



**To the members of the
European Federation of Building Societies**

Brussels, 7 May 2012
CK/WM

Global minimum standards of the Financial Stability Board for Sound Residential Mortgage Underwriting Practices ("FSB Principles for Sound Residential Mortgage Underwriting Practices")

Dear Member,

After the consultation in November 2011, on which occasion the EFBS has sent a position paper, the Financial Stability Board (FSB) has published on 18 April 2012 the principles on sound mortgage underwriting practices.

The FSB was founded in 2009 by the former G7 finance ministers and the governors of the central banks to develop and propose international supervisory standards. During the conference of the representatives of the G20 states in April 2009 the FSB was asked to support stability in the financial sector. In March 2011, the FSB has already published a review on the different residential mortgage underwriting practices. In November 2011, the FSB has enquired the interested public concerning the planned principles on mortgage underwriting practices.

In a position paper on 5 December 2011 the EFBS welcomed that the FSB has in general drawn the right conclusions from the crises in 2008. The EFBS recalled in its position paper that housing finance by home loan contracts ("Bausparverträge") complies with the capital requirements to secure the financing set up by the FSB. The EFBS also pointed out in its position paper that credit institutions may continue themselves to conduct real estate valuation as a separate process from the credit process.

The now published international principles of the FSB may influence the European discussion on the regulation of the mortgage credit as well. They focus on the effective verification of income and other financial information, on reasonable debt service coverage, appropriate loan-to-value ratios, effective collateral management and prudent use of mortgage insurance. The FSB complies with the EFBS that sufficient equity capital in the financing of residential property assures the complete financing. But the FSB does not prescribe to the supervisory authorities fixed loan-to-values (LTV). The principles also provide that the loan-to-value shall consider the real value of available equity. Lenders shall refrain from relaxing LTV ratios at the time of a boom in the property market.

With regard to the standards of the creditworthiness assessment the principles provide that the lender shall consider sufficient financial means for the costs of living while calculating the credit rate and the interest charge. The income and the financial situation of the borrower shall be revised by means of third parties' verification. The consumer shall receive clear, comprehensive and comparable information before the conclusion of the contract, in particular concerning the interest change risk and the combined products.

Regarding the real estate valuation the principles do not provide an outsourcing of the real estate valuation on a third party but the creditor shall generally inspect the property himself. The property appraisal shall reflect the value of the security as collateral over the entire life of the mortgage and should not reflect expected future house price appreciation. The property appraisal may, but does not have to be outsourced to a third external real estate appraisal. If the valuation is an internal process it should be separated from the credit granting process and the credit decision.

In terms of the use of mortgage insurance the FSB is critical and clarifies that it does not substitute for sound underwriting practices by lenders. The FSB requires furthermore that all mortgage insurers are subject to appropriate prudential and regulatory oversight.

The FSB principles will have no direct influence on the European law but they may be used to politically argue for a tightening up of the mortgage lending standards on European and national level.

The principles are addressed to the worldwide regulators of the lending standards. Due to the consideration of the FSB guidelines on European level the proposed standards may influence the discussion on the regulation of mortgage credits on EU level.

For further questions, please do not hesitate to contact us.

Yours sincerely,



Andreas J. Zehnder
Managing Director
European Federation of Building Societies

Annex: - FSB Principles for Sound Residential Mortgage Underwriting Practices