Fianna Fáil submission to the Central Bank of Ireland – Consultation on "Enhanced Mortgage Measures: Transparency and Switching – CP112"

Introduction

A mortgage is in many cases the biggest financial transaction an individual or family is likely to make. Homeownership is an integral part of Irish culture for better or for worse and therefore, it is vital that we have a fully functioning, fair and transparent mortgage market.

Since 2011 with lenders leaving the market and mergers taking place the concentration of the market has risen sharply as outlined in the Household Credit Market Report published by the Central Bank.

This lack of choice in the market has major implications for both new and existing customers. With fewer choices, the ability of a new customer to shop around for the best rate and the best deal is greatly restricted. Existing customers are also finding it difficult to shop around for the best deal.

The willingness and ability to change provider is a fundamental part of any functioning market. If an individual is unhappy with their TV provider they can move. Very often the threat to move is enough for the customer to get a better deal.

Unfortunately, this is not happening in Ireland with mortgages despite the prospect of customers obtaining significant savings. Why is it that individuals are so reluctant to switch to a different mortgage provider? This is a key question that needs to be answered.

With the lack of choice for customers and inability or unwillingness to switch mortgages it means that the mortgage market is not providing satisfactory outcomes for the consumer on a range of issues.

We have seen Irish mortgage providers charging standard variable interest rates far in excess of European norms and far in excess of what is acceptable given the current low interest environment. The average interest rate on new mortgage agreements in Ireland is currently 3.37% while the European average is 1.86% nearly half the Irish rate.

We have also seen the appalling behaviour of the banks in relation to the Tracker Mortgage crisis. This highlights the major issues and dysfunction in the mortgage market in Ireland.

These are just some of the examples of a dysfunctional mortgage market that fails to offer satisfactory outcomes for customers.

The State and Government Offices and Agencies should be doing all they can to make switching a mortgage as simple and straightforward as possible. We can see that competitive forces are beginning to make an impact for new mortgage customers. However, the same cannot be said for those on existing mortgages.

While many customers choose not to switch it is also true to say that many of the banks and lenders are making it very challenging and confusing for customers to properly assess the differences in products being offered.

Transparency is needed to facilitate mortgage switching. Transparency has broadly two meanings when it comes to mortgages. There is transparency over the different products and your current product and there is transparency over the process to switch mortgages.

One is concerned with whether there is a better deal and the other is concerned with how easy it is to switch. Many people remember the difficulty in obtaining their first mortgage and assume that switching will involve the same process. As a result many are turned off even if they can get a better deal.

Enhanced transparency measures for fixed rate and variable mortgage rates based on LTV and incentives related to mortgages

For the vast majority of mortgage holders there is the opportunity to switch their mortgage. Switching can mean switching to a new product (ie between fixed and standard variable) or to a new provider or both.

In any market in order for the competitive forces to have most impact the consumer needs to be able to move to another option quickly and inexpensively. While this may be straightforward for smaller transactions it is altogether a different story when it comes to a mortgage.

Not only is a mortgage likely to be the largest financial transaction an individual is likely to take it also involves one of the most precious asset an individual is likely to own, the principal dwelling household.

These two aspects increase the stakes for customers and in turn make customers far more inert than would be the case in other markets. One of the principal reasons for such inertia is the fact that assessing the differences between various mortgage products across the market can be difficult and if an individual does not have the confidence to assess the different options then they are likely to stay put.

It is vital so that all that can be done to make the comparing of the different options easier and transparent. The website run by the Competition and Consumer Protection Commission has been a welcome initiative and this website must be publicised more in order for it to be more widely used.

However, Fianna Fáil believes that one major issue is ignored in the Consultation process.

Discrimination between new and existing customers

Currently, it is still permitted to treat new customers differently than existing customers. This has a negative impact on the market. The mortgage lenders are currently competing quite heavily for new customers. This is to be welcomed. However, as part of this they neglect and ignore existing customers.

Some lenders will offer lower rates to new borrowers and prevent existing customers from obtaining these rates. This is fundamentally unfair.

Under our Legislation, in setting variable interest rate for owner occupier mortgages, a lender would not be permitted to discriminate between existing borrowers and new borrowers.

The only permitted exceptions would be a once-off payment or discount for the purpose of defraying a cost on bona fide and vouched basis, for example the borrowers' legal costs in taking out the loans in question or switching between loan products; and/or the borrowers' liability for stamp duty in the purchase of the home in question.

Fixed Interest Rate Mortgages

For fixed interest rate mortgages the interest rate is fixed for a specific period of time. The proposals outlined in the consultation are designed to increase transparency for the customer when the fixed rate is about to expire. Broadly Fianna Fáil would be supportive of these measures. However, 30 days would seem to be a very short time before the expiry date.

Considering that the Central Bank's own research shows the reluctance of people to move. One of the reasons is that it is such a big decision or it is perceived to be such a big decision. 30 days gives someone very little time to fully assess whether they want to go to the trouble of considering a switch to a new lender.

Consideration should be given to extending this period and making it periodic. Perhaps something like informing the customer six months before the expiration and 30 days would be more beneficial.

The requirement to provide a link to the CCPC comparison website is to be welcomed as not many people are perhaps aware of its existence and its usefulness

Proposed new Provision in the Consumer Protection Code
"6.6 (f) in the case of a mortgage with a fixed interest rate, 30 days prior to the expiry of that fixed interest rate: a) a notification of the default rate of interest applicable from the expiry of the fixed rate period; and b) where the new rate applicable on expiry of a fixed rate is not a tracker interest rate: i. a summary of other mortgage rates provided by the regulated entity that could provide savings for the personal consumer compared to the default rate of interest at the time of notification; ii. details of how the personal consumer can obtain further information on the mortgage rates outlined in paragraphs 6.6 (f) (a) and 6.6 (f) (b) (i); iii. a statement that the personal consumer should keep their mortgage arrangements under review as there may be other options that could provide savings for the personal consumer; iv. a link to the relevant section on the Competition and Consumer Protection Commission's website relating to switching lenders or changing mortgage type; and v. a reminder that the regulated entity's summary statement produced in accordance with Provision 4.28a is available on its website."

Variable Interest Rates Based on LTV

For Variable Interest Rate Mortgages the problem is much more acute. The Rates on Variable Mortgages are far in excess of what is reasonable and lenders are using the fact that customers are reluctant to move as an excuse to exploit them.

The proposals outlined in the Consultation paper are a good step forward. Fianna Fáil believes that customers on variable rates should be encouraged to consistently review their LTV ratios and that customers should switch in order to avail of a better rate.

Fianna Fáil, however, believes that lenders should be obliged to automatically move a customer to a new rate as they move down the LTV scale.

Lenders are suggesting that the reason why the rates are much higher here than in Europe is because the default risks are higher. While that may be the case for higher LTV ratios, it most certainly is not for LTVs of 60 per cent or lower.

Where a customer is diligent enough to reduce their LTV to lower levels they should be rewarded. Their rate should be automatically adjusted to the rate offered to new customers at that LTV band. Many lenders are already doing this but Fianna Fáil believes everyone should be doing this.

Proposed amendment to Provision in the Consumer Protection Code
6.5 (g) in the case of a mortgage with a variable interest rate, excluding a tracker interest rate: […] “vi) if the variable interest rate is based on Loan-to-Value, a notification as to whether the personal consumer can, or cannot, move between Loan-to-Value interest rate bands subject to the provision of an up-to-date valuation; vii) if the personal consumer is permitted to move between Loan-to-Value interest rate bands, an invitation to the personal consumer to contact the lender to discuss further; and viii) if the personal consumer is not permitted to move between Loan-to-Value interest rate bands, a notification that the personal consumer may be able to avail of other options available at a lower Loan-to-Value interest rate from another regulated entity based on an up-to-date valuation.”

Use of Incentives Related to Mortgages

Fianna Fáil is very clear on the use of incentives with mortgages. This applies equally to both new customers and switchers. Lenders should be competing on rates and rates alone. Cash back offers are not designed to provide a service to customers. Rather they are designed to attract a customer and provide the illusion that they are being offered a better deal when in fact they are not.

At best this simply adds to the confusion for a customer which in turn makes it more difficult for them to assess what options are open to them. We see the same behaviour in health insurance where a customer will display more inertia the more challenging it is to assess alternative options.

If we truly want to make mortgage switching a viable option for people we need to make it easy for them to assess their options and the principal way this is achieved is by banning promotional or incentive offers like cash back offers. By doing this we are adding transparency to the market. The paying of legal fees is fine but ultimately lenders should be competing on interest rates and nothing else.

New transparency measures on potential switching savings

This initiative is very much linked to the two issues outlined above. By banning cash back offers and by banning discrimination we would be making the market much clearer for the customer. These changes coupled with the CCPC's comparison website would make the market very clear and transparent for the customer.

It would then make the measures the Central Bank is proposing in the Consultation Paper much more effective.

Fianna Fáil would be supportive of the measures outlined in the paper but in order for them to be more effective, cash back offers should be banned and discrimination between new and existing customers should be ended.

Standardised switching information

As outlined in the introduction one of the reasons customers remain inert in the mortgage market is because they assume that the switching process is as onerous as the original mortgage application.

As taking a mortgage out is perhaps the biggest transaction an individual or couple is likely to take the initial process is time consuming and stressful. The sheer reluctance of going down that road again in many cases puts people off the switching process.

This is particularly the case when there is a young family with both parents working. Every effort should be made to make the switching process more smooth.

In our submission to the CCPC on the mortgage market earlier in the year we would have called for the introduction of a Code of Conduct on Mortgage Switching not too dissimilar to the Code of Conduct on switching bank accounts.

Whether it is a new code of conduct or the use of an existing code Fianna Fáil believes that customers should be made aware of the switching process. This process should be standardised and consistent. Once people can assess the switching process then they can more accurately ascertain the cost of switching both in terms of time and stress and hassle.

Further, there should be clear timelines that must be adhered to. There is no point in informing the customer of the switching process if they are left in the dark about how long it takes.

While excluded from this consultation the time taken by third parties (i.e. solicitors etc) must be addressed. It is no use both the lender and the borrower adhering to timelines when the solicitor then takes too long to process the switch.

Once customers are clear about the process and clear about the timelines then they can more adequately decide if switching is worth it or not. We would be removing the element of doubt which currently exists where people perceive the process to be stressful.

Fianna Fáil would be supportive of the changes outlined in the Consultation Paper including reference to the CCPC comparison website which would serve to make people more aware of this service.

A time-bound switching process with specified timelines

This very much mirrors the proposals outlined above. Having definite timelines and adhering to those timelines will make it clear and transparent to the customer exactly how difficult or easy it is to switch.

Again Fianna Fáil would have called for a Code of Conduct on mortgage switching but whether a new code is developed or existing codes are changed is a small issue. The main issue is whether this is effective.

By making clear at the start of the process what documentation a customer needs to have will yet again make it easier for them to fully assess whether switching is worth it.

In addition creating a single point of contact in both the existing and new lender would make the process better.

However, we should not just be interested in making things clear. The timelines outlined in the code must be reasonable and they must be met. If a lender does not meet the deadlines and they clearly are dragging their feet then clear penalties should be imposed on that lender.

There is no use in having timelines in order for the lenders to systematically ignore them. This would undermine the entire initiative to encourage mortgage switching.

Other Issues that need to be addressed

Central Bank (Variable Rate Mortgages) Bill 2016

Our Bill would seek to address some of the issues outlined in this submission. Principally it would ban discrimination between new and existing customers. It would ban cash back gimmicks and force lenders to compete on rates and it would oblige lenders to automatically move customers onto new rates as they move down the LTV scale.

The Government believes that the market is functioning. Nothing could be further from the truth. Our rates are still far in excess of what our European counterparts pay. Our Bill will seek to cap rates. Some argue this would adversely affect competition but this simply does not make sense.

Interest rate controls currently exist in many European mortgage markets including Belgium, Cyprus, Estonia, France, Croatia, Hungary, Italy, Portugal and Slovenia.

These markets have not died off, they are still viable. The Irish market is different to other markets but it is not the Party's view that legislation to regulate the interest rates charged to mortgage-holders is unusual and would be a massively destabilising move.

In addition if the Government were truly worried about the lack of competition why have they been so slow on allowing alternative lending models into the Irish market?

The Government should be looking out for customers and not protecting mainstream banks at all costs.

Allow alternative lenders into the market

For far too long now we have relied on pillar banks to provide financial services to ordinary people including the provision of mortgages. In many instances the Government appears to be in the business of protecting the existing lenders at the expense of new potential lenders.

In this light mortgage lending from Credit Unions should be encouraged. Some Credit Unions are large enough and have a strong enough workforce to do it themselves and where appropriate they should be allowed to do so.

The Department of Finance and the Central Bank need to work to allow the larger credit unions to move into this space. This will be beneficial to the credit unions and the mortgage market and add much needed competition.

For smaller credit unions this may not be possible but where a model can be developed whereby funds are pooled to provide mortgages this again must be explored in more detail.

Public banking as used in Germany should be explored in much more detail. No movement has been made in this space either.

The Government should be in the business of looking out for the borrower and not just the mainstream banks. Like the construction sector we can no longer rely on the mainstream banks to provide for the entire market. We need to be open to new models for mortgage lending whether it is credit union lending or a form of community banking.

This would provide more options for customers and in turn make switching more beneficial.

Conclusion

The proposals in the Central Banks consultation paper would be a welcome step forward if they were to be put in place. Fianna Fáil believes the market should be made more transparent and clear for customers. If this is achieved then customers are much more likely to switch and if customers switch we will then see the market beginning to function adequately.

However, Fianna Fáil believes we can go further. By banning cash backs and other gimmicks we would force lenders to compete on rates alone. By banning discrimination between new and existing customers we would be linking the inert part of the market to the more competitive active market for new customers.

We also believe that alternative lending models should be introduced. The State should be in the business of looking out for customers and not serving the needs of mainstream banks.