Implementation of the Mortgage Credit Directive – the scope of changes, issues of concern and their potential impact on the Polish mortgage sector

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Abstract:
In February 2014, the European Parliament approved the text of a new Mortgage Credit Directive, ending more than two years of work on the unification of the mortgage market in Europe. EU Member States have had two years to adapt their national legislations to the new requirements – the deadline for implementation of the Directive expires in March 2016. Although the final version of the Directive, whose aim is to harmonize and raise the standards of offering mortgage loans in the EU, was made significantly more relaxed relative to the original assumptions, this does not mean that implementation of the new regulations will be easy for the financial sector.
The purpose of this article is to present the main provisions of the Mortgage Credit Directive, its planned implementation into Polish law and the major challenges related to the process.

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1. ORIGIN OF THE MORTGAGE CREDIT DIRECTIVE

On 04/02/2014, the European Parliament adopted the Directive on credit agreements for consumers relating to residential immovable property (hereinafter: the Mortgage Credit Directive/MCD)[1]. Its adoption ended almost 10 years of work aimed to strengthen the integration of the EU mortgage market. Although initially regulation of the mortgage market via a Directive was not anticipated and the priority was to achieve a situation where the same mortgage credit is offered to consumers throughout the EU at the same price, the outbreak of the financial crisis of 2007–2008 changed that viewpoint. At first, regulators' attention was focused on the issue of banks' access to sources of cheap funding and cross-border activities of financial institutions, then, on issues of consumer protection and responsible mortgage lending. According to regulators, the introduction of the arrangements provided for in the Directive should "improve conditions for the establishment and functioning of the internal market through approximation of legislations and adoption of quality standards and promotion of good practices."[2]

The thus deepened definition of the Directive's purpose caused the scope of the regulation, as provided for in the act, to be very broad. The Directive not only extends its scope over all the entities that may be involved in mortgage credit service (some will be regulated for the first time) but will also apply to all stages of the credit life – from advertising and general information about mortgage credit, through the terms of credit offering and lending, ending with credit repayment and foreclosure. Given the above, it is clear that although the act does not directly regulate the parameters affecting lending policies of banks, such as limits on LTV/DTI or the maximum duration of the loan, the Directive may nonetheless have a significant impact on the shape of the credit market in the coming years.

[1]Cf. text of the Directive 2014/17/EU: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0017&from=EN
[2]Recital 8 in the preamble to Directive 2014/17/EU.

2. Current legal regime for housing loans in Poland and the scope of incoming changes

In addition to general regulations governing lending, as outlined in the Banking Law (in particular in Articles 69-79), loans secured by mortgages granted to consumers have been subjected to the regime of the Consumer Credit Act (hereinafter: CCA). It should be emphasized that only 6 articles of the act apply to mortgage loans, in particular those which regulate: the scope of pre-contractual information and the manner of its transmission in a standardized Information Form (annexed to the act), the requirement to conclude the credit agreement in writing, the scope of the mortgage credit agreement and the free credit sanction. It is worth noting that the CCA application to mortgage credit was related to implementation of the Consumer Credit Directive (CCD) in Poland[3]. Although mortgage-backed loans were excluded from the scope of the CCD, the national legislature had the opportunity to make those loans fall under provisions compatible with the Directive. This was the approach adopted by Polish legislature, opting to make mortgage credit partially subject to the Consumer Act regime. With this solution, a mortgage consumer was to be guaranteed a similar level of protection as that for consumer credit, all the more so that mortgage loans involve considerable long-term financial burdens.

Discussing the scope of regulations on mortgage credit in effect in Poland to date one cannot omit "Recommendation S on good practices in the management of mortgage-secured credit exposures." The first version of Recommendation S was published by the Polish Financial Supervision Authority in 2006, since then – in response to changing market realities – it has been amended three times. Although PFSA recommendations do not belong to the catalogue of generally applicable legislation, and their range is restricted solely to lenders supervised by the PFSA, these regulations are widely used by the industry, having a significant impact on banks' lending policies. In this context, one notes especially: (i) the credit limits imposed by Recommendation S (reducing both LTV and the maximum loan maturity; earlier versions of the regulation also included a limit on DTI); (ii) regulations concerning the rules of conduct with a mortgage consumer (including information on mortgage credit risks); (iii) strict guidelines on the structure of the bank (including the requirement to separate sales and credit risk assessment departments within the bank) and remuneration of the employees offering mortgage credit. Already existing provisions of Recommendation S largely coincide with the new requirements introduced by the MCD.

[3]Earlier, the CCA applied only to mortgage credit below PLN 80,000.

As a rule, offering mortgage credit in Poland is already subject to quite specific rules, however, the wide scope of the new Directive means that its implementation into national law will nevertheless not be an easy task. It is worth noting that even at the current stage of work, a fundamental change has been made in the philosophy of the MCD implementation; initially, law-makers planned to do this by developing a new act on mortgage credit, comprehensively covering the range delineated by the Directive.[4] At a later stage, this concept was changed; it was decided that MCD implementation would be made by amending the Consumer Credit Act and by adopting a new act on the activities of loan institutions and credit intermediaries.[5] According to law-makers, that solution will ensure greater regulatory transparency for consumers; still, some problems may arise from the fact that the credit act will not be symmetrical – i.e. due to the fact that the MCD has a much wider scope than the CCD – the credit act will place much greater emphasis on mortgage credit.

It should be noted that the Polish legislature decided to take avail of the opportunity to broaden the scope of the regulation, as provided for in Recital 13 of the MCD, extending it to all mortgage loans concluded with the consumer (and not just housing loans), excluding specific types of credit, as indicated in the directive. Where it comes to entities covered by the new act, it will apply to banks, credit unions (SKOKs) and credit institutions; for the first time, the regulation will apply to credit intermediaries and appointed representatives; the act will also affect the activities of institutions overseeing the market, i.e. PFSA and UOKiK (Office of Competition and Consumer Protection).

The purpose of this analysis is to trace the major changes that will be brought about by the regulation on the mortgage lending market for consumers and their consequences for the banking sector in Poland.

[4] Cf. draft assumptions for the act on loans related to immovable property of 06/02/2015 – http://legislacja.rcl.gov.pl/docs//1/12269251/12275741/12275742/dokument149564.pdf

[5] Cf. the version of the draft assumptions for the act on activities of lending institutions and credit intermediaries, which will also provide for amendments to the Consumer Credit Act of 8/10/2015 – http://legislacja.rcl.gov.pl/docs//1/12269251/12275762/12275763/dokument188192.pdf

3. ANALYSIS OF SELECTED PROVISIONS OF THE NEW DIRECTIVE WHICH ARE OF KEY IMPORTANCE FOR THE MORTGAGE SECTOR

3.1. Knowledge and competence requirements for staff

Bearing in mind the need to ensure professionalism in offering mortgage loans, the text of the Mortgage Credit Directive emphasizes the requirement to demonstrate an adequate level of **knowledge and competence of banks'/credit intermediaries' staff** [6]with regard to offering, drafting and concluding credit agreements (Article 9). Member States will be required to establish minimum competence requirements the scope of which has been established in the act. It should be emphasized that the competency requirements for staff are specifically (although broadly) identified and made subject to cross-border harmonization. As prescribed in Annex III of the Directive, the minimum competence requirements must include at least the following:

a) appropriate knowledge of credit products within the scope of the Directive and the ancillary services typically offered with them;
b) appropriate knowledge of the laws related to the credit agreements for consumers, in particular consumer protection;
c) appropriate knowledge and understanding of the immovable property purchasing process;
d) appropriate knowledge of security valuation;
e) appropriate knowledge of organization and functioning of land registers;
f) appropriate knowledge of the market in the relevant Member State;
g) appropriate knowledge of business ethics standards;
h) appropriate knowledge of the consumer's creditworthiness assessment process or where applicable, competence in assessing consumers' creditworthiness;
i) appropriate level of financial and economic competency.

According to the assumptions for the act implementing the MCD, by 21/03/2019 the condition that will meet the requirements of appropriate knowledge and competence is to have a minimum of five years proven experience associated with the conclusion of credit agreements relating to immovable property or to have the appropriate qualifications evidenced by diplomas. At an earlier stage of work on the draft act the above "appropriate

[6] According to the definition set out in the Directive (Article 4), "staff" means "any natural person working for the creditor or credit intermediary, who is directly engaged in the activities covered by this Directive or who has contacts with consumers in the course of activities covered by this Directive."

qualifications" were narrowed down to economic or legal training, but then the limitation was rightly abandoned. At the same time, even in the transitional period, the employer will be able to send its employees to training whose thematic scope will coincide with the requirements of Annex III of the Directive and to test competency. After the transitional period, the only way to meet the requirements regarding knowledge and competency is to take part in training, ending with an exam. It should be noted that, at this stage, the legislation provides that employees will have to undergo the training every year!

From the point of view of the banking sector, compliance with the new training requirements will cause several fundamental problems. First, given the very wide range of staff subject to the training requirement the cost of the undertaking will be very high. At the same time, it must be emphasized that, although according to Section 2 of Annex III, Member States may vary training requirements for staff members, for the time being the assumptions for the act do not provide for such a solution. Here, the question arises whether it is appropriate to require e.g. an employee assessing consumer's creditworthiness to have knowledge of the land registry. At the same time, further clarification is required with regard to the need for annual training, i.e. whether for those who have already received training a year earlier another course would be meant to refresh previously assimilated material or whether staff must undergo the entire training anew.

3.2. Information provided to consumers

Stressing the need to enhance consumers' ability to make informed decisions in the area of responsible borrowing, the MCD has broadly regulated the catalogue of information to be communicated to the mortgage credit consumer. The Directive introduced rules for the transmission of information to the consumer at three stages: (i) advertising, (ii) general information about the credit offer; (iii) standardized pre-contractual information.

The standard range of information communicated in **advertising** (Article 11 of the Directive) provides that the consumer should be provided "in a clear, concise and prominent way" with the following information:

a) name of the creditor/credit intermediary;
b) where applicable, that the credit agreement will be secured by a mortgage or another comparable security on residential immovable property;
c) the borrowing rate, indicating whether this is fixed or variable or a combination of both, together with particulars of any charges included in the total cost of the credit to the consumer;

d) the total amount of credit;
e) the APRC (with a special indication that the APRC will be included in the advertisement at least as prominently as any interest rate information);
f) where applicable, the duration of the credit agreement;
g) where applicable, the amounts of the installments;
h) where applicable, the total amount payable by the consumer;
i) where applicable, the number of installments;
j) where applicable, a warning about the currency risk.

The text of the act emphasizes that the above information should be clearly readable/audible, but does not specify any minimum requirements in this regard. The Polish legislature has decided to clarify the requirements somewhat, stipulating that "the font used, and the time within which the information is displayed must allow it to be read by the consumer." Still, given the fact that the scope of the advertising information is very broad, a concern arises whether the message would even be readable for consumers. Additionally, one should bear in mind that according to the PFSA guidelines "all relevant elements of the advertising message (specifically those required by law) should be tailored to the specific nature of the medium used for its dissemination."[7] In addition, the omission of required information in an advertising message or placing it in such a way that would prevent it from being easily read/heard constitutes, according to the PFSA (and UOKiK), an advertising message which might be misleading. Given the above, it cannot be precluded that once the new regulations on credit secured by immovable property enter into force advertising will focus solely on the press.

An advertising message should be based on a **representative example,** on the basis of the criteria adopted by the Member State. In the case of Poland, provisions of Article 8(2) of the Consumer Credit Act will apply here, which stipulate that "When determining the representative example, it is necessary to define the terms of a consumer credit agreement on which the creditor or the credit intermediary expects to conclude at least 2/3 of the contracts of that type, with the agreements taking into account the average financing period, the total credit amount and the incidence of contracts of that type on the market." At this point, it should be emphasized that the current wording of the assumptions for the Credit Act indicates that when determining the representative example account must be taken of the

[7]Cf. letter of the Polish Financial Supervision Authority of 13 April 2012:- Standards of care in designing advertising information about consumer credit, Ref. DOK/WPR/0735/5/1/12/BK, https://www.knf.gov.pl/Images/stanowisko_ws_reklam_ZBP_KZBS_13_04_2012_tcm75-30286.pdf

conditions of the credit agreement secured by immovable property, based on at least 2/3 of contracts of that type that are in the portfolio of that creditor..." It is not clear whether these tighter rules for determining the representative example (expected contracts vs. agreements actually concluded) were intended by the legislature or resulted from an editorial error; if the former, it is not clear how often to update the data about the type of contracts existing in the creditor's portfolio; assumptions for the draft act do not, for the time being, provide any clarification in this regard.

Apart from the information conveyed in advertising, Member States will also be required to ensure that **general information about credit agreements** is made available to consumers by creditors/intermediaries at any time on paper/electronically/on another durable medium. The Directive specifies a detailed and wide scope of such general information. New features introduced by the Polish law implementing the MCD include an obligation imposed on creditors to publish current regulations and the credit agreement template on their website. Furthermore, under the new requirements, at a written request of the consumer, the creditor will need to provide a copy of the credit decision sent to the credit intermediary – this solution is to prevent unfair practices where an intermediary recommends to a customer a credit offer which is more beneficial for the intermediary, arguing that the consumer has no creditworthiness at other banks.

A revolution, introduced by the Mortgage Credit Directive, is to be the adoption of a unified catalog of **pre-contractual information** provided to the consumer prior to conclusion of a credit agreement, having the form of a "European Standardised Information Sheet" attached as Annex II to the Act (the Form is subject to maximum harmonization).

Pre-contractual information in a tabular form is to be provided to the customer: (i) without undue delay, once the consumer delivers the required information necessary to complete the form; (ii) prior to conclusion of a credit agreement. At the same time, the act introduces a caveat that a credit offer must be accompanied by an information sheet if it has not already been provided or if the **characteristics** of the offer differ from the information contained in the previously submitted ESIS. Unfortunately, the Directive does not specify the term "characteristics" used in the above context. It is worth noting that an attempt to clarify the above definition was made at early stages of work on the assumptions.[8] It was indicated

[8]Cf. the assumptions for the Act, dated 18/06/2015, p. 28.

at the time that "the characteristics of an offer shall be construed as, among other things, main features of a loan, interest rate, the frequency and number of payments, the amount of each installment or other characteristics whose alteration will change credit parameters." In this context, it should be noted, however, that – given the size of the ESIS – requiring banks to re-submit the table in the case of changes in credit interest rates would be very costly to them, while providing no added value for the consumer. At the stage of work on the draft act it would be recommended to indicate that a change of offer characteristics would include a change of the credit margin or a change of the type of reference rate (e.g. from WIBOR 3M to WIBOR 6M) – and not a nominal change of the credit interest rate.

In the context of the obligation to provide pre-contractual information, essential to the Polish market will be the **transitional period** provided for in Article 14 (5) of the Act, according to which the Member States which, before the effective date of the Directive, "have implemented an information sheet that meets equivalent information requirements (...) may continue to use it until 21 March 2019." Although the Information Sheet used in Poland (under the Consumer Credit Act) for a mortgage credit contains the scope of information similar to that of the ESIS the Polish legislature decided that banks would only have a 12-month transitional period calculated from the effective date of the Act. According to the MF (Ministry of Finance), the new form is much more transparent and more accurate, moreover – as compared to the one currently used – it contains new information: on the provision of advisory services, on the intermediary's remuneration, a simulation of each installment amount.

Given the expenditures related to implementation of information forms into banking procedures (in particular IT costs), it seems that, in order to reduce the total cost of implementing the MCD in Poland, it would be more appropriate to extend the transitional period as far as possible, allowing the use of the old information form for mortgage credit. It is bizarre that on the one hand, the law-markers argue that faster implementation of the new form constitutes an added value for the consumer, while on the other hand, they state explicitly (in the context of loans in foreign currency) that pre-contractual information does not work for many customers – cf. "Identification of information requirements does not reduce risks because – as practice shows – many borrowers did not understand and in the future probably will not fully understand the specifics of the credit liabilities incurred, including the sources of risk..." [9]

[9]Page 42 of the assumptions.

3.3. Reliable rules for mortgage lending

The new Directive contains general rules meant to ensure that while offering mortgage credit to consumers creditors/intermediaries observe the **rules of business ethics**. In particular, the Directive instructs in Article 7 to act “honestly, fairly, transparently and professionally” in a relationship with the consumer. At the same time, the regulation introduces a requirement that **staff remuneration systems** do not impede compliance with the above requirement and be consistent with the risk management policy. It is stated clearly that remuneration policies for staff responsible for assessing creditworthiness should not prejudice their ability to act "in the best interest of the consumer." While it seems that the requirement existing in Poland to separate the functions of sales and credit risk assessment generally satisfies this condition[10], in the assumptions for the Act the legislature has decided to clarify that the incentive system for creditor/intermediary staff "should not be dependent solely on sales targets but should be linked to risk management through measures including compliance with internal risk mitigation regulations and compliance with internal credit standards."

Although, under the Directive, Member States may “prohibit or impose restrictions on payments from a consumer to a creditor or credit intermediary prior to the conclusion of a credit agreement” the Polish law-makers have decided not to take avail of this option. To increase transparency, however, a proviso was added, that the information on the remuneration earned by an intermediary from a given bank is public and should be provided to the consumer (no later than with the ESIS). It should be noted that the intermediary will be required to inform the consumer not only about the commission received from creditors but also about "all remuneration paid by a particular creditor, directly and indirectly dependent on the signed agreement"! The problem in this context is the fact that each intermediary will provide the consumer with this information according to their own methodology and based on the cooperation model used with the bank, i.e. some remuneration rates will be given in PLN while others as percentages, which will in turn prevent the consumer effectively from comparing those values. There is a great danger that the new consumer right to obtain information will in practice be dead.

[10]According to PFSA Resolution No. 258/2011 on detailed rules of operation of the risk management system and internal control system, and the specific requirements for internal capital assessment by banks and for review of the internal capital assessment and maintenance process, and the rules of setting a policy of variable remuneration components for persons holding managerial positions at a bank, https://www.knf.gov.pl/Images/uchwala_258_tcm75-27888.pdf .

The Mortgage Credit Directive clearly differentiates the issue of providing information/clarification to customers from provision of **advisory** services to customers. “Advisory services” means the provision of personal recommendations to a consumer in respect of one or more transactions relating to credit agreements and constitutes a separate activity from the granting of a credit and from the credit intermediation activities. Prior to the provision of advisory services to a consumer, it is necessary to provide information on a fee for the service and on the basis for the recommendation given (the bank's own products or products from the entire market). At the same time, Member States may require that providers of advisory services have an obligation to alert consumers when – considering the financial situation of the consumer – the credit agreement can cause a particular risk for the consumer (however, what a "particular risk" is or what sanctions apply for lack of such a warning have not been specified). Polish law-makers decided not to take avail of this possibility, arguing that it is for the borrower to thoroughly examine the consumer’s ability to repay liabilities, while those providing advisory services may be unable to perform a more detailed analysis, hence, conferring on them the obligation to provide additional warnings is unfounded. In order to emphasize a clear division between advisers and other market participants, it was decided instead to ban the use of the term "adviser" and "advisory services" in a situation where advisory services are offered to consumers by creditors/credit intermediaries.

An entirely new issue from the point of view of the Community market, but which does not usher a revolution on the Polish credit market,[11] is the establishment of the **obligation to assess consumers' creditworthiness** before concluding a credit agreement and to grant the credit only if the result of this assessment indicates that the obligations arising from the credit agreement are likely to be performed as required by the agreement. If a credit application is rejected by the bank the information to that effect should be communicated immediately to the consumer, however, it should be stressed that the customer needs not be informed about the reason for the negative outcome of the creditworthiness assessment (Polish law-makers considered the introduction of such a provision but eventually refrained from it). The text of the Directive itself does not provide for stricter regulation of the rules for assessing consumer's creditworthiness but it should be borne in mind that the guidelines on

[11]According to **Article 70 (1)** of the Banking Law.

this issue had already been issued by the European Banking Authority (EBA).[12] In its recommendations, the EBA notes that in order to properly fulfill the provisions of Article 18 of the MCD, banks should consider the following requirements:

1. Verification of consumer's income,
2. Storage of relevant documents for the assessment of creditworthiness (at least for the duration of credit life),
3. Preventing mistakes and misrepresentations that could disrupt the process of assessing creditworthiness,
4. Examination of the consumer's ability to meet the obligations arising from the credit agreement,
5. The need to take into account consumer's fixed expenditures in assessing his creditworthiness,
6. Taking into account possible negative scenarios in the assessment of creditworthiness.

As a rule, the new requirements of the Directive do not differ substantially from those already existing in Poland, it should be noted, however, that procedures for assessing creditworthiness used by the banks offering housing loans require amendments. As noted by the Polish Financial Supervision Authority, where a buffer rate was applied by banks (data for December 2014), as many as 19 banks (out of 23 analyzed) used a buffer rate lower than 3 percentage points, of which 7 banks assumed an interest rate growth not higher than 1 percentage point! In addition, a practice often used by banks is to lower customer's living expenses to a level inadequate to the costs actually incurred by the borrower and his family; over 47% [of loans] in 2014 were granted on the assumption that the borrower's living expenses were at or lower than the minimum subsistence level.[13] Bearing in mind the need to implement new regulatory requirements, and above all, the sector stability, banks should modify the above practices in assessing consumer creditworthiness.

3.4. Foreclosure

Due to the diversity of national rules on foreclosure and social sensitivity of the subject, for many years now it has remained outside the scope of Community regulations.

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[12] *Final report on guidelines on creditworthiness assessment, EBA*, June 2015 https://www.eba.europa.eu/documents/10180/1092161/EBA-GL-2015-11+Guidelines+on+creditworthiness+assessment.pdf

[13] *Report on the situation of banks in 2014,* PFSA Office, Warsaw 2015, pp. 77-81, https://www.knf.gov.pl/Images/RAPORT_O_SYTUACJI_BANKOW_2014_12_tcm75-41472.pdf

The outbreak of the financial crisis, however, has prompted the European Commission to address the situation of overindebted consumers having problems with credit repayment and those evicted from immovable property. The EC began to emphasize that: (i) foreclosure should be used as a last resort, (ii) if there are signs that the consumer has problems with servicing the loan, it is advisable to establish a dialogue to solve the problem (e.g. to renegotiate the repayment period or other terms of the credit), (iii) if the dialog fails, one should consider advisory services for the consumer on debt management.[14] Also the MCD text speaks in this vein; rather than focusing on the foreclosure process it advises banks to adopt practices that take into account the consumer's plight and will not allow a debt circle to arise[15].

According to Article 28, Member States should adopt measures to encourage creditors to "exercise reasonable forbearance before foreclosure proceedings are initiated." In addition, countries can impose on creditors a requirement that any charges arising from a default are "no greater than is necessary to compensate the creditor for costs" it has incurred as a result of the default (or Member States may place a cap on such charges). At the same time the directive calls on the Member States to adopt procedures to enable the best efforts price for the foreclosed immovable property to be obtained.

Implementing the provisions of Article 28, the legislature decided to require banks to undertake restructuring measures before foreclosure initiation. Under the new rules, a consumer who defaults on a loan will be asked to pay the overdue amount within a maximum of 14 days, also the request should inform the consumer about the right to apply for debt restructuring (the application must be made within 14 days of receipt of the request). If the consumer files such an application the creditor may examine whether restructuring is justified given the financial situation of the consumer. If the application for restructuring is rejected the customer should be fully informed about the reason for the rejection[16].

If the customer does not consent to/qualify for restructuring (or it has not been effective) the next step is to sell the property. And again – first, the customer must be allowed to sell to the best bidder, as a solution financially most optimal for the customer. In

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[14] *National Measures and practices to avoid foreclosure procedures for residential mortgage loans*, SEC (2011)357, European Commission, 2011 http://ec.europa.eu/internal_market/finservices-retail/docs/credit/mortgage/sec_2011_357_en.pdf.

[15] A similar tone is found in the recommendations of the European Banking Authority (EBA) – cf. *Opinion of the EBA on good practices for the treatment of borrowers in mortgage payment difficulties*, EBA, June 2013 https://www.eba.europa.eu/documents/10180/604521/EBA+Opinion+on+Good+Practices+for+Borrowers+in+Payment+Difficulties.pdf

[16] It is worth noting that the last amendment of the Banking Law requires banks to allow (under certain conditions) debt restructuring for all – not just mortgage – credit, cf. Article 75 c of the Act of 25 September 2015 Amending the Banking Law Act and other acts, http://orka.sejm.gov.pl/proc7.nsf/ustawy/1441_u.htm

their current wording, the assumptions do not clarify the issue of the property sale by the consumer on the market; this should certainly be done at the stage of work on the act. In particular, it is necessary to indicate the maximum period during which the consumer should transact the sale of the property. Otherwise, a situation may arise where the consumer theoretically puts the property for sale but prices it considerably too high, thus precluding chances of actually selling it, while the bank will not be able to foreclose because of being "required to allow the consumer to sell the property."

Foreclosure will only be the last stage of proceedings at the bank in the absence of debt service. If after selling the property the consumer still has an outstanding debt the creditor should enable repayment in installments tailored to the consumer's income.

In this context, it should be borne in mind that also the issue of foreclosure has become an object of interest to the EBA. In June 2015, the EBA issued a set of recommendations accompanying Directive 2014/17/EU[17] which banks should implement by 21/03/2016. The EBA guidelines require banks to undertake, among others, the following measures:

1. Implementation of relevant policies and procedures (early detection of consumers that may have problems with repayment and appropriate procedures for handling consumers who have problems with repayment);
2. Cooperation with the consumer (e.g. respect for consumer privacy, appropriate communication with the consumer);
3. Information and support for the consumer;
4. Restructuring (taking into account the individual circumstances of the consumer);
5. Documentation (the bank must demonstrate why the restructuring measures are appropriate for the consumer; records should be archived for a reasonable time).

A significant change will also be made with regard to the possibility of charging interest on **overdue debt** (implementation of Article 28(3)); the Polish legislature decided to ban the use of additional debt collection charges beyond default interest. This means that default interest must be sufficient to cover the cost of debt collection from immovable property. Given the fact that a similar view (debt collection charges cannot be higher than penalty interest) was already expressed by the Court of Competition and Consumer

[17] *Final report on guidelines on arrears and foreclosure, EBA*, June 2015 https://www.eba.europa.eu/documents/10180/1092172/EBA-GL-2015-12+Guidelines+on+arrears+and+foreclosure.pdf/a16dfe3a-932c-4ff3-b4ff-8cf9f54799ca

Protection[18], this regulation should not be a surprise. The previously advocated approach, i.e. the assumption that debt collection fees cannot be higher than the costs incurred by the creditor as a result of default, was rightly opposed by the SOKiK since the consumer has no knowledge about the costs actually incurred by the bank in the foreclosure process, and therefore he cannot verify whether the charges imposed on him are excessive or not.

It should be noted, however, that the regulations on foreclosure must be absolutely fine-tuned at a later stage of work on the act. The lack of precision in implementing these regulations would significantly weaken the effectiveness of the mortgage security, which in the long term could translate into a more costly mortgage credit and rating downgrades for Polish covered bonds.

3.5. Regulations concerning credit intermediaries

One of the heavily accented themes in the new Directive is the necessity to extend the regulation over credit intermediaries involved in mortgage lending. The activities of credit intermediaries had already attracted interest of the European Commission before the outbreak of the financial crisis; when developing the final text of the Directive it was stressed that irresponsible behavior of some market participants (including credit intermediaries) as well as "inefficiency, inconsistency or lack of systems for credit intermediaries"[19] are problems which harm the EU's internal market. Considering the above, the Act introduced a number of regulations relating solely to intermediaries[20], including with respect to: (i) information obligations toward consumers, (ii) the requirements for admission of intermediaries and possible revocation of licenses, (iii) freedom to provide services by intermediaries, (iv) regulation of the supervision of intermediaries.

The **definition of an intermediary** used in the Directive (Article 4 (5)) is similar to the definition used in Article 3 (f) of the Consumer Directive: "Credit intermediary" means a natural or legal person who is not acting as a creditor or notary and not merely introducing, either directly or indirectly, a consumer to a creditor or credit intermediary, and who, in the course of his trade, business or profession, for remuneration, which may take a pecuniary form or any other agreed form of financial consideration:

(a) presents or offers credit agreements to consumers;

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[18] Cf. e.g. judgment of the Warsaw Regional Court of 11-03-2013, Ref. XVII AmC 1622/12, http://orzeczenia.ms.gov.pl/content/$N/154505000005127_XVII_AmC_001622_2012_Uz_2013-03-11_001

[19] Recital 4 in the preamble to the Mortgage Credit Directive.

[20] It is important to note that intermediaries are also subject to regulations addressed both to them and to creditors (usually requirements regarding relationships of those entities with consumers).

(b) assists consumers by undertaking preparatory work or other pre-contractual administration in respect of credit agreements other than as referred to in point (a); or

(c) concludes credit agreements with consumers on behalf of the creditor."

The Mortgage Credit Directive has also added a new category, "tied credit intermediary", which means "any credit intermediary who acts on behalf of and under the full and unconditional responsibility of:

(a) only one creditor;

(b) only one group[21]; or

(c) a number of creditors or groups which does not represent the majority of the market."

According to Article 34 of the Mortgage Credit Directive, credit intermediaries are subject to supervision by the competent authorities of the home Member State.

As mentioned above, a big revolution on the intermediation market might be the obligation to provide the consumer (before performing any activities related to credit intermediation) with information about the **existence of a commission** and – as far as is known – the amount of commissions or other incentives paid by the creditor or third parties to the credit intermediary for the intermediary's services relating to the credit agreement. Where that amount is not known at the time the information is provided the credit intermediary will inform the consumer that the actual amount will be disclosed at a later stage in the ESIS[22]. As already indicated above, it cannot be precluded that because of the different models of remunerating intermediaries, which used in the market, this information will not be sufficiently clear to the consumer.

The new Directive requires intermediaries to **obtain admission** issued in the home Member State by the competent authority. It will be issued subject to fulfillment of at least the following requirements: (i) possession of professional indemnity insurance by the intermediary, (ii) good repute of the natural person/members of the board of a credit intermediary established as a legal person, (iii) an appropriate level of knowledge and competence in relation to credit agreements as described above. All admitted credit intermediaries will be entered into a register which will be kept up to date and will be publicly available online. At least two of the above requirements can be problematic for

[21]"Group" means here a group of creditors who are subject to consolidation for the purposes of consolidated accounts as defined in Directive 2013/34/EU.

[22] Even if the amount of the intermediary's commission has been communicated to the consumer at the initial stage of the relationship, it should also be stated later in the ESIS.

intermediaries. First, as already mentioned above, the requirements in terms of **knowledge and competence**, as provided for by the Directive, are very broad and require annual updates (or retraining), which can be very costly. At this stage, it is difficult to anticipate the actual availability of this type of training for smaller financial intermediation companies, especially those located outside large urban centers. It is also not clear whether these intermediaries in general have been aware of upcoming changes and the resulting need for them to undergo training. Most likely, in the long term, the market will self-regulate, i.e. banks will only be interested in working with intermediaries entered in the PFSA register and prerequisites for entry will include completion of the relevant training; it is not clear, however, how long such adaptation to the new requirements will take and what the process of eliminating intermediaries unwilling to adjust to the new requirements will look like and how effective it will be.

Another issue problematic for intermediaries will be the need to obtain **indemnity insurance**. Terms of insurance have been harmonized throughout the EU under Delegated Regulation No 1125/2014[23], according to which the minimum amount of insurance has now been [24]set at EUR 460,000 for each individual claim; a total of EUR 750,000 per calendar year for all claims. Given the fact that the above amounts will not vary by the home Member State of the intermediary/the size of its activities, etc., the new requirements for insurance may turn out to effectively remove smaller intermediaries from the market, which has already been pointed out by the Polish Chamber of Insurance expressing its opinion on the above regulation[25]. In addition, one has to consider the worst case scenario, i.e. a situation where none of the insurance companies operating in Poland will be interested in launching such insurance (at least in the initial period of the new regulation); neither the Directive nor the delegated regulation specifies what intermediaries, for whom possession of the insurance is a condition for doing business, should do in such a situation.

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[23] *Commission Delegated Regulation (EU) No 1125/2014 of 19 September 2014 supplementing Directive 2014/17/EU of the European Parliament and of the Council with regard to regulatory technical standards on the minimum monetary amount of the professional indemnity insurance or comparable guarantee to be held by credit intermediaries,* http://eur-lex.europa.eu/legal-content/PL/TXT/?uri=CELEX:32014R1125

[24] The above figures are to be reviewed by the Commission every two years

[25] *Consultation on Professional Indemnity Insurance (PII) for mortgage credit intermediaries (EBA/CP/2013/46), Responses: Polish Insurance Association:* http://www.eba.europa.eu/regulation-and-policy/consumer-protection-and-financial-innovation/draft-regulatory-technical-standards-rts-on-professional-indemnity-insurance-pii-for-mortgage-credit-intermediaries?p_p_auth=KKGTXww7&p_p_id=169&p_p_lifecycle=0&p_p_state=maximized&p_p_col_id=column-2&p_p_col_pos=1&p_p_col_count=2&_169_struts_action=%2Fdynamic_data_list_display%2Fview_record&_169_recordId=628370&_169_redirect=http%3A%2F%2Fwww.eba.europa.eu%2Fregulation-and-policy%2Fconsumer-protection-and-financial-innovation%2Fdraft-regulatory-technical-standards-rts-on-professional-indemnity-insurance-pii-for-mortgage-credit-intermediaries%2F-%2Fregulatory-activity%2Fconsultation-paper

Under the new requirements, the sector of financial intermediation is to be supervised by the PFSA, the supervision not to consist solely of registration, therefore, the regulator will be entitled to verify compliance with the requirements for admission and fulfillment of the obligations imposed on the intermediary. However, given the degree of fragmentation of the financial intermediation sector in Poland, implementation of these tasks can be extremely difficult in practice.

4. Conclusions

Despite many years of work to integrate the mortgage lending market in the EU, it does not seem that the Mortgage Credit Directive has contributed significantly to the creation of an internal market for mortgage credit or has led to a significant increase in the degree of protection for consumers taking housing loans. The Directive is largely an extensive collection of good practices but does not contain enough concrete recommendations which could actually eliminate adverse market practices. On the other hand, implementation of the directive requirements will be quite costly from the point of view of the credit sector, and in the case of smaller operators active in the financial intermediation sector, may lead to their elimination from the market.

Without a doubt, the greatest effort for the market will be – at least initially – the need to adapt to new educational requirements; also the necessity to adapt to the changed disclosure requirements will require significant investment. It is not clear, however, whether the new requirements will actually improve the quality of the mortgage credit portfolio in Poland.

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Implementation of the Mortgage Credit Directive – the scope of changes, issues of concern and their potential impact on the Polish mortgage sector

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