EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 22 May 2013

on mortgagor protection

(CON/2013/33)

Introduction and legal basis

On 30 April 2013, the European Central Bank (ECB) received a request from the Spanish Secretary of State for Economic Affairs and Business Support for an opinion on a draft law on mortgagor protection, debt restructuring and social housing (hereinafter the 'draft law'), which was enacted by the Spanish Parliament on 8 May as Law 1/2013[1].

The ECB's competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union and the third and sixth indents of Article 2(1) of Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions[2], as the draft law relates to the Banco de España and to rules applicable to financial institutions insofar as they materially influence the stability of financial institutions and markets. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. Purpose of the draft law

The purpose of the draft law is to improve the functioning of the mortgage market by reinforcing the independence of valuation agencies and services[3], introducing a maximum 30-year repayment period for mortgage loans on principal residences if used for securitisation purposes, and improving transparency with regard to mortgage loans by requiring a mortgagor's statement that they have been warned of potential mortgage loan risks.

In addition, under the draft law foreclosure proceedings may only begin once the borrower has been in default for a minimum of three months. Moreover, the courts or the parties may challenge the foreclosure proceedings based on unfair terms in the mortgage contract. The latter amendment has been introduced to

1 Law 1/2013 entered into force on the date of its publication in the *Boletín Oficial del Estado* No 116 of 15 May 2013.

2 OJ L 189, 3.7.1998, p. 42.

3 Under the draft law, the Banco de España has powers to verify the independence of valuation agencies and services and if necessary to impose sanctions.

bring the Spanish implementation of Council Directive 93/13/EEC[4] into line with a recent European Court of Justice judgment[5].

The draft law is also aimed at protecting principal residence mortgagors by limiting default interest and introducing deductions for early repayment of their remaining debt following foreclosure.

For principal residence mortgagors in particularly vulnerable situations as defined in the draft law, the draft law provides for a two-year moratorium on evictions and, in line with the Code of Good Practices that credit institutions may voluntarily adhere to, debt restructuring and reduction measures or, should these fail, delivery of the property in lieu of payment.

Finally, the draft law requires the Spanish Government to promote the establishment of a social housing fund for the benefit of mortgagors evicted from their principal residences.

2. General observations

2.1 The ECB notes that the European Commission has adopted a proposal for a Directive that aims to promote responsible lending and borrowing and ensure that borrowers are offered affordable loans, thus reducing the need for recourse to foreclosure of properties[6]. The draft law appears to be compatible with this proposal.

2.2 It is primarily for the national legal order to balance the interests of the parties in a default or foreclosure situation as fundamental property rights and other socio-economic interests will be at stake. Also, the ECB considers that the changes to the mortgage and foreclosure legislation envisaged in the draft law should be based on a thorough assessment of their impact on the financial system[7]. In addition, in this context, the Spanish authorities should monitor the effects that the protective measures envisaged for mortgagors could have on provisions and the fulfilment of regulatory capital requirements of credit institutions.

2.3 The ECB nevertheless stresses that foreclosure should be regarded as a last resort. Secured lenders should be interested in avoiding foreclosure proceedings, which are expensive and generally generate lower proceeds than voluntary sales, where the mortgagor continues to meet all or some agreed part of their repayment obligations. It is therefore important: (a) that secured lenders adapt their current practices to deal with defaulting borrowers so as to avoid foreclose proceedings; and (b) that the regulatory framework provides incentives to all parties concerned to agree on a timely and reasonable debt restructuring in the event of a default.

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4 Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts (OJ L 95, 21.4.1993, p. 29).

5 Judgment of 14 March 2013 in Case C-415/11, *Mohamed Aziz* v *Catalunyacaixa*.

6 See the European Commission proposal for a Directive of the European Parliament and of the Council on credit agreements relating to residential property, (COM/2011/0142 final), and the accompanying Commission Staff working paper on 'National measures and practices to avoid foreclosure procedures for residential mortgage loans' of 31 March 2011, (SEC(2011) 357 final).

7 See paragraphs 2.1 and 2.3 of Opinion CON/2012/40. All ECB opinions are published on the ECB's website at www.ecb.europa.eu.

2.4 To this end, a more comprehensive set of measures that addresses the underlying causes of mortgage distress and attempts to avoid, insofar as possible, foreclosure proceedings should be pursued. Only a comprehensive resolution strategy can address the challenges that arise in the face of changed economic circumstances of borrowers, significant changes in property values and the potential for resultant unviable mortgages, whilst maintaining appropriate incentives for both the debtor and creditor, and minimising the potential for moral hazard. Equally, while the establishment of a social housing fund is to be welcomed, this initiative should form part of a comprehensive and unified strategy for dealing with mortgage distress. Such a strategy may ultimately result in fewer foreclosures and a reduced need for a social housing fund.

This opinion will be published on the ECB's website.

Done at Frankfurt am Main, 22 May 2013.

[signed]

The President of the ECB

Mario DRAGHI