Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

FAQ - Outcome of the Review of Mortgage Measures

23 November 2016

1. Why were the mortgage measures introduced?

The mortgage measures were introduced in February 2015 to enhance the resilience of both borrowers and the banking sector, and to reduce the risk of bank credit and house price spirals from developing in the future.

The Central Bank does not wish to regulate or directly control housing prices.

Housing market policy issues like taxes, building measures and the shortage of supply of housing for buyers and renters are outside of our remit. Financial sector regulations cannot address these issues, which must instead by addressed by other targeted policies.

While the measures set requirements for lenders, they do not replace responsible lending standards and the application of suitability requirements by lenders. Lenders must continue to be satisfied that mortgages are affordable for borrowers for the duration of the life of a loan.

While it is accepted there have been consequences, we believe these measures ultimately help to protect borrowers from potential future crises. Had similar measures been in place during the boom period, the impact of the financial crisis on households and on financial stability would have been reduced.

2. What is the outcome of the review?

Following an extensive consultation and evaluation process, the review affirms that the overall framework is appropriate and the measures are contributing to financial and economic stability, reducing the risk of unsustainable lending and borrowing.

Following the review, the framework is broadly unchanged. The 3.5 times ceiling on the loan to income (LTI) ratio remains. Requirements for buy to let borrowers and the exemptions for negative equity mortgage borrowers from the measures also remain unchanged.

The review identified a number of refinements to improve the sustainability and effectiveness of the current framework.

The refinements from 1 January 2017 are:

- The ceiling on the loan to value (LTV) ratio for all first-time buyers will be set at 90 percent. This is a shift from the current requirements, which puts the ceiling at 90 percent for loans up to €220,000 but at 80 percent for the balance of loans above €220,000. This means that first-time buyers can borrow up to 90 percent of a value of a home, with a requirement for a 10 percent minimum deposit.
- The 20 percent minimum deposit requirement (i.e. maximum LTV ratio of 80 percent) continues to apply to second and subsequent buyers.
- The structure of the proportionate LTV allowances is amended. Five percent of the value of new lending to first-time buyers will be allowed above the 90 percent LTV limit and 20 percent of the value of new lending to second and subsequent buyers for primary residences will be allowed above the 80 percent loan to value limit. This replaces the current regulation which allows 15 percent of total lending for primary dwellings (the sum of lending to first-time buyers and second and subsequent buyers) above the LTV limits.
- The current two-month valuation period will be extended to four months in recognition of the fact that a portion of house sales can take longer than the average three months to conclude.
- There is a technical amendment to the scope of the non-primary dwelling home limit so that large commercial landlords and developers are not in-scope of the Regulations. This is being implemented by applying the Regulations to consumers based on the definition in the Consumer Protection Code 2012 and that used by the Financial Services Ombudsman to define the scope of its jurisdiction.

3. When will the changes come into effect?

These changes will come into effect from 1 January 2017.

4. What are the changes that apply to first-time buyers?

Under the current measures a first-time buyer (FTB) is required to have a minimum deposit that was linked to the value of the loan – for example: 10 percent of the value up to €220,000 and 20 percent of anything above that.

Following the review, if you are a first-time buyer, you will now be required to have a minimum deposit of 10 percent of the value of the property, so you can get a mortgage worth up to a maximum of 90 percent of the value of the property.

If the property is worth €350,000, the first-time buyer will be required to have a minimum deposit of 10 percent or a €35,000 deposit. It should be noted that the minimum deposit requirements are just limits and not a target. For many borrowers, a higher deposit requirement may be more appropriate, according to individual circumstances and a lender's credit risk assessment processes.

The measures relating to loan to income ratio, of 3.5 times your household's gross income, remain the same, as will the 70 per cent LTV limit for buy to let properties.

5. What changes have been made to the proportionate allowances?

The value of allowances above the LTI limit remains unchanged. Lenders will continue to be permitted to make exemptions for up to 20 percent of the value of total new lending for primary dwelling homes above the LTI limit

The allowance for exemptions to the LTV Requirements has been refined, differentiating between first-time buyers and second and subsequent buyers.

For first-time buyers, lenders will be allowed to lend up to 5 percent of the value of new lending in this category (i.e. to first-time buyers) in excess of 90 percent on an annual basis. This modest allocation caters for specific cases that might be assessed as a reasonable credit risk by a lender.

For second and subsequent buyers, lenders will be allowed to lend up to 20 percent of the value of new lending to these borrowers in excess of 80 percent on an annual basis.

In the long-term splitting the two groups, which have different characteristics, will give the Central Bank flexibility to adjust these specific limits if threats to financial stability emerge.

6. Why is there a different approach being adopted for first-time buyers and other borrowers?

The approach taken when the measures were introduced was to have different limits for first-time borrowers and for other borrowers. This approach was taken to address the concerns raised at the time regarding fairness, access to mortgage finance and homeownership for first-time buyers and was informed by empirical research, for example, the finding that first time buyers (FTBs) have a lower risk of default than second and subsequent buyers (SSBs).

The review of the measures has found that a higher LTV 90 per cent remains appropriate for FTBs due to continued empirical evidence showing lower default among FTBs relative to SSBs.

However, further investigation of the different default risk of FTBs and SSBs shows that, using the most recent data, the difference in default rate between FTBs and SSBs is now no lower for buyers who purchased cheaper valued houses. To improve the sustainability and effectiveness of the current framework, the €220,000 value threshold has been removed for first-time buyers which means that first time buyers require a 10 per cent deposit when buying a home.

7. What is the definition of a first-time buyer?

A first-time buyer is defined as a borrower to whom no housing loan has ever before been advanced. Where the borrower under a housing loan is more than one person and one or more of those persons has previously been advanced a housing loan, none of those persons is a first-time buyer.

The requirement for all borrowers of a particular loan to be FTBs is aligned with the definition of FTB from the the Office of the Revenue Commissioners.

8. How will the proportionate allowances be assigned?

This will be a matter for individual lenders, based on an evaluation of each specific borrower and the lender's own credit policies. The limits are supplementary to individual banks' credit policies and are not designed as a substitute for lenders' responsibilities to assess affordability and lend prudently.

We expect lenders to continue to define and implement rigorous and prudent standards to their own internal credit assessments policies and procedures, making all lending decisions on a case by case basis as required by the Consumer Protection Code and other regulations.

9. Is there any flexibility in the proportionate allowances?

The proportionate allowances have been a feature of the measures since their introduction. The proportionate allowances mean that lenders will be able to make decisions based on an individual borrower's circumstances.

Lenders will still be required to assess an individual borrower's affordability and lend prudently on a case by case basis, in line with the requirements of the Consumer Protection Code and other regulations.

There have been some changes to the proportionate allowances for the LTV measures.

For second and subsequent buyers (SSBs), the review found that it is still appropriate to allow for a certain amount of new lending above the SSB LTV limit. Under the amendments to the framework, 20 per cent of the value of new lending to SSBs will be allowed above the 80 per cent LTV limit. This is broadly in line with the current new lending for SSBs above the LTV limits since the introduction of the measures.

For first-time buyers (FTBs), the amendment to the threshold means that FTBs now face a 90 per cent maximum LTV ratio. Lending above 90 per cent LTV should take place only in exceptional circumstances. In recognition that some limited flexibility for higher LTV lending may be warranted, 5 per cent of the value of new lending to FTBs will be allowed above the limit.

While the measures set requirements for lenders, they do not replace responsible lending standards and suitability requirements. Lenders must continue to be satisfied that any mortgage will be affordable for borrowers over the lifetime of a loan in line with the requirements of the Consumer Protection Code.

10. Am I guaranteed a mortgage up to the new levels when I apply?

No. Lenders are still required to assess each loan application on a case by case basis. Ultimately the amount of any loan offered is a matter for individual lenders, but only a proportionate level of mortgages will be allowed to exceed the LTV and LTI limits.

The limits are supplementary to individual banks' credit policies and are not designed as a substitute for lenders' responsibilities to assess affordability and lend prudently.

We expect lenders to continue to define and implement rigorous and prudent standards to their own internal credit assessment policies and procedures, making all lending decisions on a case by case basis as required by the Consumer Protection Code and other regulations.

11. Who do the mortgage measures apply to?

The mortgage measures continue to apply to mortgages secured on residential property in the State. Equity release and top-ups on existing mortgages will continue to be covered by the measures.

Mortgages out of scope of the measures remain as follows:

- The LTV and LTI limits do not apply to refinancing of a housing loan (i.e. switcher mortgages) or housing loans entered into in order to address arrears or pre arrears.
- Housing loans for borrowers in negative equity who are selling their home and wish to obtain a mortgage for a new property are not in scope of the LTV limits although the usual lending standards of the individual banks applies to these borrowers. Where the borrower under a housing loan is more than one person and one or more of those

persons is a borrower under a *negative equity loan*, all of those persons are borrowers under a negative equity loan. These loans are in scope of the LTI limit.

- The LTI limits do not apply to housing loans for non-PDH purposes (i.e. buy–to-let).

There is a technical amendment to the scope of the non-primary dwelling home limit so that large commercial landlords and developers are not in scope of the regulations. This is being implemented by applying the regulations to housing loans advanced to consumers only. The definition of consumer to be used in the regulations is based on the definition in the Consumer Protection Code 2012 and that used by the Financial Services Ombudsman to define the scope of its jurisdiction, and will include persons acting outside the course of their business, trade or profession, in addition to persons (including sole traders, companies, partnerships and other unincorporated bodies of persons) with an annual turnover of €3 million or less in the preceding financial year, taking into account the combined turnover of any group of persons of which they are a member.

12. The Central Bank made clear its position was not to change the measures – why were the changes made?

The Central Bank has always committed to reviewing the measures on a regular basis and on the introduction of the measures noted that it may, in future, consider it necessary to adjust any or all of the parameters of the proportionate LTV and LTI ratios in response to economic, market, or other developments. The first review examines the early performance of the measures against the stated objectives and the potential side effects of the measures. This is to ensure that the measures are correctly calibrated to prevent the build-up of risk in the financial system related to the property market.

The review affirms that the overall framework is appropriate and the measures are contributing to financial and economic stability, reducing the risk of unsustainable lending and borrowing.

Following the review, the framework is broadly unchanged. The 3.5 times ceiling on the loan to income (LTI) ratio remains. The LTV requirements for buy to let borrowers and the exemptions for switcher mortgages, mortgages under the Mortgage Arrears Resolution Process and negative equity mortgage borrowers also remain unchanged.

The review identified a number of refinements to improve the sustainability and effectiveness of the current framework.

13. What evidence was provided to support these changes?

The review was informed by data gathering and analysis by the Central Bank and by the submissions from external parties following the public call for evidence. The analytical framework will guide further reviews and will be enhanced as new data and methodologies become available.

We have published research throughout the review process and a further seven research papers have been published today (23 November). We have also published an extensive report on the outcome of the review process itself along with a feedback statement on the submissions received from the call for submissions.

14. Are these changes an acknowledgement that the measures were flawed in the first place?

No. The review has affirmed that the overall framework is appropriate and the measures are contributing to financial and economic stability and reducing the risk of unsustainable lending and borrowing. Following the review, the framework is broadly unchanged.

The measures will remain a permanent feature of the environment to help reduce the probability of boom-bust cycles and over-indebtedness.

15. Why are you not changing the 'buy to let' LTV limit?

The Central Bank is satisfied that the 70 per cent LTV limit for BTLs does not require changes as the current limit is still considered appropriate for the risks associated with this market.

16. Why were no allowances introduced for those renting properties?

The Central Bank considered a range of suggestions during its review including submissions on the effect of the measures on the rental market. Our analysis, published in the economic letter series, shows that rents have been rising nationally since before the introduction of the mortgage measures. A number of factors have been contributing to pressures in the rental market, including shortage of supply, changing expectations, low rates of housing sales and the improving economy.

Allowance for those renting properties, particularly those paying high rents in Dublin and other cities, featured as part of a number of submissions. The Central Bank's response to these submissions can be found in the Feedback Statement.

The refinements introduced should address concerns that the measures were contributing to pressures in the rental market due to the fact that FTBs in some cases needed to save for longer to buy a property. The new 90 per cent LTV limit for FTBs will result in broadly similar deposit requirements for FTBs compared to immediately prior to introduction of the measures, when many banks commonly required 90 per cent LTVs.

The removal of the property value threshold will also remove any geographic differences in LTV limits, and FTBs in cities and other regions with higher house prices will face the same LTV requirements as those in the rest of the country.

17. What impact have the measures had over the past 18 months?

Over the past 18 months, the measures have contributed to making sure that those who have purchased properties in that time are better prepared to manage their mortgage payments in the event of a future downturn in the economy.

The objective of the measures to increase bank and borrower resilience is a medium-term one and it is too early to assess empirically whether the measures have been effective in meeting this objective across the entire mortgage portfolio. The true test of the resilience of banks and borrowers will come only if the economy and property market experience another crisis.

Householders will be better protected as they will have a deposit in place that will limit the exposure to negative equity. Banks will be better protected as there is a buffer between the loan and the value of the home. Had similar measures been in place during the boom period, the impact of the financial crisis on households and on financial stability would have been reduced.

As part of this review, a number of different approaches have been taken to assess whether new lending issued under the measures is more resilient to shocks than lending that was carried out previously. This analysis points to improved resilience following the introduction of the measures.

18. Are you satisfied that the Central Bank took on board the views of the 51 stakeholders who made submissions in relation to this?

Yes. The Central Bank staff working on the review undertook an extensive review of all the evidence submitted by individuals and organisations. We are grateful to those who took the time to make these submissions. The Central Bank's response to these submissions can be found in the Feedback Statement.

19. How many responses did the Central Bank get to the call for submissions?

The Central Bank received 51 submissions. All submissions can be found here, along with a feedback statement.