

Eurofinas Response to the European Banking Authority's

Draft Guidelines on Creditworthiness Assessment Draft Guidelines on Arrears and Foreclosure

Draft Guidelines on Creditworthiness Assessment

Question 1: Do you agree with the proposed Guidelines? If not, outline why you disagree and how the Guidelines could be improved. Please respond separately for each of the seven Guidelines.

Introductory observations

Eurofinas, the voice of consumer credit providers at European level welcomes the opportunity to respond to the Consultation Paper on Draft Guidelines on Creditworthiness Assessment.

Eurofinas supports the work of the European Banking Authority (EBA) in enhancing consumer protection in the mortgage credit sector.

Who we are and why we are concerned

Depending on market characteristics and structure of Member Associations, Eurofinas represents first and second charge mortgage lenders.

From experience, we have seen that a high number of local authorities have applied either fully or partially, the Consumer Credit Directive (CCD) to the mortgage credit sector. Such authorities are therefore likely to consider, when transposing the Mortgage Credit Directive (MCD), to apply this Directive to consumer credit as well. This is almost certain, where permitted by EU law, in countries which do not have civil law distinctions between mortgage and consumer credit lending.

The CCD is the golden standard for regulation of consumer credit in the European Union. This legislation already includes an obligation to assess the creditworthiness of applicant borrowers (article 8). Eurofinas fully supports such obligation because we perceive it as a precondition for successful and sustainable lending. In this regard, we draw your attention to the potential interactions between the creditworthiness assessment in the mortgage credit and consumer credit sectors.

General remarks

Eurofinas shares the view with the EBA that creditors must carry out creditworthiness assessments. Indeed, all steps should be taken to ensure that such assessments are carried out in a professional and adequate way. In this respect, we would also like to emphasise the importance of the use of data. Lenders must be encouraged to base their assessments on the widest range of sources available. Against this backdrop, lenders should however remain free to decide upon suitable systems and relevance of factors.

Importantly, one must appreciate that such assessments are carried out at one particular moment in time. It is essential to take this aspect into consideration when scrutinising the execution of creditworthiness assessments.

We draw your attention to the recent Judgment of the Court of Justice of the European Union in Case C-449/13. This case concerns the application of the CCD's obligation to assess borrowers' creditworthiness¹. The Court recognised that the CCD "affords the creditor a margin of discretion for the purposes of determining whether or not the information at its disposal is sufficient to demonstrate the consumer's creditworthiness and whether it is necessary to check that information against other evidence".

Eurofinas fully agrees with the EBA that over indebtedness of European households is a serious phenomenon which must be treated as such. However, over-indebtedness can be caused by multiple factors, primarily by certain macro-economic factors and personal circumstances. This has been recognised in a recent study on household over-indebtedness conducted by Civic Consulting on behalf of the European Commission.² Nevertheless, several aspects of the Guidelines seem to imply that over-indebtedness or payment difficulties are necessarily the result of inappropriate creditworthiness assessments.

Given that lending practices vary per EU Member State, we believe that the obligations laid down in the Guidelines should be phrased in an appropriately broad manner. Whilst the Guidelines provide sufficient flexibility to encompass the different characteristics of the lending and mortgage systems, some will prove difficult to implement in practice and may even raise issues with regard to legal certainty. Also, it is important to ensure consistency of the guidelines with "Level 1" regulation. In this respect, we are concerned by an increasing liability and litigation risk stemming from the proposed Guidelines.

Specific remarks

Guideline 1: Verification of the consumer's income

(1.1) Eurofinas is of the opinion that an obligation to verify the consumer's income history and any variability over time can be problematic and rather burdensome on creditors. In this respect, we emphasise the importance of the proportionality principle. Yet, proportionality is currently only mentioned in guideline 1.2. In addition, the income history seems to be relevant only with regard to consumers with irregular income (e.g. freelancers). In our view, relevant information relates to the income the consumer

¹ See CA Consumer Finance SA v. Ingrid Bakkaus and others, Case C-449/13, 18 December 2014. More information at: <http://curia.europa.eu/jcms/upload/docs/application/pdf/2014-12/cp140184en.pdf>

² Civic Consulting of the Consumer Policy Evaluation Consortium, "The over-indebtedness of European households: updated mapping of the situation, nature and causes, effects and initiatives for alleviating its impact – Part 1 and 2", 4 December 2013, Berlin.

receives at the time of applying for the credit and a general estimation of the income to be received in the future.

Eurofinas would therefore like to suggest to EBA to use, instead of “the consumer’s income history and any variability over time”, the following wording: “including the consumer’s underlying income capacity, and the consumer’s income history, if relevant, and any variability over a sufficiently long period of time”.

- (1.2) Eurofinas would like to point out that the requirement that creditors should use information provided by sources that are independent of the consumer’ seems inconsistent with article 20 of the Mortgage Credit Directive. Pursuant to this provision, information used for creditworthiness assessments shall be obtained by the creditor from relevant internal or external sources, including the consumer. We strongly believe that this guideline should not be more restrictive than “level 1” regulation.

Indeed, while the use of external sources can be encouraged, one cannot rule out that in certain circumstances this is simply not relevant (e.g. in case of limited debt history, or when an applicant borrower is self employed). Furthermore, it may not be compatible with the existing available sources for lenders. In this regard, we recall that a very diverse landscape exist across Europe for credit bureaus. The latter may be private or public and collect negative or positive data. It is our view that the use of external sources may simply be more relevant for Member States with more detailed registers.

- (1.3) Eurofinas is concerned about the introduction of notions aimed at guaranteeing the quality of the information provided by the consumer, specifically third party verification. For example, would the receipt of a pay slip or tax declaration from the consumer fulfill the third party verification requirement? Or is the intention that a creditor consults a borrower’s employer or the tax authority? We are of the opinion that these notions are too vague and would be difficult to apply and justify operationally.

Guideline 2: Documentation and retention of information

- (2.1) We propose that, instead of “the creditor should maintain complete documentation of the information that leads to mortgage approval”, the EBA should consider using the following “the creditor should maintain records of the relevant information that leads to mortgage approval”. Such wording would minimize the documentation which the creditors are obliged to maintain and therefore be in line with the principle of proportionality.

Guideline 3: Identification and prevention of misrepresented information

- (3.1) We agree that information provided to consumers should not be misleading. Nevertheless, we find this guideline rather unclear. In addition, the text seems to introduce a subjective standard for creditors to comply with. In our opinion, the Guideline would read better as follows: “the creditor should design loan documentation in a way that avoids the risk that the consumer may misunderstand the information provided by the creditor or credit intermediary”

In addition, it must be clear that the assessment is carried out at the time that the credit agreement is concluded.

Guideline 4: Assessment of the consumer's ability to meet his/her obligations under the credit agreement

- (4.1) This guideline is not entirely clear to Eurofinas. We would like to ask the EBA to clarify, or define, the term 'undue hardship'. In addition, the reference to over-indebtedness or payment difficulties implies that such matters are necessarily the result of inappropriate creditworthiness assessments, while household' over-indebtedness can have multiple causes, such as unemployment, relationship breakdown, or illness. As a matter of fact, these events may occur after a loan has been granted or possibly not have been reasonably foreseen at the time when it was granted. In addition, Eurofinas would like to recall that "responsible borrowing" is an important way to prevent or minimize "undue hardship".

Moreover, we draw attention to the fact that the MCD provides that the lender should only assess the "probability" for the customer to fulfill its obligations. There should be consistency with "level 1" regulation

- (4.3) We believe it is good practice to take as many relevant factors as possible when assessing an applicant borrower's creditworthiness. We therefore support, for example, including obligations to service other loans and regular payments. However, we would like to draw the EBA's attention to the fact that not all information may be available at the time of assessment. In addition, depending on the Member State, the existing infrastructure may not have sufficient details about borrowers.

Here again, the reference to over-indebtedness or payment difficulties implies that such matters are necessarily the result of inappropriate creditworthiness assessments. We disagree with this.

Guideline 6: Allowance for potential future negative scenarios

- (6.1) This Guideline would be problematic in terms of implementation. For this reason, we propose to change the term "potential negative scenarios in the future" to "scenarios which are foreseeable".

Guideline 7: Identification of groups of loans with higher risk profiles

- (7.1) We think this guideline is a prudential requirement which may not be best placed in this guidance document.

Draft Guidelines on Arrears and Foreclosure

Question 1: Do you agree with the proposed Guidelines? If not, outline why you disagree and how the Guidelines could be improved. Please respond separately for each of the five Guidelines.

General remark

Eurofinas fully supports measures to encourage creditors to exercise reasonable forbearance before foreclosure proceedings are initiated. In addition to these particular obligations for creditors, we feel that the Guidelines should also include a requirement setting out the borrower's obligation to cooperate with the creditor.

As a general remark, we would find it helpful if the Guidelines further clarify the concept of "payment difficulties". It is currently not clear to us whether such difficulties relate to a certain credit agreement or to payment difficulties in general.

Specific remarks

Guideline 2: Engagement with the consumer

(2.2) This Guideline may prove problematic in case the consumer may not want to cooperate with the creditor. We therefore suggest the following wording "When the consumer goes into payment difficulties, the creditor should take reasonable steps to work with the consumer to establish why difficulties have arisen." As an alternative, other means such as phone calls or web communication should be considered as valid.

The reference to data protection legislation in this guideline gives the impression that consent is always necessary, even, for example, in the case of an intermediary communicating payment default information to credit bureaux. It should be clarified that the reference to consent relates to personal information such as the causes of default.

Guideline 3: Provision of information and assistance to the consumer

(3.1-3) Eurofinas would like to point out that this Guideline introduces additional requirements to article 28 of the MCD. In principle, we fully support the provision of information on the consequences of payment difficulties and resolutions. However, we also emphasise that personal information may also commonly be disclosed by third parties, such as charity organisations which may be able to offer advice on debt management.

(3.4) We would find it helpful if this Guideline is more specific as to the actual signposting needed for consumers in difficulty (e.g. debt advice agencies rather than general schemes to encourage house buyers).

Guideline 4: Resolution process

- (4.1) Outside the judicial framework, concessions given to consumers are at the entire discretion of lending institutions. We believe that this Guideline suggests otherwise.

It should clearly be stated that the concessions mentioned are only examples and that when forbearance is judged to be inappropriate/has been exhausted, the creditor has the right to foreclose.

Guideline 5: Documentation of dealings with the consumer and retention of records

- (5.1) This guideline goes further than the requirements laid down in article 28 of the MCD, while such stricter requirements are not necessary to achieve the objective of article 28 MCD. Furthermore, Eurofinas points out that EBA's proposal may not be consistent with "level 1" regulation.

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