. both *usus* and *fructus*.

The formal requirements *ad validitatem* of the convention through which the right of habitation is acquired. When the right of habitation is acquired through a convention - *per deductionem* – the formal requirement for the contract to become valid is to be authentic. To acquire opposability, the convention shall be subjected to the real estate publicity procedure.

Even for Sale Model ERS, no special legal provision was adopted in Romania. No license is required for the existing Sale Model products belonging to this life annuity category and their legal mechanism can be legally founded by either of the legal constructions described above or by their cumulation into a single legal construction, the legal institutions being compatible and complementary. As opposed to the situation faced by the provider when it sold Sale Model ERS in Bulgaria\(^\text{342}\), there is no need for the provider to be a registered insurance company.

### 6. Reasons for undeveloped markets

**a) Legal barriers**

Loan Model ERS do not exist in Romania and would not be regulated by the existing Romanian legislation. Banks consider that a possible regulation of ‘equity release’ – type products in Romania would have to take into account both the specificities of Romanian banking legislation, and the aspects regarding consumer protection. However, no specific legal barriers have been identified to suggest that Loan Model ERS could not be marketed if providers decided to offer it.

There are no subsidies or governmental promotions of ERS. No articles were provided in the legal doctrine with respect to the subject of ERS, and the academic environment has not made any calls that government should carry out any particular legislative initiatives in this area. One respondent, a legal expert, is nevertheless intending to initiate the juridical doctrine for ERS in Romania by publishing an article on the subject soon.

It is too early to evaluate the risks, the cultural reactions, the economic success etc. of a product that has only been offered on the market since less than a month.

\(^{342}\) See Country section on Bulgaria (on p.113).
XII. Bulgaria

1. General Information

<table>
<thead>
<tr>
<th>Category</th>
<th>Bulgaria</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>96.5</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>27.4</td>
<td>9.2</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>2.9</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>64.4</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>9.9</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>370</td>
<td>7820</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>7.6</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>-14.5</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>25.0</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>17.3</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
<td>1</td>
<td></td>
</tr>
</tbody>
</table>

| ERS Market?                                         | Sale Model less developed |

2. Providers

The only provider recorded with a product is HILD, a real estate specialist that offers a Sale Model ERS. A description of the company providing these products can be found in the country section above on Romania (where a subsidiary of the HILD Holding Group is also active\(^{343}\)).

3. Markets\(^{344}\)

Responses from Bulgaria were low and the Central Bank and others have confirmed that no statistics on the volume of Sale Model ERS is available for Bulgaria.

4. Legal situation

a) Sale Model ERS

Below is an outline of the current legal framework for the products which are more or less variations of the ‘sales contract’.

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\(^{343}\) See Country section on Romania (on p.112).

\(^{344}\) The Central Bank of Bulgaria and the Financial Supervision Commission both participated in responding to our study, but after uncertainty about who had the competency to answer our survey, neither was able to provide a completed questionnaire.
Bulgarian legislation allows ‘sale and lease back’ arrangements as well ‘sale and keep the right for lifelong maintenance and occupancy’ arrangements. Those contracts are concluded under the provisions of general civil legislation (Law on Obligations and Contracts). There are no legal barriers for conclusion of such contracts, nor executive body to regulate civil relations under the contracts. In case of non-performance of the obligations and/or breach of the rights under the contracts, the cases go to the court for ruling.

Regarding the ‘sale arrangements as insurance products’, the Bulgarian Insurance Code, in art. 230 a (under the title "Retirement or annuity insurance") regulates contracts concluded by the nature of trade and containing operations for acquisition of real rights in real estate through payment of life or term pension or rent. The Code presumes that in the cases of ‘sale arrangements as insurance products’, a transfer of real rights shall be accepted as payment of insurance premium. The product consists of most of the elements of a ‘home reversion’, but the ‘right of lifelong occupancy’ is not given as a mandatory element under the mentioned definition in Bulgarian Insurance Code.

The Bulgarian Financial Supervision Commission (FSC) took a decision on the case with HILD’s business in Bulgaria and concluded that this business reliant on the Sale Model schemes requires an insurance license. Unfortunately, the FSC was not able to provide further explanations on this issue or similar cases.

b) Loan Model ERS

These credit-based ERS do not exist in Bulgaria. The legal framework regarding such ‘mortgage reversion arrangements’, the Bulgarian Commerce Code, has a ‘bank credit’ defined in art. 430 as a contract under which a bank shall be obliged to provide to a borrower a sum of money for a certain purpose and under agreed conditions and terms, and the borrower undertakes to use the sum as agreed and to return it (the principle) as well as to pay interest on the credit, as agreed with the bank. It is not allowed under the Law of Obligations and Contracts (art. 152) to be agreed in advance in the contract that if the obligation is not performed, the creditor shall automatically become owner of the property, nor any other agreement which stipulates in advance a manner for satisfying the creditor other than the one provided for by the law. Otherwise, the contract is considered invalid by virtue of the law. This means that the normal procedure to enforce a claim secured by a mortgage has to be applied and there is, what is typical for all European legal orders, no way to get around the procedures of foreclosure by anticipating a transfer of property in case of default.

Bulgarian law has no objections to the selling of reverse mortgages as second mortgages where there is a first charge claim on the property and repayment of the loan is planned out of the sale of the property when the borrower dies. The sale of the mortgage under such specific circumstances is a matter of a particular bank’s policy. Banks are simply not interested in developing such products at the current time.

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345 The controversy over services being offered that are similar to those of an insurance company without the registration of the provider was reported by the media. E.g. http://paper.standartnews.com/en/article.php?d=2007-11-02&article=7312.
Group 4: Member States with no ERS

XIII. Belgium

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Belgium</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>78.0</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>9.8</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>19.9</td>
<td>20.6</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>121.8</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>6.8</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>36.8</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>11530</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>63.0</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>36.7</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>1173</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>10.7</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>11.7</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>25.8</td>
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</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>17.0</td>
<td>16.2</td>
</tr>
<tr>
<td>ERS Market?</td>
<td>No market</td>
<td></td>
</tr>
</tbody>
</table>

Belgium has one of the highest levels of owner-occupation in the EU with recent 2007 data putting the figure at 78%. Over the last 10 years, individual mortgage debts have more than doubled and the volume of mortgage credit outstanding as a percent of GDP has also almost doubled over the same period, going from 19.5% in 1998 to almost 40% in 2007. The average amount of new mortgage loans for house purchase has been growing from EUR 67 000 in 1998 to EUR 126 000 in 2007346. Private universal banks have provided about 95% of mortgages until now and falling interest rates and tax deductible mortgage payments throughout the 1990s saw the number of new mortgages more than triple over that decade, a significant share of which were in fact remortgages taken out to withdraw some of the equity accumulated as a result of house price appreciation.347 Nevertheless, lending rules in Belgium are particularly mindful of

protecting the consumer from any over-commitment and unnecessary exposure to the risk of overindebtedness.

2. Markets, products and providers (none)

ERS do not exist in Belgium. The level of information on ERS made publicly available is very low, with minimal media coverage. Only a small quantity of academic studies, and guides and leaflets, have featured the subject of ERS, and then almost only with references to the Loan Model or reverse mortgages.

In terms of the use of ERS, Loan Model products are currently not commercialised due to legal barriers described below. For Sale Model products – the only system that falls into this category is the ‘verkoop op lijfrente / vente en viager’ – ‘sale with life annuity’. In this system, the property is sold but (part of) the price is not paid at the time of the sale but in monthly instalments. There are some provisions in the Civil Code with regard to these contracts (art. 1968 et seq. C.C.), but there is a lot of contractual freedom. Often part of the price will be paid immediately, and the rest in instalments. The obligation to pay instalments ceases to exist when the person determined in the contract deceases. When immovable property is sold in this way, a notary needs to execute a deed. It is also possible to limit the obligation pay instalments in time. Such contracts are aleatory contracts. The seller is secured by a mortgage on the property. The seller immediately ceases to be the owner and this normally also implies the loss of the right to occupy the property. To avoid this consequence, it is possible only to sell the bare ownership of the house and to retain the usufruct. The instalments will then be lower. These products are not commercialised on a large scale by mortgage credit undertakings. There is a profitability problem, a problem of high administration costs and the aleatory character. The aleatory element and the fact that the property of the house immediately goes to the buyer who may obtain the property at a low price if the seller deceases quickly also makes such contracts not unpopular with heirs.

The system based on ‘viager’ from private to private has existed for centuries. Data on these private activities usually exercised through notaries are not available and do not seem to be significant enough to give details about.

a) Preparatory legal discussion

(1) Relevant legislation

The Act of 4 August 1992 on Mortgage Credit applies to credit contracts secured by a mortgage or similar security on immovable property and primarily intended for the acquisition or retention of rights in immovable property. The borrower must be a natural person mainly acting for non-professional purposes (art. 1-2 of the Act). An ERS would normally not fall under the provisions of the Act as the aim of the credit will often be other than the acquisition or retention of rights in immovable property.

The Act of 12 June 1991 on Consumer Credit applies to credit agreements granted to a consumer. All agreements that fall under the Mortgage Credit Act are, however, excluded from the scope of application of the Consumer Credit Act. Credit agreements secured by a mortgage, but not (primarily) intended for the acquisition or retention of rights in immovable property (e.g. health related expenses, travelling, ...) – as will often be the case in an ERS – would thus fall within the scope of application of the Consumer Credit Act. Certain provisions of the Act do not apply to credit contracts above EUR 20 000 and for which a notary has drawn up a deed (art. 3 Consumer Credit Act). These provisions

346 See the next section 3 on the legal barriers to ERS in Belgium (on p.118).
also have as a consequence that second mortgage loans may well fall under the scope of application of the Consumer Credit Act.

The Consumer Credit Act has detailed provisions on publicity, pre-contractual information, responsible lending, prior consultation of the credit register, unfair contract terms, early repayment, etc.

(2) Discussion in literature

The discussion in literature on ERS exists but the number of articles on the subject is limited. A number of seminars dedicated to the subject were nevertheless organised recently:


The banking sector is in favour of introducing ERS in Belgium when accompanied by an adequate legal framework. It is pointed out that the OECD in its March 2007 report on Belgium advised in favour of the introduction of these products in Belgium. It is further stressed that in the absence of a specific legal framework in Belgium, Belgians may seek to buy these products abroad. The Organisation for Credit Undertakings (Beroepsvereniging voor het Krediet) has made a proposal to the government for new legislation that would provide for a legal framework for ERS. This proposal is discussed below.

The main Belgian consumer organisation Test Achats is opposed to ERS and thinks that the disadvantages outweigh the advantages. They argue that introduction of new products would only render it more complex for the consumer. If the introduction of ERS were nevertheless considered, Test Achats wants pre-contractual obligations of information and advice and transparency requirements. Similar scepticism exists with OIVO – another consumer organisation.
3. Reasons for undeveloped markets

a) Legal barriers

Neither the Consumer Credit Act, nor the Mortgage Credit Act currently provide a suitable framework for ERS; in addition the provisions or the Civil Code on mortgages as well as compound interest make Loan Model ERS currently impossible.

(1) Consumer Credit Act

There is inter alia the obligation to provide for a maximum period of time within which the amount borrowed must be reimbursed if the contract is concluded for an indefinite period and does not provide for periodic reimbursement (art. 22 §2). The act does not provide for the possibility to make repayment dependant on death or vacation of the property; the obligation to consult the credit register does not give an indication on the risks involved in ERS, consultation of the credit register gives an indication of the creditworthiness, which is not directly relevant for ERS as there is no repayment schedule.

(2) Mortgage Credit Act

Compound interest is restricted under the current legal provisions:

Art. 10 Mortgage Credit Act only provides for interests calculated on the principal sum outstanding. Art. 1154 Civil Code currently limits the possibilities to compound interest. It is only possible to compound interest if:

- the interest was due on an outstanding capital;
- the interest was due and for a period of minimum one year;
- if such demand to compound the interest is either concluded in a specific contract or is the object of a judicial summons.

Interest on compound interest will only be compounded if the agreement or summons is renewed and concerns the new interest that became due and this over a period of one year minimum (art. 1154 B.W.).\textsuperscript{355}

Other provisions or the Mortgage Credit Act are similarly considered unfit for ERS, such as the provision limiting the compensation for early repayment to three months interest,\textsuperscript{356} the obligation to consult the credit register,\textsuperscript{357} and the provision granting the borrower the right of (complete) early repayment at all times.\textsuperscript{358}

(3) Mortgage Act – Title XVIII Civil Code

**Amount:** The provisions of the Civil Code that determine how mortgages are to be registered all presume the secured sum can be determined in advance.\textsuperscript{359} As this would depend on the sums actually taken out, several provisions would need to be amended.\textsuperscript{360}


\textsuperscript{356} See Article 12 § 1 Mortgage Credit Act.

\textsuperscript{357} See Article 9 Act 10 August 2001 on the Credit Register.

\textsuperscript{358} See Article 26 § 1 Mortgage Credit Act.

\textsuperscript{359} See Mortgage Act – Title XVIII Civil Code.

\textsuperscript{360} See Art. 80, 1st para., art. 83, 4th para. Mortgage Act.
Although it is possible to under Belgian law to grant a mortgage that covers future debts ('mortgage for all sums' – art. 51 bis Mortgage Credit Act), the maximum amount of the mortgage, and thus of the debts secured should be determined in advance.

**Limited Lifetime of a Mortgage:** The current legislation provides that when interest is due on a principal sum, the lender can only benefit from the mortgage for a period of three years for those interests\(^\text{361}\).

**Maximum period for mortgages:** There are provisions for a maximum duration of 30 years for mortgages\(^\text{362}\). This provision is also considered problematic for ERS as a longer period may be needed during which the debt is secured, without incurring extra costs.

**Early repayment:** Both if the agreement would fall within the scope of application of the Consumer Credit Act and of the Mortgage Act, the fees that can be charged by lenders in case of early repayment are capped (cf. max. two / three months of the total cost of the credit, depending on the amount of the credit - art. 23 Consumer Credit Act; maximum three months interest - art. 12 Mortgage Credit Act). This is considered insufficient by the industry in case of ERS,\(^\text{363}\) as a larger number of uncertainties play a role in case of ERS (evolution of the market for immovable property, and of the price of the property itself, uncertain duration of the contract). Three months of the total costs of the credit are considered insufficient to compensate such risks, and the risk of early repayment would then have to be reflected in the interest rate charged, which in turn would have an influence on the capital that could be lent.

(4) **Tax Law**

The costs of ERS would be extremely high at present (relevant provisions: art. 87, 93, 262, 263 Code on registration and mortgages taxes and court fees).

A registration tax of 1% is due when a mortgage is granted (art. 93 Code on registration and mortgage taxes and court fees). In addition, there is a mortgage tax of 0.30% and there is the fee of the notary for the execution of the deed. These taxes and fees are normally determined on the basis of the amount secured. This is problematic in case of ERS as the amount to be secured cannot be determined in advance.

In addition, the costs of ERS could be very high as interest would be compound, thus increasing the amount secured.

Finally, whereas for standard mortgage credits, a mortgage is usually not taken out on the total amount borrowed, it would be necessary to secure the total amount by a mortgage in case of ERS – thus increasing the costs.

The credit industry therefore pleads for special rules on costs for ERS.\(^\text{364}\) The current costs would have a discouraging effect.

b) **The Legislative proposal to overcome legal barriers**

There is presently a proposal discussed that was made by the industry in a memorandum to the government. This proposal has not been made publicly available and the

\(^\text{361}\) See Art. 87 Mortgage Act - Title XVIII Civil Code.

\(^\text{362}\) See Art. 90, lid 1 Mortgage Act - Title XVIII Civil Code.


government has not yet reacted to it. It also has not yet been discussed in the Consumer Council (Raad voor het Verbruik) – where both consumers and the industry are represented.

The proposal proposes to adapt the Mortgage Credit Act rather than to adopt a separate act or to amend the Consumer Credit Act. The Consumer Credit Act is deemed not appropriate to deal with ERS due to the complex nature of the service.

(1) Scope of application

Under the proposal made by industry, the same companies that are now allowed to grant mortgage credit ('mortgage credit undertakings') in the sense of art. 37 Mortgage Credit Act would be allowed to commercialise ERS. This also would include insurance companies. The prudential requirements and supervision that applies for mortgage undertakings would also apply to ERS.

According to the proposal, ERS would be restricted to people acting primarily or exclusively for non-professional purposes365. ERS would be possible for the habitual residence.

(2) Overview of the main provisions of the proposal

Independent advice: The proposal provides for a prior consultation with a public notary. According to the legislation in force, a public notary is obliged to provide independent advice and to point out the rights and obligations arising from an act before drawing up a deed366. The proposal made by industry suggests that the borrower would be able to waive this obligation of a prior consultation.

Information provided by the creditor: The current Mortgage Credit Act provides for an obligation to hand over a written offer to the borrower with all contractual conditions and the duration of the offer. Such obligation would also be provided for ERS according to the proposal. The proposal moreover sets out what information should be given in this offer. The current provisions of the Mortgage Credit Act would be amended to accurately reflect the different nature and modalities of ERS.

Cooling off period: The proposal also introduces a cooling off period for ERS (currently non-existent for mortgage credit). The borrower who signed an ERS contract could still withdraw from the contract as long as a public notary did not draw up the deed. The obligation to consult the notary before the act is passed has to be seen in this regard and indeed only makes sense if the borrower is still able to withdraw from the contract.

The borrower/credit taker would, however, be charged with the administrative costs and valuation charges.

Valuation: Before the conclusion of the credit agreement, an independent expert appointed by both parties will valuate the property. Further specifications would be necessary as to the qualifications of the expert. The proposal provides for further detailed rules on the appointment of the expert.

Monitoring: The possibility to monitor whether the value of the good is preserved or increased is considered crucial by the credit industry. The proposal therefore provides

365 Though the paper by Heymans (fn 349) mentions that these products are not considered suitable for young persons, in other texts, it is mentioned that an age limit may be contrary to the non discrimination law and should perhaps be left out.

366 Art. 9 § 1 Act of 25 Ventôse year XI on public notaries.
that the creditor has the right of access to the good to inspect whether the good is well preserved.

**Capitalisation of interests:** Interests would be capitalized on a yearly basis (amendments of the current legislation would be necessary in this regard – cf. supra - current restrictions on compound interest).

**Costs and charges:** Certain costs would be incorporated in the interest rate, other costs would be reflected in separate charges. The latter would include non-recurrent charges (a charge for drawing up the deed, a charge in case of early repayment, a charge for not taking up credit, a charge for administering the file, a valuation charge).

**Termination of the contract:** The contract would end in case the borrower dies or moves. The contract could provide for specific reasons to end the contract (such as a failure to preserve the property). The termination of the contract would render the amount borrowed due. A specific procedure for recovery would be provided for. The borrower (or his heirs) has the right to reimburse the outstanding debt by paying the value of the property at that time. The value will be determined in common agreement by the parties. The proposal provides for specific provisions (derogating from the actual provisions on recovery) with short time periods:

- absent an agreement on the value of the good within a period of maximum 3 months and forty days from the termination of the agreement, or;
- absent payment of the value agreed upon within a period of nine months form the termination of the agreement,
- the lender can sell the property.

The proposal also deviates from the current article 59 of the Mortgage Credit Act that provides for obligatory mediation as this is considered to prolong the procedure unnecessarily. Any surplus is for the borrower or his heirs.

**c) Cultural barriers**

Cultural or sociological factors were not mentioned as playing a particular role in obstructing the development of the market. The economic (business incentive) and financial (consumer demand) factors were seen as highly significant, though naturally the biggest hindrance to the product development is the legal framework making it illegal at present.

**4. Risks and benefits**

The concept of ERS is being promoted by trade associations representing the financial services providers. As no products exist, consumer risks and benefits can be assumed similar to those outlined in the general section of the report\(^{367}\). However, responses have shown that the risk of a family dispute of inheritance was an issue for concern.

A response was received however, that the level of financial education was especially relevant for ERS compared to other more traditional financial services, and a severe warning was placed on these Loan Model products by the consumer association\(^{368}\).

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\(^{367}\) See Part I: General Report D.III.

\(^{368}\) This was made clear at the presentation made by Test Achats at their seminar on reverse mortgages on 18 April 2008.
XIV. Malta

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Malta</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
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<td>75.0</td>
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<tr>
<td>House prices (average annual % change 2003-2007)</td>
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<td>9.2</td>
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<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>2.0</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>14.2</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>37.6</td>
<td>34.9</td>
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<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>4940</td>
<td>7820</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>81.8</td>
<td>65.2</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>0.4</td>
<td>9.2</td>
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<tr>
<td>Population growth (% 2008-2035)</td>
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<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>19.8</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>13.8</td>
<td>16.2</td>
</tr>
<tr>
<td>ERS Market?</td>
<td>No market</td>
<td></td>
</tr>
</tbody>
</table>

The characteristics of Malta’s national housing market will also affect the future development of the ERS market. The majority of Maltese residents are homeowners. Mobility is not a very relevant factor in Malta. Rising house prices could lead to first time home buyers to initially purchase affordable small apartments from which they would probably choose to move after a number of years. Most people buying a new home for the first time usually borrow funds in the form of a mortgage referred to as a ‘hypothec’\textsuperscript{369}. Due to the particular characteristics of the legal provisions in this regard, it would seem that the rental market mainly attracts foreigners. Some statistics from the National Statistics Office for 2005 show that there are 75% Homeowners (55% Freehold: 20% having Ground Rent), 20% Tenant Occupancy, 5% Other.

2. Markets, products and providers (none)

ERS are not offered in Malta according to the definition laid out for this study. However, products that resemble Loan Model ERS but are in actual fact simply traditional ‘forward’ loans are provided to consumers who agree to use their housing asset as collateral for obtaining the loan\textsuperscript{370}. Because these secured loans can be either be an alternative source of liquidity for certain population groups (though not primarily the elderly) or facilitate the market conditions for the future appearance of actual ERS, they are briefly outlined in this section.

\textsuperscript{369} See Articles 1994 - 2095 of Title XXXIII (Privileges and Hypothecs) of the Civil Code (Cap. 16).

\textsuperscript{370} Despite the non-existence of ERS in Malta, one provider in that country did reply to our questionnaire but with the following definition of ERS in mind “An Equity Release Loan is considered to be a ‘Second Mortgage Loan’ for consumption with a repayment schedule and having a maturity date”.
Two banks in Malta have loan products based on the second charge on a mortgage claim but these are not widespread and as such have only lately started being offered to customers by licensed institutions. The Malta Financial Services Authority (MFSA - the regulatory authority for all financial services in Malta) does not have specific data available as there are no regulatory returns/schedules which have been specifically tailored for the reporting of such products. The number of second mortgage related loans and the total amount involved are still rather insignificant when compared to these banks' credit portfolio. Despite the early stage this product has reached in Malta, given the product's development in other countries, there also appears to be scope for growth within the Maltese market. Similarly, based on other countries' experience, the main factor leading to the emergence of ERS will probably be an ageing population.

Malta does not have a specific definition of an ERS in its legislation and therefore there is no ERS specific regulation in Maltese legislation. Very little material is published on the subject even if media commentary and some leaflets exist.

In terms of complaint handling, as with every financial product / service available in the Maltese market, the MFSA has a Consumer Complaints Unit (CCU) which receives complaints that consumers may have in relation to products / services offered by licensed institutions. The CCU, whose role is that of a mediator, tries to deal with such complaints and to arrive at an equitable solution to problems which arise. However, the CCU's recommendations are not legally binding. Naturally, if there is no agreement with regards to a complaint, the customer can still take further redress action as deemed practicable in the circumstances to obtain compensation. More information on the role of the MFSA’s consumer complaints redress mechanism is available on its website. The MFSA’s Consumer Complaints Manager is a member of FIN-NET.

3. Legal situation

   a) Loan Model ERS

Currently, there is no Maltese legislation that specifically regulates Loan Model equity release products. Nonetheless, it is submitted that particular areas of legislation would nonetheless regulate aspects of such products as well as some of the terms and conditions upon which they are to be provided.

No special definitions for an ERS-like product can be found under Maltese law. They are considered to be an off-shoot of loan and accordingly regulated by the Civil Code. Furthermore, the terms and conditions of loans are governed by the Consumer Credit Regulations.

(1) Contract Law

Loans for consumption (referred to under Maltese Law as 'Mutuum') are defined in article 1842 of the Civil Code as "a contract whereby one of the parties delivers to the other a certain quantity of thing which are consumed by their use subject to the obligation of the borrower to return to the lender as much of the same kind or quality"\textsuperscript{371}. The requirement that loans for consumption must have as their object a thing that can be consumed distinguishes this form of loan from other types of loan, such as the loan for use (referred to as 'Commodatum').

A loan for consumption is concluded upon the delivery of the fungible object, so much so that the loan does not exist until the thing lent is delivered. Mutuum therefore transfers the ownership of the object to the borrower.

\textsuperscript{371} See Civil Code, Chapter 16 of the Laws of Malta, Art. 1842.
The borrower is under an obligation to return to the lender as much of the same kind or quality of the fungible object. The time and place of restitution are regulated by the agreement of the parties. If this is not agreed upon, it is up to the Court to establish the term.\(^{372}\) Article 1078 of the Civil Code also provides that if the time for payment is left to the debtor and the subject of the loan is money, then the term shall be of two years if the sum is due without interest or six years if the sum is due with interest.\(^{373}\) Where time has been agreed upon the law provides that the lender cannot claim the loan back before the expiration of such time.\(^{374}\)

**Mutuum** is considered by default to be a gratuitous contract.\(^{375}\) Interest however can be agreed upon between the parties. The law stipulates a maximum rate of interest of 8%\(^ {376}\) and allows compound interest provides that such interest be not due for a time less than a year.\(^{377}\)

The law permits loans at rates beyond 8% when such loans are made by credit and financial institutions.\(^ {378}\)

A loan entered into under the above provisions is generally accompanied with a security for repayment taking the form of a general hypothec by virtue of which the borrowers secure the restitution of the capital and interest with their property present and future and a special hypothec or special privilege over a specific immovable.\(^ {379}\) Whilst **mutuum** can be expressed tacitly and therefore may be unwritten, a hypothec may only be created by public deed.\(^ {380}\)

It is submitted that, lacking specific legislation on the matter, a Loan Model ERS (or reverse mortgage) would be regulated in accordance with the civil law provisions mentioned above relating to loans for consumption (**mutuum**).

In addition to the Civil Law provisions, additional safeguards are provided also by general consumer legislation, in particular article 44 of the Consumer Affairs Act which prohibit certain unfair terms in consumer contracts. A reverse mortgage provided to an individual who acts for purposes not related to trade, business or profession would invoke protection of the said Act.

(2) Bank licensing

Loans provided by banks are generally authorised and approved by the home loans office of the respective banks. The applicant normally is required to provide proof of ownership of the collateral and a statement of income which will subsequently form the basis of repayments.

Whilst specific restrictions on advertising relating to equity release loans per se do not exist., principles of best practice requiring that adverts should be fair, clear and not misleading would have to be adhered to. In this light, the relevant provisions of the Consumer Affairs Act, Chapter 378, are also to be complied with.

\(^ {372}\) See Ibid., Art. 1848(2).
\(^ {373}\) See Ibid., Art. 1078.
\(^ {374}\) See Ibid., Art. 1072.
\(^ {375}\) See Ibid., Art. 1849.
\(^ {376}\) See Ibid., Art. 1852.
\(^ {377}\) See Ibid., Art. 1850.
\(^ {378}\) See Ibid., Art 2025.
\(^ {379}\) See Ibid., Title XXIII.
\(^ {380}\) See Ibid. Art 2025.
The Banking Act, chapter 371, the Financial Institutions Act, Chapter 376 and the Insurance Business Act Chapter 403 are significant to the provider of equity release products taking the form of lifetime loans. In the event that such lender raises the funds for the said loan products by accepting deposits on a day to day basis from the public, then such activities could constitute ‘banking’ in terms of the Banking Act and would require licensing and be regulated according to the said Act. Similarly, where the said funds are raised from other financial institutions or from other professional market parties such as institutional investors and insurance companies, and where the person undertakings the carrying out of loans, then such person may qualify as a ‘financial institution’ under the Financial Institutions Act. Finally, depending on the nature of the reverse mortgage, it is possible that the equity release plan be interpreted as a class of long term business of insurance relating to ‘life and annuity’ described by Schedule II to the Insurance Business Act as the effecting and carrying out contracts of insurance on human life or contracts to pay annuities on human life.

(3) Consumer Law

According to Article 7 of the Consumer Affairs Act, the Minister is empowered to regulate consumer credit offers and the conclusion of agreements for the provision of credit terms and facilities and to stipulate and regulate the terms and conditions that may or may not be adopted in such agreements. In accordance with his powers under this Article, the Minister published the Consumer Credit Regulations of 2005.

Significantly, despite being based in the large part on the Consumer Credit Directive (87/102/EEC), the said Regulations provide that the articles of the Directive are also applicable to ‘home loans’. The Maltese Regulations, on the other hand, define a creditor as a trader who grants credit in connection with the supply of goods or services to consumers, or in connection with home loan agreements. A ‘home loan agreement’ is in turn defined as a credit agreement whereby the consumer may purchase, reconstruct, alter or improve immovable property for his own residence or that of his dependants and which is secured either by a hypothec or similar right or charge howsoever described on an immovable property, or by a surety.

The Regulations provide that, prior to the conclusion of a home loan agreement, the creditor shall be obliged to provide the consumer with the general pre-contractual information listed in the Schedule to the Regulations, together with a personalised standard information sheet in a specific format also provided in another Schedule to the Regulations. In the agreement itself, the creditor is to provide for the right of the consumer for a reduction if he pays credit before it is due, a clear description of the security provided to the creditor, a clear indication of costs for breach of contractual obligations and a clear statement of fees (including costs of legal services).

The Regulations do not apply to home loan agreements where the amount exceeds one hundred and eighty-six thousand and three hundred and forty-nine euro and eighty-seven cents.

381 See Consumer Affairs Act, Chapter 378 of the Laws of Malta, Art. 7(f).
382 See Consumer Credit Regulations, LN 84 of 2005.
384 See Consumer Credit Regulations, LN 84 of 2005, Reg. 2.
385 See Ibid.
386 See Ibid., Reg. 5.
387 See Ibid., Reg. 7(1)(f).
It is submitted that a reverse mortgage could likewise be regulated by the Consumer Credit Regulations if the reverse mortgage satisfies the definition of ‘home loan agreement’. In this respect, it would be necessary to assess whether the borrower intends to or at least may possibly utilise the loan for the purchase, reconstruction, alteration of his or his dependants’ immovable property.

As with other financial products, the service provider itself has to provide all the requisite pre-contractual information to the prospective customer in order to ensure that an informed decision about which product is best suited to the individual’s requirements is taken. As far as Malta is aware, no one else at the moment, but may be provided by licensed intermediaries.

Whilst there is no specific restriction on the advertising of ERS, any related advertising has to be within the best practice guidelines promoted by the MFSA and addressed to credit institutions.

b) Sale Model ERS

(1) Civil code

In this case, the home is actually sold, normally at a discount in return for a lump sum payment and, or regular income coupled and the right to continue living in the home until death or until the seller moves out of the home.

It is submitted that such a sale would be regulated by the normal civil law provisions relating to sale of immovables\(^\text{388}\). The lump sum payment would in turn be considered as part of the sale price and the regular income could be considered also as deferred payment of the said price or as the creation of a life annuity regulated by article 1706 of the Civil Code. The right to continue to live in the home until death or until vacation of the home would qualify as a right to usufruct, or use or habitation regulated by Title III of the Civil Code.

(2) Consumer Affairs Act

Even in the case of Sale Model ERS, in addition to the Civil Law provisions, reference need also be made to general consumer legislation, in particular article 44 of the Consumer Affairs Act which prohibits certain unfair terms in consumer contracts.

4. Reasons for undeveloped markets

a) Legal barriers

(1) Prudential regulation

To date it does not appear that prudential regulation imposes a maximum duration on mortgages or any limitations on home reversion plans. Furthermore, it does not appear that ERS necessarily require insurance, banking or financial institutions licences. As stated above, it is only when these said schemes qualify as insurance business, banking or activities of a financial institution under the relevant legislation that a licence application need be filed and that prudential legislation need be complied with.

Nonetheless, due to lack of specific legislation and rules or directives by the Malta Financial Services Authority in this respect, there could be a degree of legal uncertainty

\(^{388}\) See Civil Code, Chapter 16 of the Laws of Malta, Title VI.
as to which specific types of schemes would be considered to be subject to the aforementioned areas of prudential regulation.

(2) Private Law

Potential Barrier of Early Termination – As mentioned above, the Civil Code provisions on loan for consumption provide that where the time for repayment has been agreed upon, the lender cannot claim the loan back before the expiration of such time. It is believed however that this limitation should not affect significantly the profitability and risk of an equity release product.

Potential Barrier of Compound Interest – The Maltese Civil Code allows compound interest provided that such interest shall not be due for a time less than a year.

Potential Barrier of Amortisation – There is no Maltese legislation relating to required amortisation that prevents lenders in Malta from offering ERS.

Potential Barrier of Lack of Data for Risk Evaluation – Lenders routinely carry out public and land registry searches on the borrowers to ascertain creditworthiness of the borrowers and good title on the property. Architects normally provide appraisals as to the creditworthiness of the real estate itself. In the event that the sale realises insufficient funds, the borrower or his heirs would not have returned “to the lender as much of the same kind or quality” as required at law and therefore the borrower (or his heirs) would be personally liable to pay the balance. For this reason, it is submitted that lack of data for risk evaluation is not a significant barrier.

Potential Barrier of Transfer of Title – In the case of Sale Model ERS, the sale would occur upon the conclusion of the equity release agreement but would be coupled with a right to usufruct, use or habitation on the property sole in favour of the borrower. A reverse mortgage on the other hand requiring conditional transfer of title could take the form of a sale subject to a suspensive condition regulated under article 1063 of the Civil Code. It could also take the form of a promise of sale also subject to a suspensive condition.

Potential Barrier of Transfer of Sureties – under Maltese law a security in the form of a privilege or hypothec may be ‘transferred’ to a third party by payment by subrogation regulated by article 1164 of the Civil Code. In this case, the third party pays the original lender and is subrogated in the rights of the original lender. The advantage of this procedure is that the third party retains the ranking of the original lender. This is common practice when for example a bank takes over a loan previously given by another bank.

Potential Barrier of Mortgages in respect of Future Debt – Article 2027 of the Civil Code provides that a conventional hypothec is not valid if the sum for which it is agreed upon is not specified and stated in the deed. If the debt resulting from an obligation is conditional as to its existence, or indeterminate as to its value, the creditor cannot demand the registration of the hypothec except for an amount expressly stated by him, saving the right of the debtor to cause such amount to be reduced, where competent. It is not therefore possible to demand registration of hypothecs for future indeterminate debts.

389 See Ibid., Art. 1072.
390 See Ibid., Art. 1850.
(3) Tax Law

It does not appear that there are currently any tax incentives under Maltese law that encourage the use of the home to enhance the income of the elderly or the disabled.

(4) Bankruptcy Law

Bank guarantee schemes in Malta are implemented by means of the Depositor Compensation Scheme Regulations, Legal Notice 369 of 2003, as amended by legal notice 35 of 2006. Article 13 of the Regulations provides that where it appears to the competent authority that a participant is unable, for the time being, for reasons which are directly related to its financial circumstances to meet its obligations arising from claims by its depositors and seems to have no early or foreseeable prospect of being able to do so, or has otherwise suspended payment or where an order has been made by the Courts of Malta for the winding-up or liquidation of a credit institution, the competent authority shall make a determination to that effect within twenty-one days of the occurrence of such circumstances.

On being informed by the competent authority that a determination has been made under regulation 13(1), the Management Committee of the Compensation Schemes shall publish a notice in at least two local newspapers, informing depositors of the credit institution concerned of such determination and of the manner in which claims supported by documentary evidence are to be submitted.

It is immediately noticeable that the wording of the Regulations seems to imply that compensation schemes are available exclusively to ‘depositors’ and not generally to consumers of the credit institution. Arguably, therefore a borrower, including a borrower under a Loan Model ERS, would not be able to make a claim for compensation under the Regulations since such a borrower would not, at least in the context of his loan, be considered a depositor.

b) Economic barriers

Maltese providers who replied consider the economic risk of non-repayment in the case of second mortgages as substantially high. In fact, the providers generally require property and life insurance cover to secure the loans. Continuous monitoring is effected on all lending. Furthermore, the value of collateral items is also reviewed.

The biggest risk to the consumer was seen as loss of income but this is because the respondent was not replying for an ERS but a second mortgage product where repayments are due throughout the term of the loan.

There are costs associated with legal searches relating to ascertaining good title of the borrower on the property to be secured by hypothec or privilege. It has been observed that Maltese public registry and land registry search costs are relatively high when compared to other countries. Nonetheless, it is also noted that such costs do not seem to have created an economic barrier to borrowers taking first time home loans. It is submitted that the costs should likewise not constitute a significant barrier to a person availing of equity release products.

391 Because of the non-existence of ERS in Malta, responses were more related to second mortgages than ERS as such.
392 Abela Delicate, Francoise: Home Loans: Civil and Bank Law Perspectives, p.29.
c) Cultural barriers

According to a survey carried out by the Malta National Statistics Office entitled 'Perceptions on Retirement and Pensions’ of 2005, only 1.5% of the respondents view property as a possible source of retirement income. Interestingly, none of these respondents were from the age groups of 18-24 and 55-64. It has been argued that a possible reason for this is that the older group is more attached to their property and would traditionally pride themselves in leaving inheritance, including houses, to their children or to their immediate family.

5. Recommendations of a Maltese expert group on ERS (2005)

A government expert group has explored the possibilities of introducing ERS in Malta in order to improve the pension systems. Their conclusions summarise the existing obstacles and threats especially with regard to the UK ERS Market which had been explored in depth before. The summary reads:

"Most housing wealth is different from other forms of wealth or savings. The impact of use of property for retirement income is uncertain and would be unevenly distributed:

- There are various reasons while people may not want to release equity locked in their property.
- Even if equity in property is released, it will not necessarily be channelled towards funding retirement income but may be used to finance other purchases or other needs such as health care.
- In addition, the spread of wealth including housing wealth is likely to be uneven and unequal. Variation in house values and holdings of dwelling types among income earners leads to wide variations in the amount of property equity that can be released by different categories of people.
- Moreover, equity in property has a fluctuating value like other investments despite the general idea that property prices do not go down in Malta.

It is thus considered that savings in property and housing assets should not be considered as a substitute to other supplementary forms of Second and Third Pillar pension provisions, but rather as assets that individuals can use to supplement their private pension savings should they so wish. Financial products, known as Equity Release Plans, exist which enable the release of equity held in residential property without the need to move out of the property.

There are two main types of Equity Release Plans known as 'Home Reversion Schemes’ and ‘Lifetime Mortgages’ (or Mortgage-Backed Equity Release Plans). Each has their own advantages and disadvantages. Research has not yielded information regarding the use of financial products for the release of equity in property in countries other than the United Kingdom (‘UK’). In the UK, these arrangements are used as a source of voluntary third pillar pension provision – namely targeting (although not only) those pensioners who receive a low pension and who may not necessarily have any other liquid savings.

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395 See (fn 394).
Research did not yield any international regulatory guidelines for financial products aiding release of equity tied up in property for retirement purposes. The experience of the UK market shows that there may be scope for regulating Equity Release Plans. In fact, the UK is moving towards regulating this market namely due to three common factors:

- the relative complexity of the products per se;
- the relatively aggressive sales of these products; and
- the consumers who purchase these products are largely unable to understand the details or risks involved.

So far in the UK, only the sale of first charge Lifetime Mortgages is regulated by the Financial Services Authority (‘FSA’), while the UK Government has completed a consultation exercise with stakeholders regarding the regulation of Home Reversion Plans. It is probable that the latter will be regulated post 2006 by the FSA. In so far as the local market is concerned, although saving in housing appears to be increasing, only few people appear to plan or see their property as a potential source of retirement income according to a recent survey.

However, Equity Release Plans may prove to be an attractive option in due course, to certain segments of the population in Malta which are on the increase and to whom these plans are ordinarily attractive outside of Malta, such as single persons, childless couples and elderly people living independently rather than with their family.

These demographic changes in households and the population, coupled with a high home-ownership percentage which appears set to increase through increasing savings in housing assets, and possibly a culture change towards property, may lead to the emergence of equity release markets in due course.

Detailed research would need to be carried out to assess the potential for development of this market in Malta. Moreover, there is no legal framework which provides for the regulation of Equity Release Plans. Hence, should there be market demand for these types of products, it is considered that further research is carried out regarding the development of a proper regulatory regime to address the risks identified and discussed in the UK as a result of their experience in the use of Equity Release Plans.

A number of factors (such as taxation and inheritance law amongst others) would also need to be looked into in further detail.

Recommendations:

- Property should not be seen as a substitute source of retirement income to Second and Third Pillar pensions – but rather as a complement thereto.

- There is scope for considering property as an optional Third Pillar pension. A detailed study should be carried out in due course to assess the potential for the development of an Equity Release market in Malta.

- If demand for Equity Release products results, it is recommended that further research is carried out regarding the need or otherwise of a tailored regulatory regime for such plans, and other related areas such as inheritance law and taxation. A supporting educational campaign should accompany at any time any availability of these types of products.”

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396 Please note that since these words were written, regulation of home reversions (Sale Model ERS) in the UK is now in place and has been since April 2007. Please see p.9 for more details on the UK legal situation.
### XV. Greece

#### 1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Greece</th>
<th>EU Median</th>
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</thead>
<tbody>
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<td>Owner occupation (% of households, latest)</td>
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<td>House prices (average annual % change 2003-2007)</td>
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<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
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<td>Growth in mortgage debt (% 2007)</td>
<td>21.4</td>
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<td>Residential mortgage debt (% of GDP, 2007)</td>
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<td>Net replacement rates on mandatory pension programmes (%)</td>
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<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
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</tr>
<tr>
<td>ERS Market?</td>
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</table>

Owner-occupation is the overwhelming tenure in Greece, and the country’s housing market is unique in having no social rented sector following the transfer of these to their tenants in the 1990s. A high proportion of these owner-occupiers are also outright owners with anecdotal evidence estimating that only one quarter of all households actually acquired their property with a mortgage (among the lowest rates in Europe). This is mainly due to historically high interest rates, buyers relying on help from their families rather than bank loans, and the tradition of owner-occupiers building their own houses on plots of land and living in them for the rest of their lives. The mortgage market in Greece, though marked by being without specialised mortgage credit institutions (other than those covering public-sector employees), is still seeing mortgage debt growth in line with the rest of Europe, with government policies that include tax relief on mortgage interest payments while also taxing imputed rental income (though only for properties of a very large size). As shown in the table above, target pensions for average earners in Greece are among the highest in the OECD countries alongside those for Luxembourg, the Netherlands and Spain, and this generous pension along with other forms of help for elderly people means there may be weaker demand for ERS than elsewhere.
2. Reasons for undeveloped markets

ERS are not offered in Greece. Below are three categories of reasons that explain why this is so.

a) Social situation

The following social circumstances surrounding these products would continue to make ERS not very popular in Greece:

a) Not many elderly people are in care homes, because family relations are traditionally strong in Greece, thus when in need, the elderly move to stay with their children\(^{397}\).

b) Traditionally, an elderly homeowner in Greece would rather sacrifice the quality of his life in order to leave an inheritance to his children of all his estate, than take an ERS and enjoy a better life but leave nothing or less of his estate to his children\(^{398}\).

Nevertheless, it is the view of consumer representatives from Greece that there would be a mass of consumers potentially finding ERS interesting\(^{399}\).

b) Economic situation

Another barrier put forward by the financial institutions to explain why products such as ERS do not exist in Greece is economic and refers to the cost of securing the house. Due to regulatory constraints in the Greek legal system, Greek banks say they will be exceedingly burdened with costs should they want to offer ERS such as roll-up mortgages, or even simply innovative mortgage loans such as interest-only mortgages or fixed repayment mortgages\(^{400}\). Under the current law and the current practice of the banks, the home loan is not secured by a mortgage, the cost of which is very high. It is secured by a ‘pre-notice of mortgage’. The mortgage pre-notice is a court decision which grants to the creditor a preferential right for the registration of a mortgage. If (and only if) the claim of the creditor is pronounced final, then the ‘pre-notice’ is transformed into a mortgage and is considered to be registered as a mortgage (with all the legal consequences related to the mortgage) dating since the (initial) date of registration of the pre-notice (court decision) to the Land Registry. The pre-notice of mortgage (art.706 of our Code of Civil Procedure), but the mortgage as well (art 1269 of the Civil Code), are related to a specific amount of money. The interpretation made by the providers is that if the ERS is given to the consumer not as a lump sum but on instalments, that would

\(^{397}\) The ENEPRI/ Jehoel-Gijsbers & Vrooman, Report on Social Exclusion of the Elderly (2008) explains that care can be provided either informally or formally, and that the relationship between formal and informal care can be expressed in country typologies using 'primary responsibility' to distinguish countries, e.g. does it lie with the individual (Scandinavian model where the State steps in), the nuclear family (Continental model), or the extended family (Mediterranean model). In the latter group is Greece alongside Italy and Spain, where the family often has a legal duty to support relatives up to the third degree (http://www.money-advice.net/media.php?id=3316). This is also in line with findings from the Survey of Health and Retirement in Europe (SHARE) that has recently published results showing that in terms of financial transfers (i.e. gifts) the elderly in Greek are the largest recipients from their children. See p.181 under: http://www.share-project.org/t3/share/fileadmin/pdf_documentation/selected_results/CH4.pdf.

\(^{398}\) Based on anecdotal evidence from conversations with Greek nationals.

\(^{399}\) From an email exchange with the Greek consumer organisation EKPIZO ‘Quality of Life’. What is also interesting in the case of Greece is the relatively high proportion of widows among the elderly women (together with perhaps a weaker labour market participation rate in line with trends from Southern Europe) who are known to be the greater users of private home reversions generally and thus potentially ERS too. Among the women over 80 in Greece almost nine tenths are widowed. See work by the EU on the Survey of Health and Retirement in Europe (SHARE), http://www.share-project.org/t3/share/fileadmin/pdf_documentation/selected_results/CH4.pdf.

\(^{400}\) This information was provided to us in a letter by the Hellenic Bank Association, and later verified with conversations with their legal adviser.
necessitate, under the current legal environment in Greece, multiple mortgage pre-notices, one for each payment. This however is open to legal debate and is not a unanimous viewpoint.

c) Legal situation

Although the Greek financial market does not currently include ERS, there is no literal legal restriction reported. Nevertheless, the current legal environment would not apply to such products unless adapted accordingly.

For example, there is no maximum duration for mortgages in Greek legislation as such, but of course mortgages are, under the law, repayable from an individual’s lifetime income and the lender has to pay capital plus interest to the creditor on a regular basis (monthly or otherwise). In this conventional mortgage, under prudential rules of the bank supervisory law, older people are not considered to be creditworthy. Consequently, roll-up mortgages and fixed repayment lifetime mortgages, which provide for repayment only when the home is sold, cannot be offered under current Greek law. Below are several aspects which may or may not need attention:

(1) Amortisation:

As in France, Greek mortgages are related to regular payments against capital and interest. While France changed this law and made it possible for the mortgage to be repaid only after death of the borrower and exclusively out of the return from the sale or auctioning of the property, this adaptation would still have to be done in Greece.

(2) Regarding data on risk evaluation related to the value of the land.

Because the value of the land is extremely important in ERS, many problems may arise for the consumer, if the land is not sold at its proper value. This is particularly problematic in Greece, where there is already an immense problem with the forced sales of the (confiscated) home or other immobile property of the debtor: Such property is very often sold at a value significantly lower than its real commercial value. This leaves the debtor disadvantaged in both of two ways: without his/her house any more and with a remaining debt. This could also happen under ERS. The only way it could be restricted is if Greek products were to have a valid no-negative equity guarantee, which is the case for products found in a number of other countries, especially the UK.

(3) Transfer of title and transfer of sureties.

In Greece, the legal system permits contracts where there is a transfer of title and also allows for the surety to be transferred to a new lender. However, this transfer of surety is only possible by assignment of the claim, whereby as a result of ‘accessoriness’, the mortgage is transferred ipso jure to the assignee. Furthermore, Greece has a system of creating mortgages separately from the loan agreement of the parties concerned.

(4) Mortgages in respect of future debt

In the Greek legal system, the mortgage is related to a specific sum. This sum may refer to a claim as it stands at the moment when the mortgage is created plus legally related sums like e.g. interest. So, a mortgage may not cover a future debt as such, but may
cover a specific sum of money, which is allowed to be estimated higher than the initial sum so as to cover interest and expenses\textsuperscript{401}.

(5) Codes of Conduct or Recommendations

Should ERS be offered in Greece, there would certainly be a strong necessity for an adjusted Code of Conduct. But what is more important is to have the adequate legal environment which would protect borrowers in all aspects (advertising, provision of information, provision of advice, information during the contract, no negative equity, transparency, cancellation and other).\textsuperscript{402}

(6) Tax law

Tax law could be used to promote or to put barriers to ERS. In conventional home loans with mortgage, there is currently, in Greece, a tax law provision according to which the sums paid yearly for repayment of the home loan are deducted from the income when the loan belongs to the so-called first residence of the borrower. This is an incentive for people to acquire a home of their own on a home loan secured on a mortgage. Similar provisions could be adopted for ERS. Moreover, according to Greek tax law, the rent paid to the homeowner is deductible from one’s income. This provision could be useful to promote ERS.

(7) Bankruptcy law

The general section of the report explains how important the guarantee schemes are and would be in the case of ERS\textsuperscript{403}. It is the view from the consumer perspective, that this level of protection is adequate. With the current world financial circumstances of 2008 in mind, it is self-evident how insecure it is for someone to be dependent on the financial health of a credit institution.

(8) Insurance law

It is the view of one of the Greek survey respondents that should Greece have ERS in their legal system, it would be foreseeable to them how important it would be to have lengthy debate on the possibility of obligatory insurance in the legal discussions. This would primarily focus around the insurance against negative equity for the consumer. The no negative equity guarantee is seen by the great majority of respondents of our study as crucial for consumer protection\textsuperscript{404}.

\textsuperscript{401} This is specified in the Greek Civil Code and is covered in great detail in the European Mortgage Federation Study on the Efficiency of the Mortgage Collateral in the European Union (2007) p.61 (http://www.money-advice.net/media.php?id=3315).

\textsuperscript{402} Response from Questionnaire SQ64.

\textsuperscript{403} See Part I: General Report section E.

\textsuperscript{404} See Part I: General Report section C.
XVI. Portugal

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Portugal</th>
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<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
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<td>Per Capita Mortgage debt (EUR)</td>
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<tr>
<td>Per capita private pension fund assets (EUR)</td>
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<td>Population (2008, million)</td>
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<td>16.2</td>
</tr>
<tr>
<td>ERS Market?</td>
<td>No market</td>
<td></td>
</tr>
</tbody>
</table>

Portugal has always had a relatively high rate of owner-occupation for cultural reasons and because historically there have been few alternative investments. A history of rent control also meant that ownership of rental property was often unprofitable. A typical household would buy or build a house after marriage, often with the help of the extended family. The rate of owner occupation rose from 66% in 1991 to 76% in 1999 because of the fall in mortgage interest rates and the introduction of important tax benefits for owner-occupiers, including tax deductibility of mortgage interest.

Owner-occupiers pay a high proportion of their household income for servicing of their mortgage loans and indebtedness is significant if judged by the ratio of mortgage debt as a percentage of GDP. Mortgage periods usually last 15-20 years, with a legal maximum of 40 years and until only recently have the banks and the government permitted loans to run until a borrower is 70 (though the borrower is not covered by life insurance after the age of 65). The proportion of housing credit in total credit to households increased to 49% in 2007 reflecting the strong competition in mortgage market in recent years, and the value of housing credit in terms of outstanding residential loans grew by 10% in 2007. Though not the first country that one typically associates with mortgage equity withdrawal, there is some evidence that owner-occupiers have been increasing the size of their mortgages in order to fund non-housing consumption in Portugal. This will be linked to house prices having risen significantly in the early 1990s, though with large geographical variations between price changes in Lisbon and the Algarve region.
comparing to those of the interior areas\textsuperscript{405}. Though neither sustainable nor a sign of future policy direction, Portugal’s pension spending has grown faster than that of most of the other EU Member States going from 5.4\% of GDP in 1990 to 10.5\% in 2003 (compared to an OECD average of 7.7\% and only exceeded by France, Germany and Italy)\textsuperscript{406}.

2. Markets and products

In Portugal, there are no ERS. Nevertheless, there are some equivalent products such as ‘sale and lease back’ and ‘secured lending’ provided by banks and other financial institutions. As explained below there are no specific legal barriers in opposition to ERS, and the general legal barriers that may be applicable are not sufficient to determine the failure or impossibility of ERS in Portugal.

There is also no generalised practice in Portugal that involves selling your house to another private individual in exchange for a rent, a sort of ‘private’ home reversion.

The market is less sophisticated and banks are less proactive in bringing forward new products\textsuperscript{407}, compared to other neighbouring countries such as Spain. Also, though income poverty does exist among homeowners in Portugal, one argument used to explain why these products are not being demanded is that the cost of living in Portugal is lower than in certain places such as the UK where certain material well-being requires substantial liquid funds.

There is no proper rental market so buying and staying is the favoured option. Second charge mortgage lending is not a common practice though refinancing of mortgage contracts with the aim of transferring the loan is used by many (despite the almost only use of variable interest rate credits). Consumers do look for better bank offers and these often offer to pay for all expenses and fees involved to make the refinancing more attractive. Access to credit for the elderly is not easy due to banking practices. In fact, the usual practice is for lenders not to go beyond 50 years loans, as long as the borrowers’ age, at the end of the loan, is not over 80 years. This means that a 65 year old may only be able to obtain a credit offer with a fixed term of maximum of 15 years.

3. Legal situation

The activity of building societies in Portugal is regulated by law and they are absolutely not allowed to grant any sort of credit by themselves\textsuperscript{408}. If a building society desires to promote and sell ERS products there has to exist a partnership with an authorized credit institution. As opposed to Spain where Loan Model ERS are granted by building societies, in Portugal, building societies are only allowed to promote these kinds of products on behalf of a credit institution. Credit institutions are the only institutions authorised to grant credit in Portugal and, out of those, it is mainly banks and financial institutions of credit that can provide mortgage loans. Banks do not offer ERS in Portugal.


\textsuperscript{407} As an example, it is very unusual for a credit product to be sold where the principal is not being continually reimbursed over the term of the credit i.e. interest-only loans do not really exist and when they do they are over very short periods of maximum of 5 years for even the most aggressive lenders.

\textsuperscript{408} See Decreto-Lei 211/2004.
There is no legal limit in place on mortgage loans’ term\textsuperscript{409} despite the fact that the usual practice is for lenders not to go beyond 50 years loans, as long as the borrowers’ age, at the end of the loan, is not over 80 years.

As confirmed by the central bank, Loan Model ERS are not possible under the existing regulatory framework\textsuperscript{410}. However, Sale Model ERS are not forbidden by the Portuguese law. Nor are they forbidden for private citizens or for building societies.

4. Barriers

a) Social and cultural barriers

The main reasons for the non-existence of this kind of product in Portugal are mainly cultural ones. In fact, Portuguese people are still very conservative and wary in what concerns indebtedness and new financial/banking products. With regards to ERS more specifically, and since it may affect the bequest of the borrower, cultural and sociological reasons are the main obstacle to an ERS market\textsuperscript{411}.

b) Some legal impediments

In Portugal, there is no legal framework regarding ERS. We have no knowledge of any legal regime being prepared, or even planned, concerning this matter. However, there are also no clear legal barriers that prevent banks from offering these kind of products, or even similar ones, and there are no specific legal barriers that prevent the development of an ERS market in Portugal. As far as Loan Model ERS are concerned, the existence of certain legal uncertainties, related, namely, to successor’s rights and to creditors’ ranking claims, coupled with maybe some lack of demand and/or incentives by banks and other credit institutions, could be the reasons why these special type of mortgage loans are not being offered. Below are nevertheless some reasons that may explain the as of yet undeveloped market, and if any Loan Model ERS is to be provided in Portugal, the product will need to respect the same rules of any other loan or mortgage loan.

In Portugal, there is no legal time limit for a mortgage or regarding the age of the borrower. Nevertheless, the Portuguese banks have a practice concerning regular mortgages that mean that they do not exceed a period of 50 years, and that the borrower shall not be over 80 years at the end of the mortgage. This is due to the difficulty in providing additional guarantees beyond this age, especially as it relates to life insurance. However, there are some general limitations that shall be taken into account and that are applicable to ERS.

Like other countries, in what concerns the legal implications of compound interest (anatocism), though generally forbidden, the Portuguese law\textsuperscript{412} does however allow this practice under only two circumstances:

- Agreement between the borrower and the lender, posterior to the maturity of interest; and
- Court notice to debtor in which he is informed that he will capitalize on interest earned or proceed to payment under penalty of capitalization.

\textsuperscript{409} See Decreto-Lei 349/98, article 3 (with the modifications performed by Decreto-Lei 231/2002).

\textsuperscript{410} As mentioned above, the reason put forward is that they would hardly fit within the current legal framework given that the entities usually involved in these transactions, building societies, are not allowed to trade these sorts of products.

\textsuperscript{411} Response from Questionnaire SQ63.

\textsuperscript{412} See nr. 1 of article 560 of the Portuguese Civil Code.
Still relating to anatocism, the law\textsuperscript{413} stipulates that only interest corresponding to the minimum period of one year can be capitalised. Nevertheless, the above mentioned rules will only be applicable if they are not contrary to rules or private uses of commerce, leaving a possibility for bank anatocism – which is very common practice in Portugal and allowed by the majority of judicial decisions.

In what concerns mortgages in respect of future debt, they are not allowed by Portuguese law since that it stipulates that all business (mortgages included) must be determinable. In fact, the legal regime does not allow the constitution of mortgages as a way to guarantee future debts. If such mortgage occurs, it may be considered void because its purpose is indeterminable.

As already mentioned, there are no legal barriers hindering the existence of Sale Model ERS just as there are none regarding ‘private home reversions’. The principal of contractual freedom, which is a cardinal principle of Portuguese law, makes it possible for a private person to conclude a contract very similar to Sale Model ERS.

\textsuperscript{413} See nr. 3 of article 560 of the Portuguese Civil Code.
XVII. Poland

1. General information

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<tr>
<td>ERS Market?</td>
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</tr>
</tbody>
</table>

2. Markets and products

Homeownership ranks very high in people over 60 who have a low mobility.

In Poland, ERS are called odwrócona renta hipoteczna or umowa dożywocia (lifetime agreement). No such products are presently marketed or offered. But there is some discussion among banks who are interested in financial innovation and consider introducing. A special website to promote the idea of reverse mortgages is dedicated to this issue\(^{414}\). It explains its functioning and collects opinions ('blog') and refers at least to one newspaper article, a promoting video and a TV programme. These activities focus only on Loan Model ERS. However, there are also no Sale Model ERS marketing Poland.

However, there is a declining replacement ratio in old-age systems and there are severe problems in getting access to medical services since private health insurance is required. With an ageing population and children living increasingly far from home, as well as the increase in divorces, the traditional form of home reversion is used especially for old age care where the homeowner gets care for lifetime in exchange for the home. There are usually no financial benefits involved. Especially the Catholic Church and charities offer such schemes.

\(^{414}\) See http://www.reversemortgage.pl.
3. Law

Polish law has no regulations that would hinder the spread of this system but anatocism is forbidden according to Art.482 &1 of the Polish Civil Code. Debtor protection is also viewed by one respondent as a concern that should be adequately discussed before he thinks a product should be brought on the market.\textsuperscript{415}

4. Barriers

There are cultural barriers as far as elderly people in Poland do not trust sufficiently in the financial sector. This is why home reversions are kept in the private sphere (friends, family members) where institutionalised providers are only the church and charity organisations. But even the press has reported on some cases where people had been let die after signing the contract in order to keep the property without the burden of the rent which at least is rumour that surrounds the traditional schemes.

\textsuperscript{415} Based on conversation following Questionnaire response SQ54.
XVIII. Slovakia

1. General information

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<td>Per Capita Mortgage debt (EUR)</td>
<td>1210</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>72.9</td>
<td>72.9</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>566</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>2.0</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>-1.5</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>23.0</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>16.1</td>
<td>16.2</td>
</tr>
<tr>
<td>ERS Market?</td>
<td>No market</td>
<td></td>
</tr>
</tbody>
</table>

2. Legal situation

The Slovak Republic has not developed respective legal regulation regarding ERS as financial services for supplementation of a pension. In a certain way, the aim of releasing equity using Sale Model products could be achieved e.g. through the Civil Code (sale of real estate with registered right to use it for life). This legal instrument is nevertheless not defined as a financial service and it is not used very often in Slovakia. One reason put forward is that at present, people still prefer keeping the real estates for their heirs, although this cultural preference could change if a massive marketing campaign were to take place.
XIX. Denmark

1. General information

<table>
<thead>
<tr>
<th>Category</th>
<th>Denmark</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>54.0</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>10.4</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>18.1</td>
<td>20.6</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>211.4</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>8.4</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>92.8</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>38710</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>86.7</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>76.8</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>52400</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>5.5</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>7.0</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>23.6</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>15.6</td>
<td>16.2</td>
</tr>
<tr>
<td>ERS Market?</td>
<td>No market</td>
<td></td>
</tr>
</tbody>
</table>

Specialist mortgage banks have 90% of the mortgage market in Denmark, and most mortgage loans are with a fixed interest and carry no prepayment penalties, a feature almost unique in Europe and largely due to loans being funded via callable bonds (meaning that if borrowers pre-pay their loans the credit institutions can repay bond investors). The mortgage market is judged as flexible and innovative loans such as interest-only loans for a period of up to ten years were introduced in 2003 following passing of laws416.

2. Mortgage market, legal situation and ERS

The first Danish mortgage bank was set up in 1797 as a direct consequence of the need to finance the rebuilding of Copenhagen after a great fire in 1795. Since the mid-19th century, the mortgage banks have taken up a predominant position in the financing of real property in Denmark.

The Danish mortgage market is based on effective and low-cost arrangement of credit of which the following features are characteristic:

- the loans are granted against security in the real property of the borrower;
- the loans are fixed-interest, long-term loans;
- the loans are granted within certain limits laid down in the Mortgage Credit Act;
- the effective interest is fixed by the market in a transparent manner;
- the loans are funded entirely through issuing of bonds;
- the bond investors have full knowledge of the security of the bonds which is based on the mortgage on the real property, the legal framework, and the solidity of the mortgage bank through nearly 200 years all bonds have been repaid.

Through the long-standing tradition as financial market players specialised in the granting of long-term loans against mortgages on real property, the mortgage banks have achieved a central position in the Danish economy. The significant dual role of the mortgage bonds - as an effective funding instrument on the one hand, and a secure investment on the other - has given the bonds a central positioning the Danish capital market, and in the longer term also in a wider international perspective.

### 3. Reasons for undeveloped market

Denmark, like the Netherlands\(^4\)\(^{17}\), produces unexpected results in terms of the existence of ERS because by looking at some of the factors that have been highlighted as drivers in the general report\(^4\)\(^{18}\), one would expect schemes to exist in the country. Although loan products are said to exist where disbursement takes place in instalments, these are so insignificant that no ERS are reported for Denmark which meet the criteria of this research. In fact, the products in Denmark are so flexible that they can also be used for ERS purposes without having to be designed to it specifically. One respondent mentioned the questionnaire and research emphasising the use of real property as a financing object in connection with retirement as misleading. Neither in legislation nor in practice are there specific age requirements for borrowers and the mortgage financing in Denmark is not subject to any such rules. In practice, all homeowners may raise loans against mortgages on real property only based on creditworthiness and the loan-to-value in question. Softer requirements will be imposed on the consumer the lower the ratio and this has led to seniors mortgaging their homes for the purpose of equity release by way of an ordinary mortgage. Mortgage lending to seniors was thus quoted as “does not involve special products, special circumstances etc.”\(^4\)\(^{19}\).

There are however no legal barriers to selling ERS as providers who have a licence as a mortgage credit institution. They do not need a special additional license for ERS. Some economic barriers may explain the non-existence of special ERS though. One respondent said that ERS in Denmark is made up of only one type of product: “The bank get security in your house for a certain amount, and you get a draft right for the same amount. Now the consumer can totally free handle his draft right. He can spend it all the next day, or he can draw a small amount every month. When at any point in time he reaches the total draft limit, he must be able to pay bank the variable interest rate, and if one day he cannot do that, the house will be sold by the bank”. What this implies is that under such a product, the consumer seems to carry almost the entire risk of both: spending money too fast and/or living longer than expected.

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\(^{17}\) See following Country section for the Netherlands (on p.144).

\(^{18}\) See Part I: General Report section D.I.

\(^{19}\) Based on written response from a provider.
The barriers that seem to be preventing development of ERS in Denmark include the nature of provision of the financial services and the usefulness of other similar products that have become extremely popular over past years. The lack of competition in the provision of advisory services (and rather complex nature of counselling involving longevity risk for bank employees) was suggested by one respondent as a serious constraint on the development of the market because it appears that banks in Denmark have a de facto monopoly in providing financial advice at the current time\textsuperscript{420}.

The major challenge for ERS however is dealing with the flexibility offered by the Danish mortgage system. This ranges from the growing propensity that borrower’s have to remortgage (no doubt linked to the system that allows no early repayment charge), the general introduction of ‘flexible’ mortgages in which buyers can make over- and under-payments within certain parameters (with a more erratic curve for household equity - no longer rising smoothly over time), and the popularity of innovative products which offer clear short-term benefits to the consumer such as the interest-only mortgage. When they were introduced in Denmark in 2003, it was argued that they could benefit young families (e.g. at the birth of a child) as well as older people to supplement a fall in their incomes after retirement. Data show that it is these two extreme age groups that have the higher interest-only mortgages as a percentage of all owner-occupier mortgages (50 % for those aged 60+, notwithstanding the smaller mortgage sample size for that age group). By the end of 2005 they accounted for 25.6 % of all the outstanding mortgage debt and for 31.5 % of the owner-occupiers’ mortgage debt. This exceptionally quick growth has continued and by end 2007 represented 43 % of owner-occupiers’ outstanding mortgages\textsuperscript{421}. Denmark formally limits the interest-only period, to ensure that buyers are forced to begin to repay the capital sum after ten years at most (although provided the price of the house had not fallen buyers expected to be able to remortgage at that point and take out another interest-only loan). Recent legislation introducing a system of covered bonds has relaxed this restriction and one offer has already been announced containing a 30-year interest-only period\textsuperscript{422}.

\textsuperscript{420} Response from Questionnaire SQ46.
\textsuperscript{421} See Denmark’s central bank’s MFI financial statistics, available under http://nationalbanken.statistikbank.dk/statbank5a/default.asp?w=1024.
\textsuperscript{422} See EMF Hypostat 2007 http://www.money-advice.net/media.php?id=3288.
XX. The Netherlands

1. General Information

<table>
<thead>
<tr>
<th>Category</th>
<th>Netherlands</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
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<td>75.0</td>
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<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>4.5</td>
<td>9.2</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>559.0</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>1.9</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>100.0</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>34140</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>96.8</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>60.1</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>37931</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>16.4</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (% 2008-2035)</td>
<td>5.3</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>21.8</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>14.7</td>
<td>16.2</td>
</tr>
<tr>
<td>Number of ERS Providers</td>
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</tr>
<tr>
<td>ERS Market?</td>
<td>Sale Model less developed</td>
<td></td>
</tr>
</tbody>
</table>

In the Netherlands, the growth of owner occupation has been supported by state backed guarantees on mortgages and tax subsidies for homeowners. The overall level of owner-occupation has risen steadily decade after decade and made important jumps over short periods of time in the 1990’s. This rise in owner-occupation from a relatively low base was matched by a decline in social renting, partly as a result of the sale of some social housing, followed by housing associations gradually becoming financially independent after subsidy reductions. In 2006, 40% of households in the Netherlands contained at least one member who was aged 55 or older.

In the Netherlands, lenders offer a variety of mortgage types where the product range is one of the broadest in Europe. One factor behind this variety is that lenders tried to take maximum advantage of the fact that mortgage-interest payments were fully tax deductible in the Netherlands and that issuances were increasingly made up of saving and equity-based mortgages (products combined with investments designed to pay off the debt at term). In the same vein as ERS, in terms of offering consumers a solution to their liquidity shortages, innovative products such as interest-only mortgages became popular. Housing loans are generally consented at far greater loan-to-value ratios than in most other countries in Europe and often represent higher income multiples than elsewhere. In credit more generally, because there is no age restriction for people
wanting credit, other than request for a compulsory insurance from the bank above a certain age, ERS is not seen as the main answer to the wishes of cash strapped homeowners.

2. Markets and providers

In the Netherlands, one provider of Sale Model ERS has been identified on the market but only at the end of the research, and thus no responses from them have been included in this study. In any case, the market is expected to be very small and would not make a big difference on the aggregate size of the EU ERS market. With the exception of this one provider, ERS do not exist as defined by our definition. The products on the market are only extended versions of the more traditional mortgages, and if they were anything else than that, such products would not be regulated. Consequently, answers from the authorities indicate that the Dutch financial services authority and the Dutch central bank do not supervise the suppliers of these schemes and have no clear vision on them.

3. Products

More generally though, despite its advanced mortgage market, there are currently still relatively few products aimed at the elderly segment of the population. Two recent reports, one entitled ‘Holland – Pensions Champion’ stresses the strategic focus the country has in becoming the location for EU pension funds and pension-service providers, yet another more relevant report for our study, stresses that the Dutch financial sector is insufficiently developed in the banking and insurance markets to deal with population ageing (comparing the situation in the Netherlands with developments in Germany and Japan). This later report says that no products are currently offered with a specific focus on ‘doorleven’ (lifetime) in the Netherlands, though it does acknowledge that some providers are active in offering what they term “more general products” such as a life and ‘opeethypotheek’ (‘eat a mortgage’). This later word is sometimes misleadingly used synonymously with ‘Omkeerhypotheek’ (‘reverse mortgage’) the more official word used to refer to Loan Model ERS.

The several types of products identified by the authorities as enabling to extract liquidity from one’s home, do not include Loan Model ERS. Instead, they include: the extended/second mortgage; and the sale and leaseback construction, which can either be for the house and land or for the land only, and can be with or without a rental fee. Though not the subject of our investigation within this report, the extended/second mortgage products can be offered by all credit institutions, though even then, the numbers for these loans are not visible as such since they are included in the total number of mortgages.

Instead presently “homes are sold and the seller will lease it back or buy a cheaper house. Another method is to sell this property and the seller or the buyer has a lifelong usufruct. In both cases the owner loses home ownership of the property. Another method is a loan secured with a second mortgage on the house.”

423 The Dutch Authority of the Financial Markets were not able to help provide information on the market for these products.


a) Loan Model ERS

Since mortgage financing has become the dominant form for all kinds of equity release the article points to the fact that the important rise in house prices in recent years has built up hidden values in these homes: “More and more people want to have cash. It makes the value of their home liquid. They are less linked to their home and to their heirs. There are many reasons to liquidate equity. I mention a few: a lump-sum to buy a motor home or to make a world tour, a periodical supplement on the pension income, a gift to the children, purchase of nursing and care for the elderly.”

It is further mentioned that a growing number of people have difficulties to pay their mortgages out of their regular income. ERS would help them to keep this income and use their homes instead.

Rabobank who participated in our research by completing a questionnaire, did so with the understanding that its product was at least an equivalent to ERS. Its “opeethypotheek” (“eat-up mortgage) is “the granting of a credit to a natural person only on the basis of the value of a given security regardless the income of that person.” The respondent has also published an article in the Dutch language which describes the Rabobank product as follows:

“A type of loan whereby an owner takes up a housing credit from a current account with a secured mortgage on his home. The credit covers also the interest owed on the credit account. The reason for this credit was the demand from the market of mainly older clients that the value of their homes were silver. A credit in current account is very flexible. The borrower can in principle decide how and for what purpose he wants to use the credit. This type of loan is so far mainly “passively” marketed. The reason is that a number of points have not yet sufficiently crystallized. Nevertheless, there are an estimated more than 5,000 of these mortgages in the Netherlands. It is intended that the credit is paid back only at the time of the selling of the house. For the provision of a ‘opeet-hypotheek’ Rabobank has set a number of standards. In the first place the credit may not exceed 75% of the crash value of the property and less if there is other remaining debt of a home loan. The remaining 25% are intended as a buffer for setbacks. In second place, the borrower must in principle be older than 55 years. In the third place should the borrower be well informed about the risks associated with this type of loan. He should sign that he understood these risks and accepts them. On the fourth place the borrower should agree on how the credit is made available. If the borrower i.e. wants to use the credit for a pension, he should be entitled to a monthly payment. In the fifth place there will be ongoing communication with the borrower how his situation has evolved and what adjustments would be needed.”

After special request, the author gave the following additional answers: “The borrower can always repay the credit. He has to repay the amount of the credit above 75% of the value of the mortgaged property. If he fails to do so the bank has the right to sell the property. In practice in such cases the bank and the borrower will try to find a solution for the problem. Borrowers that have exceeded the 75% limit are hardly known partly because the ERS is a relatively new phenomenon and partly because the bank does a close monitoring of this type of credit.”

The product is used for equity release but not exclusively designed for it. It allows for all kind of equity releases, may be revoked earlier, has no necessary lifetime approach, does not provide for pensions only and keeps the debtor personally obliged to repay the credit.

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426 See (fn 425) p.347 section 1.
427 See (fn 425) p.349 section 3.2.
It therefore falls into the category of second mortgages which release equity in general and have been excluded from this investigation.

However, it would be incorrect to report that ERS did not exist at all however small the existing market. The products described here are either a lump sum payment or they calculate a rent for a fixed period of say 10 years and deduct it from the proceeds from the sale. These actors are not currently regulated by consumer credit regulation and are not seen by financial authorities as being a financial product, however, if they compete with a financial product there may be enough grounds for regulation of these as well.

b) Sales Model ERS

With regards to Sale Model ERS and the necessary distinction between these and sale and lease back arrangements that do exist (some of these providers even fear regulation), all these products nevertheless have the feature in common of not being subject to supervision. From the different providers actively selling these products, we are able to separate the 3 providers active in the sale and lease back for the house and land with rental fee, and the one provider (Finquiddity) offering sale and lease back for the land only, from the one provider found to be offering something resembling a Sale Model ERS (described by the authorities as a “sale and lease back for the house and land without rental fee”). This provider is a housing corporation called Torenstad verzilverdwonen (translated as City Tower Redeemed Living) but the volume of business transactions is unknown and thought to be very limited.428

Because these are not ERS and not associated with either elderly people or issues of retirement and supplementing deficient pension income, a Dutch provider responded in the following way to the question of the typical user: “A couple of retired people who want to make the value of their house liquid in order to maintain or improve their lifestyle, to make an expensive trip or to buy a car, a boat or a camper.”. The emphasis shows that the product is thus clearly referring to a different clientele to the generally well represented pensioners on low income seeking to make home improvements, pay for care, and maintain the lifestyle they had during the employment phase of their lives.

4. Legal situation

The Netherlands has no specific legislation concerning ERS. There is therefore no official minimum age for persons who wish to take out an ERS.

A loan secured by a mortgage on a home is often referred to as concerning only the acquisition, construction, renovation or improvement of the dwelling. The Act on financial supervision entered into force on January 1 2007. According to this administrative law the lender has a number of obligations:

- provide information that consumers reasonably need in order to get an adequate picture of the product;
- inquire about the financial position of the consumer, his knowledge, experience, objectives and risk attitudes;
- give advice according to the collected information;
- hand out this advice and information in textual form;
- give accurate, understandable and not misleading information in Dutch;
- apply his own lending standards;
- refrain from supplying credit in case this would lead to over-commitment.

428 The provider’s website is available at: http://www.torenstad-verzilverdwonen.nl/.
The Financial Markets Authority (AFM) will monitor the compliance of the lender with these obligations. Neither the AFM nor the legislature has so far given a precise description of what "excessive" credit granting would mean. Industry assumes that the borrowing capacity of a consumer is limited by the purchasing price of the home.

But the AFM also stated that these standards are not directly applicable to the "opeethypothek". The author of the report expects that these standards will apply and the question of excessive lending practices may play an important role since according to normal standards of acquiring a home via mortgage loans the “opeethypothek” could be seen as an excessive burden since it may cover the whole of the equity.

Unlike administrative law, contract law is fully applicable. Since 1989 the Mortgage Code contains rules prescribing certain behaviour for lenders before and during credit contracts for "the purchase, renovation or improvement of homes". The code sets out rules for pre-contractual information, the content of an offer, the calculation of the maximum credit, and the APR. The Code of Conduct of the European Mortgage Federation also covers more than 95% of the professional mortgage loan providers in the Netherlands. Furthermore, this code also only applies to loans to consumers who intended to purchase, renovate or improve an owner-occupied home. A consumer who believes that a mortgage lender fails to comply with the code of conduct, may complain to an independent Ombudsman. In addition, a Commission has recently been set up to monitor whether the mortgage loan providers themselves observe the standards included in the code concerning the creditworthiness of the consumer.

5. Reasons for undeveloped markets

One characteristic of the Netherlands is that it is not uncommon at all for households to have two mortgages, in fact according to a report on housing wealth and ageing, a head of household of 70 years of age is still expected to face an average number of mortgages of 0.5.429

Reasons for the lack of formal ERS despite the developed use of mortgage based products etc. may lie in the fact that these products actually serve a similar purpose to ERS by allowing homeowners to extract liquidity from an earlier age by assigning claims to their property. These loans do not contain the safety measures which an ERS is expected to contain and repayment of the outstanding debt is expected to be met through regular repayments made during the lifetime of the borrower, and is not conditional on the sale of property from the outset. Dutch banks prefer some repayment to take place during the term of the loan and although interest only loans do exist they are very rare, usually banks try and receive half of total principal repayments during the term and the other half at the end. Despite products that at first appear as Loan Model ERS, these are revealed to be more familiar with the traditional ‘forward’ loans than reverse mortgages and often operate from a current bank account.

One area where the Dutch seem to be relatively well prepared is in terms of adequate housing for the elderly, though whether or not this will mean that there will be less trading down in old age is not conclusive. The government does however invest in

429 Because assuming two mortgages at once would be exceptional (because of the transaction costs involved), many households took a second mortgage after they first became owner-occupiers. Presumably this often happens when the household moves to another house, or decides to improve the house. As opposed to the UK where it is usual to refinance mortgage loans frequently, in the Netherlands, it is more related to moving to another house, as this often implies renegotiation of the mortgage and often leads to extending the size of the loan, possibly by taking a second mortgage. A second mortgage may also be taken without moving. Unlimited mortgage interest deductibility often makes it unattractive to repay the loan, since investing in other assets is likely to offer higher returns. Especially since the tax reform of 2001 lowered the effective tax rates on capital returns, it is almost always in the interest of the homeowner to maximize mortgage debt. See Rouwendal, Jan: Housing Wealth and Housing Portfolios in an Ageing Society (discussion paper) in Netspar (2007) under http://www.money-advice.net/media.php?id=3261.
suitable homes and has clear targets and action plans for housing for older persons, which is set out in Memorandum 64 as “the over-55s must have access to adequate housing, geared to their individual needs and supported by customised care provisions (‘supported living’)“\textsuperscript{430}.

Though cross country comparisons are difficult, a report from 2005 which studied how the Dutch elderly spend their housing wealth confirmed that Dutch households consider home equity more as a resource to be used in case of ‘catastrophic events’ than as a source of regular supplementary income. The research, based in part on information collected during interviews with elderly people, concluded that housing wealth will, for the greater part, keep on functioning as unused savings for the Dutch elderly for the foreseeable future\textsuperscript{431}.

6. Benefits and risks

a) Benefits

In a recent article\textsuperscript{432} favouring the introduction of ERS into the Netherlands from Rabobank the English summary stresses that "an increasing number of Dutch people want to turn the surplus value of their house into liquid money as a supplement to their pension or for other purposes. In the Netherlands, there are no specific rules or provisions for changing this surplus value into liquid money. However, it has been stipulated by law that a credit provider must be able to prove that he has gained information about the customer and the latter’s situation which is sufficient for assessing whether or not it would be justified to grant this credit."

b) Risks

For the provider the right to withdraw from an overdraft credit can create overindebtedness especially if the credit limit is exceeded. There is also a problem to predict the date of death in an individual case which may differ from general statistics. The lender may have to force an old client out of his or her home which can damage the reputation of the lender. The Dutch report\textsuperscript{433} further cites a depreciation of the value of the home due to a general drop in prices or of the relevant property in particular or because of poor maintenance.

As the credit in a current account has a variable interest rate, the size of the loan depends on the developments in the money markets. If interest rates rise further or faster than expected, it probably means that the credit limit is attained earlier. The lender may then be forced to sell the home.

\textsuperscript{430} See The Netherlands Institute for Social Research (van Campen, Cretien; ed.) \textit{Values on a grey scale (Elderly Policy Monitor 2008)}, available at http://www.scp.nl/english/publications/books/9789037703924/\_Values\%20on\%20a\%20Grey\%20Scale.pdf. The report has a section on housing which explains that over 15% of households over 55 live in a home designed for older occupants (approx. 30% of which had access to care on call). Care-supported housing is designed especially for older occupants, with standby care facilities on call (meaning that people can receive care or nursing within their home from a residential care home, home for the elderly, service centre or support centre in their local neighbourhood).


\textsuperscript{432} See (fn 425) p.347 introduction (in English in text).

\textsuperscript{433} See (fn 425) p.350 section 4.5.
XXI. Cyprus, Czech Republic, Estonia, Latvia, Lithuania, Luxembourg, Slovenia

In the abovementioned EU Member States, the responses to our inquiries revealed that no ERS products exist and no discussions on these products was or is taking place. The experts also mentioned that no barriers, particularly legal barriers, existed to the introduction of either Loan or Sale Model ERS. The situations in these countries resemble those found in Member States were more detailed reports were available like Cyprus (with Greece), the Baltic states (with Hungary), and the Czech Republic and Slovenia (with Italy).

1. Cyprus

<table>
<thead>
<tr>
<th>Category</th>
<th>Cyprus</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>68.0</td>
<td>75.0</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>7.0</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>28.2</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>44.8</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>8870</td>
<td>7820</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>0.8</td>
<td>9.2</td>
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<tr>
<td>Population growth (% 2008-2035)</td>
<td>41.1</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (% 2008)</td>
<td>17.7</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>12.4</td>
<td>16.2</td>
</tr>
<tr>
<td>ERS Market?</td>
<td>No market</td>
<td></td>
</tr>
</tbody>
</table>

2. Czech Republic

<table>
<thead>
<tr>
<th>Category</th>
<th>Czech Republic</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>58.7</td>
<td>75.0</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>19.6</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>45.1</td>
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</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>15.3</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>1890</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>64.4</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>46.7</td>
<td>65.2</td>
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<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>466</td>
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</tr>
<tr>
<td>Population (2008, million)</td>
<td>10.3</td>
<td>9.2</td>
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### 3. Estonia

<table>
<thead>
<tr>
<th>Category</th>
<th>Estonia</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>96.0</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>26.5</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>47.0</td>
<td>20.6</td>
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<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>5.6</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>31.5</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>36.3</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>4190</td>
<td>7820</td>
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<tr>
<td>Population (2008, million)</td>
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<tr>
<td>Population growth (%, 2008-2035)</td>
<td>-7.2</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (%, 2008)</td>
<td>25.2</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>17.2</td>
<td>16.2</td>
</tr>
<tr>
<td>ERS Market?</td>
<td>No market</td>
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### 4. Latvia

<table>
<thead>
<tr>
<th>Category</th>
<th>Latvia</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>87.0</td>
<td>75.0</td>
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<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>37.6</td>
<td>20.6</td>
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<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>6.7</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>43.9</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>33.7</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>2960</td>
<td>7820</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>2.3</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (%, 2008-2035)</td>
<td>-13.2</td>
<td>4.5</td>
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### 5. Lithuania

<table>
<thead>
<tr>
<th>Category</th>
<th>Lithuania</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>97.0</td>
<td>75.0</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>4.8</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>61.8</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>17.5</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>1440</td>
<td>7820</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>3.4</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (%, 2008-2035)</td>
<td>-10.9</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (%, 2008)</td>
<td>23.0</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>15.8</td>
<td>16.2</td>
</tr>
<tr>
<td>ERS Market?</td>
<td>No market</td>
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</table>

### 6. Luxembourg

<table>
<thead>
<tr>
<th>Category</th>
<th>Luxembourg</th>
<th>EU Median</th>
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</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>74.6</td>
<td>75.0</td>
</tr>
<tr>
<td>House prices (average annual % change 2003-2007)</td>
<td>8.8</td>
<td>9.2</td>
</tr>
<tr>
<td>Number of transactions per 1000 homeowner (2007)</td>
<td>10.8</td>
<td>20.6</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>13.8</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>22.1</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>38.5</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>29030</td>
<td>7820</td>
</tr>
<tr>
<td>Net replacement rates on mandatory pension programmes (%)</td>
<td>96.2</td>
<td>72.9</td>
</tr>
<tr>
<td>Replacement Rate of Public Pension in relation to Wages (%)</td>
<td>86.7</td>
<td>65.2</td>
</tr>
<tr>
<td>Per capita private pension fund assets (EUR)</td>
<td>688</td>
<td>1650</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>0.5</td>
<td>9.2</td>
</tr>
</tbody>
</table>
ERS do not exist in Luxembourg and no specific legal barrier has been identified to suggest that Loan or Sale Model ERS could not be marketed if providers decided to offer it.

7. Slovenia

<table>
<thead>
<tr>
<th>Category</th>
<th>Slovenia</th>
<th>EU Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner occupation (% of households, latest)</td>
<td>84.0</td>
<td>75.0</td>
</tr>
<tr>
<td>Total Outstanding Residential loans (EUR billion, 2007)</td>
<td>2.7</td>
<td>61.7</td>
</tr>
<tr>
<td>Growth in mortgage debt (% 2007)</td>
<td>36.5</td>
<td>14.2</td>
</tr>
<tr>
<td>Residential mortgage debt (% of GDP, 2007)</td>
<td>8.0</td>
<td>34.9</td>
</tr>
<tr>
<td>Per Capita Mortgage debt (EUR)</td>
<td>1320</td>
<td>7820</td>
</tr>
<tr>
<td>Population (2008, million)</td>
<td>5.4</td>
<td>9.2</td>
</tr>
<tr>
<td>Population growth (%, 2008-2035)</td>
<td>-3.1</td>
<td>4.5</td>
</tr>
<tr>
<td>Old age dependency ratio (%, 2008)</td>
<td>16.6</td>
<td>24.2</td>
</tr>
<tr>
<td>65+ (% of total population, 2008)</td>
<td>12.0</td>
<td>16.2</td>
</tr>
<tr>
<td>ERS Market?</td>
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</tr>
</tbody>
</table>