Initial assessment: The effectiveness of measures for protection of mortgagors

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Vol. 3, N.º 1 (January 2014)

The persistence of the financial and economic crisis has brought with it, among other things, the weakening of an ever increasing proportion of household economies. In many cases, this has translated into households' loss of their primary residence. In response, over the past two years, the government has enacted a series of measures aimed at alleviating the pressures faced by mortgagors.

This article provides an initial assessment of the actual effectiveness of the measures to protect mortgagors, approved by the government since 2012, based on the results recently published by the Ministry of Economy and Competitiveness. Although not too much time has passed and public information available, in some cases, is limited, at present, we have not observed much recourse to the measures. Perhaps this can be explained by the somewhat strict requirements in place for the measures to apply. Nevertheless, the relaxation of these criteria would have a negative impact on banks´ balance sheets.

Introduction

According to the EPA labor force survey from the third quarter of 2013 –the latest available at the time this article was written– all active members are unemployed in 10.4% of households and 3.7% of households receive no income at all. As a result, households´ capacity to pay off previously contracted debts is constrained (according to the Bank of Spain, the mortgage loan NPL rate, for example, stood at 5.1% in the third quarter of 2013) and, in some cases, this results in the loss of their primary residence.

For the past two years, the government has been enacting a series of measures aimed at alleviating such dramatic situations. The Code of Good Practices (henceforth, in its Spanish acronym CBP), signed by a majority of credit institutions, the moratorium on evictions for two years for particularly vulnerable households (both economically and socially), and the creation of a Social Housing Fund (henceforth, in its Spanish acronym FSV) for households that have lost their residence in mortgage foreclosure processes are some of the most significant recent measures.

The main objective of this article is to provide a brief overview of the latest measures for mortgagor protection, and an initial assessment of their effectiveness, in light of the results recently

[1] A.F.I. - Analistas Financieros Internacionales, S.A.

published by the Ministry of Economy and Competitiveness.[2]

The Code of Good Practices: Debt restructuring and dation in payment

The Code of Good Practices was approved as part of the Royal Decree-Law 6/2012 of March 9th, for urgent measures to protect mortgagors without funds, and it has been signed by virtually every credit institution operating in Spain that has granted mortgages.

In summary, the protective mechanism it establishes and for which a specific group of mortgagors is eligible[3] consists of three types of solutions, the application of which is individual with the requirement that the non-viability of the immediately preceding measure be demonstrated:

- **Restructuring of mortgage debt** to ensure repayment of the loan. The measures include the following:
  - A five-year grace period for repayment of capital.[4]
  - An extension of the repayment period to up to 40 years following the granting of the loan. It should be noted that, according to the Official Association of Mercantile and Property Registrars, the average term for new mortgage loans is half this duration, or about 20 years.
  - Reduction of the interest rate applicable to the 12-year Euribor + 0.25% during the grace period, when the current average margin of new mortgage loans far exceeds 3%, according to the Bank of Spain.
- **A haircut of up to 25% of the mortgage loan still outstanding**, provided the restructuring plan is not viable: that is, the monthly mortgage payment basis exceeds 50% of the aggregate income of the debtor's household unit.[5]
- **Dation in payment** of the primary residence used to secure the mortgage loan, thus resulting in a write-off of the outstanding debt. Even if no longer the owner of the residence, the debtor may stay on in the residence, paying an annual rent equal to 3% of the total amount of the debt at the time of dation.

According to the first results of the CBP, which cover the period between April 2012 and September 2013, 1,684 debt restructurings were undertaken for mortgaged households that met the pre-established requirements. Although this is a considerable volume in absolute terms, it is not quite as much in relative terms (see Table 1).

Table 1

Estimate of impact of debt restructuring under CBP

Restructurings of mortage debt	1,684
% mortgages for acquisition of residence	0.03%
% mortgage novations	0.47%
Absolute figures:	
No. mortgages for acquisition of residence (31/12/2012)	6,140,645
No. of mortgage novations (Apr12-Sep13)	358,835

Sources: Bank of Spain, Ministry of Economy and Competitiveness, INE and AFI.

[2] For further information, see the following link: http://www.mineco.gob.es/portal/site/mineco/menuitem.ac30f9268750bd56a0b0240e026041a0/?vgnextoid=bc73a4cf7f892410VgnVCM1000001d04140aRCRD&vgnextchannel=864e154527515310VgnVCM1000001d04140aRCRD

[3] For further details, see publication in the Official State Gazette: http://www.boe.es/boe/dias/2012/03/10/pdfs/BOE-A-2012-3394.pdf

[4] Amended by Law 10/2013, of May 14th, of measures to strengthen mortgagor protection, debt restructuring and social rents, available at the following link: http://www.boe.es/boe/dias/2013/05/15/pdfs/BOE-A-2013-5073.pdf

[5] Amended by Law 10/2013.

Hence, if one takes note of the fact that behind each of these operations lies a mortgage, and further notes that there are now some 6 million outstanding mortgage loans in Spain, barely 0.03% of the total have benefited from the measure. If we compare it to the volume of mortgage novations arranged in the same period of time, that is, to the total mortgage loans whose financial conditions have been changed, then these would represent only about 0.5% of the total. This small percentage reveals that the measure was already being used by credit institutions to minimize mortgagors' risk of default and, accordingly, prevent an increase of the NPL rate in this business segment.

Only 0.5% of mortgage novations took place under the new framework approved by the government for the protection of mortgagors without resources. This small percentage reveals that the measure was already being used by credit institutions to minimize mortgagors' risk of default and, accordingly, prevent an increase of the NPL rate in this business segment.

The impact of the haircuts, for their part, is much more modest. According to figures published by the Ministry of Economy and Competitiveness, barely 6 such operations have been approved since this additional measure for the protection of mortgagors came into force.

Lastly, 611 dations in payment have been carried out under the CBP (see Table 2), which represents, according to Bank of Spain data, approximately 4% of the dations in payment of primary residences recorded in all of 2012 (the total number for the first three quarters of the year 2013 is unknown). Although this measure was not ultimately approved with a universal and retroactive character,[6] as a result of its inclusion in the reform of the Mortgage Law (Romero, 2013), the number of dations in payment approved under the CBP would represent barely 0.09% of the number of households that are underwater (that is, the value of their mortgage debt exceeds the value of the asset that is used to secure the mortgage): in other words, of the total potential group eligible for the measure in strictly economic or financial terms, if this option had been available to all types of debtor.

Table 2

Estimate of impact of dation of payment under CBP

Dation in payment of mortgage debt	611
total % of dations in payment of primary residence	4.33%
% underwater mortgages	0.09%
Absolute figures:	
Total dations in payment of primary residence (2012)	14,110
No. of underwater mortgages (3Q13)	672,000

Sources: Ministry of Economy and Competitiveness, INE, the Official Association of Mercantile and Property Registrars and AFI.

Two-year moratorium on evictions

One of the protective measures receiving the most attention in the media was the two-year moratorium on evictions for mortgagors in an especially vulnerable economic and social position. Approved in a Royal Decree-Law 27/2012, of November 15th, of urgent measures to strengthen mortgagors protection,[7] the government gave the measure continuity in Law 10/2013, of May 14th,

[6] Lastly the possibility was considered of applying haircuts to outstanding debt resulting from a mortgage foreclosure of between 20 and 35%, provided there is a repayment commitment in the following 8 and 5 years, respectively. For further information, see Law 10/2013.

[7] For further information, see the following link: http://www.boe.es/boe/dias/2012/11/16/pdfs/BOE-A-2012-14115.pdf

of measures to reinforce mortgagor protection, debt restructuring and social rents.

Taking into account solely the economic and financial requirements to be met by mortgagors who wish to benefit from the measure (the unavailability of statistics on the social requirements makes an estimate impossible), some 157,000 households could have benefited from a moratorium on evictions, which represents 0.96% of all households in Spain (Romero, 2013).

Table 3

Estimate of impact of 2-year moratorium on evictions

2-year moratorium on evictions	1,500
% potential beneficary households	0.96%
% total evictions from homes	3.17%
Absolute figures:	
Potential beneficiary households	157,000
Total evictions from homes (Jan13-Sep13)	47,340

Sources: Bank of Spain, Ministry of Economy and Competitiveness, the General Council of the Judiciary, INE and AFI.

According to data recently published by the Ministry of Economy and Competitiveness, 1,500 evictions have been stopped (see Table 3), which represents nearly 1% of potential beneficiary households (this percentage would likely be lower if the social requirements had been included in the estimate of the ratio´s denominator). If set against the total number of evictions registered from the coming into force of the measure until the end of the third quarter of 2013, the figure would represent barely above 3%. It is true, nonetheless, that the actual proportion may be somewhat larger, since the statistics published by the General Council of the Judiciary refer to all types of residences and not only primary ones, and to all forms of possession, not only ownership.

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Social Housing Fund

The Social Housing Fund represents another of the more significant measures aimed at protecting mortgagors that have been implemented in recent years. Enacted by the government, it consists of a stock of 6,000 residences held by credit institutions that have been offered for rent to all families that have been evicted and are in a situation of necessity or at risk of social exclusion. To enable access to housing on the part of this segment of the Spanish population, the rent for these residences ranges between 150 and 400 euros a month.

According to data published by the Ministry of Economy and Competitiveness, only 615 residences have been occupied (see Table 4),

Table 4

Estimate impact of FSV

FSV residences occupied	615
% capacity of FSV	10.25%
% deliveries of primary residences	
according to Bank of Spain	1.89%
according to Official Association of Mercantile and Property Registrars	2.05%
Absolute figures:	
No. of FSV residences	6,000
No. of deliveries of primary residences (2012)	
according to Bank of Spain	32,490
according to Official Association of Mercantile and Property Registrars	30,035

Sources: Bank of Spain, Ministry of Economy and Competitiveness and AFI.

that is, barely above 10% of the residences in the FSV. However, according to figures published by the Bank of Spain and the Official Association of Mercantile and Property Registrars, approximately 30,000 Spanish households lost their primary residence in 2012. That is, about 2% of evicted households were covered by this measure.

Conclusion

The results recently published by the Ministry of Economy and Competitiveness of some of the measures for the protection of mortgagors, such as the CBP, the moratorium on evictions or the creation of the FSV, allow for making an initial assessment of the situation. Under the CBP, only 0.03% of mortgaged households have benefited from a restructuring of their debt and barely 0.1% of those who could have applied for dation in payment, if it had been universal, have been allowed to benefit from this measure. Eviction has been suspended for two years for only 1% of potential beneficiary households, while only 2% of the households that have already lost their homes in a mortgage foreclosure have been able to occupy a residence provided by the FSV.

On their own, these percentages reveal the small extent of the impact of the measures to protect mortgagors since their coming into force through the third quarter of 2013, and how restrictive some of the eligibility requirements are. However, although an expansion of the exclusion threshold that defines the potential group of beneficiaries would broaden the social impact of the protective measures, it could also lead to other negative consequences for banks´ balance sheets (above all, with regard to the CBP) and, generally for the economic and financial stability of the country as a whole.

References

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