How mortgage regulations are changing globally

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What is the most significant change we've seen in regulation in the past year?

UK: There are two key bodies that handle mortgage regulation in the UK. The first is the Financial Conduct Authority (FCA) and the second is the Prudential Regulation Authority (PRA). The FCA regulates all home-owner mortgages and lifetime mortgages such as equity release lending. Meanwhile, the PRA determines the amount of money that lenders, such as bank and building societies, need to hold, and the risk controls that they need to maintain. In October 2019, the FCA issued responsible lending rules and guidance covering borrowers who wanted to switch mortgage and were up to date with payments but did not wish to borrow any more money, by reducing barriers to such switches.

On 31 January 2020 the FCA announced a new mortgage advice and selling standards rules with immediate effect and a transition period running to 30 July 2020. These rules are intended to give consumers more choice in how they buy a mortgage and remove barriers created by earlier legislation. The rules centre around ensuring that consumers only pay for specific mortgage advice and ensuring that advisers must explain why they are not recommending cheaper mortgage options.

Germany: There were no significant changes in regulation regarding non-commercial mortgages.

US: The significant regulatory developments in the U.S. residential mortgage industry are:

- **Federal Developments**:
  - **Mortgage Underwriting**: The Consumer Finance Protection Bureau (CFPB) has indicated that the "GSE Patch" (a temporary category under which loans eligible for purchase or guarantee by Government Sponsored Enterprises) will be extended beyond its pending expiration in January 2021. It will permit federally backed lenders continued underwriting leeway in addressing the 43% debt-to-income underwriting standard and is expected to preserve over $250 billion in loan originations.
  - **Flood Insurance Reauthorization**: The National Flood Insurance Program has been extended until September 30, 2020. It preserves flood insurance for approximately 5 million insurance policies, 22,000 communities, and provides $1.3 trillion in coverage.
  - **CMBS Markets**: The Federal Housing Finance Agency (FHFA), Fannie Mae and Freddie Mac's regulator and conservator, has implemented its goal of creating a common mortgage-backed security (MBS) protocol via the "Single Security Initiative." It is being done via a common securitization platform (CSP) which will now underpin the operations of the $4.6 trillion MBS market.

- **COVID-19 Regulation:** The *COVID-19 Aid, Relief, and Economic Security Act* (CARES ACT) applies to federally backed mortgages, which account for approximately 70% of all residential mortgages in the U.S. For borrowers under financial distress due to COVID, the CARES ACT provides for forbearance (payment delays) on mortgages for up to 12 months. Late charges, extra fees and penalties are prohibited. Limited documentation is required to prove eligibility. Multifamily loans under HUD programs also have forbearance, but under shorter forbearance periods (up to 90 days). Loan servicers on federally backed mortgages are prohibited from starting foreclosures before May 18, 2020.

- **State COVID Response**
- Beyond federal limitations, state and local authorities in many U.S. states have issued COVID-19 focused temporary orders restricting remedies on residential mortgages. These vary state-by-state. Examples include:
- **California**'s suspension of residential foreclosures state-wide through May 31, 2020;
- **New York**'s 90-day moratorium on the enforcement of foreclosures and prohibitions "until further order" against filing foreclosure actions and other non-essential cases; and
- **Florida**'s suspension of residential mortgage foreclosures through May 18, 2020.

Mexico: There were no significant changes in regulation regarding non-commercial mortgages.

China: Since August 2019, China's central bank (PBOC) has changed the way commercial lenders set interest rates for loans. The mortgage rates will be based on Loan Prime Rate, or LPR, the new benchmark rate system, which will be linked to the PBOC's medium-term lending facility (MLF) interest rate.

New mortgage loan rates for first-home buyers shouldn't be lower than related LPRs. It has also been reported that the rate for second-home buyers must be at least 60 basis points higher than LPRs. Also, the loan prime rate is set on the 20th of every month, instead of daily.

Borrowers could negotiate with lenders on how to adjust their interests of mortgage loans each year based on changes of the LPR.

<u>What impact will COVID-19 have in shaping regulations in the future if any?</u>

UK: The FCA issued guidance on 20 March to mortgage lenders specifically dealing with COVID-19. This guidance is to be reviewed in the next 3 months. It is based and builds on two important principles binding mortgage lenders, namely, to treat the interests of its customers fairly, and to act honestly, fairly and professionally in accordance with the best interests of the customer.

The main principles of the guidance are that:

1. A borrower experiencing difficulties or who reasonably expects to do so, may ask for a payment holiday and if that request is made, a 3 months' payment holiday is to be offered, unless the mortgage lender can demonstrate that it is reasonable to do otherwise. More favourable arrangements can also be offered such as reducing or waiving interest.
2. A payment holiday should be offered to anyone that indicates that they are or may be in difficulty making their mortgage payments.
3. No fee or charges can be applied to any request.
4. Any request for or any payment holiday agreed must have no impact on the credit rating of any person concerned as this is due to circumstances entirely outside of their control.
5. No repossession should be commenced or continued at this time. This applies irrespective of the stage which any repossession proceedings have reached.

Germany: The impact of COVID-19 will most likely depend on how fast the country's economy will recover. If the recovery materializes at a slower than expected pace, it is fair to assume that stimuluses will be introduced to promote the recovery of the economy. Instruments that reduce interest rates and an easier access to lending might be one of those stimuluses. This can lead to higher prices for real estate which – in turn – can change the ratio of equity and debt in relation to the financing of the acquisition prices. Loans are likely to be backed by mortgages. In consequence, the level of indebtedness will increase, and the solvency of the debtors will decrease, thereby also decreasing the value a mortgage can provide to secure the lender.

Another possible instrument could be a regulation differentiating the access to lending by the level of the borrower's exposure to the COVID-19. For instance, a borrower who is more exposed to other individuals or is employed in an industry which largely depends on the contact of individuals (i.e. the hotel or catering industry) could possibly be treated differently from a borrower who has no such exposure.

Background for this differentiation would be that the more exposed borrower is more likely to be infected and therefore might be considered to present a higher risk to default on a debt. On the other hand, depending on the impact of COVID-19 on the economy, it is also a possibility that the government will guarantee to the lender to a certain extent that a mortgage-backed loan will be repaid. In this scenario, it is likely that the regulation on mortgages would be relaxed.

US: COVID-19 is disrupting every aspect of the U.S. economy and social life. It will continue to effect massive political, legal and social changes. Stop-gap regulatory responses will continue to attempt to "flatten the curve" of this disruption, but it is hard to see how the industry and the legal infrastructure can manage the fallout (it is still hobbled by lockdown in many places). With over 33 million people filing for unemployment and an unlikely V-shaped recovery, lenders will be facing a tsunami of distressed borrowers, mortgage defaults, impaired collateral, and deteriorating credit quality.

While the residential real estate market has been particularly hard hit, in recent weeks effective short-term solutions have been created for both homeowners and mortgage servicers. Depending on the length and severity of the economic impact created by COVID-19, it has yet to be seen if these temporary adaptations will result in longer-term changes for the residential mortgage market.

Lenders are likely to seek relief (and receive it) in adjusting underwriting standards and recalibrating debt-to-income and credit quality standards. It is also likely that banks may propose that the Federal Reserve and Treasury establish a credit facility for mortgage servicers, who are being hit hard by the relief provided to borrowers.

For borrowers, we expect continued stopgap measures to spread out payment regimes in the short-term. Despite major efforts to provide liquidity for the market via monetary policy and stimulus programs, borrowers are faced with a highly damaged economy, rent strikes and impaired income prospects. They will enhance bottlenecks in having loans underwritten, as lenders attempt to respond to an evolving regulatory and economic environment. However, federal, state and local temporary mortgage forbearance measures as well as moratoriums or restrictions on foreclosures and evictions, in particular, seem unlikely to continue for the long-term after the economic impact of the COVID-19 situation stabilizes.

Mexico: COVID-19 is more likely to have an impact on business practices and not so much on legislative matters, since the consequences and results of an event such as this one is already regulated. However, when drafting an agreement, the will of the parties mainly dictates the rules, and for this reason, the impact would be reflected in the clauses of the agreements when dealing with acts of God and force majeure events. For this reason, it is likely that moving forward, these types of clauses will play a greater role in all kind of agreements, including the insertion of rules and exceptions for the enforcement of a mortgage guarantee under a scenario like the one we are currently facing.

China: Since January 2020, the China Banking Regulatory Commission and other governmental agencies released a number of measures to outline the special circumstances being implemented as a result of COVID-19. Under these measures, generally, financial institutions should flexibly adjust personal repayment arrangements such as housing mortgages and reasonably postpone the repayment period. Also, financial institutions are encouraged to negotiate with borrowers and appropriately reduce the interest on individual housing loans for those who temporarily lose their sources of income due to the pandemic.

In practice, most banks should grant an extension for instalment repayments for borrowers = affected by COVID-19. For example, for those who have lost their income temporarily due to the pandemic, the Bank of China (BOC) can offer 3-6 months' delayed repayment arrangements dependent on individual circumstance. Another example of this is if confirmed or suspected cases or their spouses are overdue in making repayment during the pandemic period, the China Industry and Commerce Bank will not consider this a breach of contract or include them in the list of defaulting customers.

During the COVID-19 outbreak, banks and other financial institutions have been encouraged to actively use online technical means to handle banking services. In the event that borrowers could not apply for the extension of the banking agreement and sign the extension agreement through traditional face to face meetings, the banks could take the form through a non-contact approach, primarily through online financial services tools such as WeChat to solve the problem.

What regulations can we expect in the future?

UK: COVID-19 is likely to have a long-term impact on the economy and so it may well be that the guidance issued and referred to above will be extended beyond its initial three-month term. If the economy returns to normal, it is unlikely that COVID-19 will result in any specific new regulations in what is already a heavily regulated sector.

Other regulation that looks likely is facilitating the ability of borrowers to switch mortgage providers more easily. Research published in March 2019 shows that borrowers are reluctant to switch even if they could get far better deals elsewhere. The FCA is looking to intervene to help borrowers who do not switch and is issuing a consultation paper on potential remedies later in 2020, which may lead to new regulations.

The PRA is expected to introduce new mortgage reporting requirements for regulated home lenders and home finance administrators effective 1 October 2020.

Germany: We're likely to see legislation geared towards breaking the vicious circle of cheap money, high real estate prices, increase of indebtedness of the acquirer, decrease of acquirer's solvency, and decrease of the value of a mortgage for the lender; regulation might be introduced to limit the ratio of the acquisition price allowed to be financed by loans and backed up by mortgages.

US: If a new administration is elected, especially if the majority of the Senate shifts, significant "New Deal" restructuring can be expected.

On a more pragmatic level, the need to improve logistics surrounding closings has become quite evident as a result of state and local orders that have closed businesses, including title companies, and imposed social distancing requirements that often make in-person closings difficult or impractical. While virtual closings would seem to present an answer, current laws pertaining to electronic signatures, recordings, and notarizations make closings in an online world more difficult. The SECURE Notarization Act, proposed in March—permitting remote online notarization nationally—may, if passed, be a first step in the path to a digital transformation of the mortgage industry.

Mexico: There are a number of financial institutions which have been granted grace periods and subsequently restructured under certain conditions the repayment of loans, as otherwise a high volume of lenders would default, pushing lenders to foreclose a large sum of mortgage guarantees; a situation similar to what we saw during the 2008 financial crisis, which is not a desirable outcome for lenders or providers.

As a result, the Bank of Mexico and the Mexican Bank Association have issued policies to considerably reduce the inter-bank interest rate as well as to negotiate its payments terms for four months in order to support the real estate market, which has been paralyzed to date as a result of COVID-19.

However, these conditions have developed through the will of the parties concerned and not through a binding decree or regulation. Therefore, in order to protect the interests of the parties involved, we could see future regulations of a public nature that bind financial institutions to behave similarly in the treatment of delinquency interest and in the terms of loan payments.

China: There is currently a high level of financial pressure and an increased risk of defaults. As a result of this, debt restructuring volumes will increase. It is also likely that the interest rate will be reduced for a prolonged period. Other measures such as debt relief and tax cuts may also be adopted to promote business activities.

Online technology and big data related technology will also be encouraged to use to make lending process more quickly and efficient.