How the Global Financial Crisis is Affecting EU mortgage Laws

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I. MORTGAGE LAWS BETWEEN LOCAL DIMENSION AND GLOBAL ASPIRATIONS

As a fundamental part of property law, mortgage law has been usually dealt with according to the mainly local approach that has largely characterised property law studies. For a long time, the legal diversities between national laws delayed the development of all-encompassing analyses of the mortgage laws, also extending to their trans-national dimension and/or to the feasibility of legal integration in this field.

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At the end of the 1970’s, the United Nations Commission for International Trade Law (UNICTRAL) assigned to Prof. U. Drobnig (Max Planck Institut für ausländisches und internationales Recht, Hamburg) the compilation of a study on the need and feasibility of the legal harmonization of the law of security rights in the European Community. As it is well-known, the study resulted in a negative statement on the issue of the feasibility of any legal integration activity in this area, due to the extreme high level of differences existing in the reviewed legal systems: «Report of the Secretary-General: International Payments. Study on Security Interests» (1977) 8, U.N. Comm’n on Int’l Trade L.Y.B., pp. 171-221,
Yet, exactly as it is for property law, security over immovables devices are
the outcome of a legal historical process aimed at resolving economic problems
that were shared by the diverse legal experiences at a certain stage of their de-
velopment. Thus, also this area of the law possesses an intrinsic trans-national
dimension that goes beyond the short perimeter of local technicalities. Indeed,
even among these domestic technicalities, it is possible to detect a certain ‘com-
mon core’. To give but one example from the historical perspective, it should
suffice to recall that in ancient legal experiences the common form of security
was the grant to the creditor of the seisin 3 over specific things; from this start-
ing point, the economic development of the societies has been associated with
the emergence of non-possessory security, and with the shaping of devices that
could leave the debtor/grantor of the security with the formal entitlement to the
object of security 4.

Today, it is the increasing interrelation of the (not only) western economies,
together with the interconnection of the world’s financial markets, that clearly
results in new incentives for the shaping of common technical solutions, starting
with the background of different national legal traditions. To be sure, societies
that share economic needs aspire to create similar legal rules. This is the major
challenge worldwide, that the law of security rights is facing these days.

This challenge has been made more demanding by the financial crisis that
started in 2007 from the sub-prime emergency in the USA, soon expanded to
Europe and the rest of the world, and still has yet to be overcome.

This paper tries to assess the impact the current economic and financial
context has on European mortgage laws. The assumption underlying the fol-
lowing pages is that —especially after the global crisis— European mortgage
laws are forced, by the needs of the international finance, toward uniformity

U.N.Doc.A/CN.9/SER.A - it is the most quoted study in the international literature on secured transac-
tions. See also U. Drobnig, Empfehlen sich gesetzlichen Maßnahmen zur Reform der Mobiliarsicher-

3 To mean property, possession or every form of apprehension and control of things Germanic
peoples used the all-inclusive expression of: Gewere, in the territories of today’s Germany (scientific
studies on the Gewere were started by the Germanists’ scholarship in the xix century: K. F. Eichhorn,
Einleitung in das deutsche Privatrecht mit Einschluss des Lehrechts, Göttingen, 1823, p. 395 ff.; W. E.
Albrecht, Die Gewere als Grundlage des älteren deutschen Sachenrechts, Königsberg, 1828, 2. Aufl.,
1967; A. Heusler, Die Gewere, Weimar, 1872, 2. Aufl., 1968, p. 50; E. Huber, Die Bedeutung der Ge-
were im deutschen Sachenrecht, Bern, 1894; H. Brunner, Grundzüge der deutschen Rechtsgeschichte,
Die Gewere-Theorien, Münster, 1910; H. Mittels y H. Lieberich, Deutsches Privatrecht, 9. Aufl., Mün-
chen, 1981, p. 89 ff.); saisine, in the current territories of France (F. J. Longrais, La conception anglais-
aise de la Saisine du xvi au xiv siècle, Recueil Sirey, Paris, 1925, p. 19 ff.; Alb. Canadian, Propriété,
in Alb. Canadian, A. Gambino and B. Pozzo, Property-Propriété-Eigentum, Padua, 1992, p. 195 ff.) and
seisin beyond the Channel (J. H. Baker, An Introduction to English Legal History, 4th ed., London, 2002,
p. 226; S. E. Thorne, Livery of Seisin, in S. E. Thorne, Essays in English Legal History, London, 1985,
p. 31 ff.); in today’s Norway’s domains the term was skeyting, and skötning in the areas of North-Eastern

4 See F. Fiorentini, Le garanzie immobiliari in Europa. Studio di diritto comparato, Bern/Naples,
for Italy. See also R. W. Turner, The Equity of Redemption, Its Nature, History and Connection with Eq-
reali dell’obbligazione, Milano, 1935, cap. I; S. A. Riesenfeld, «Security Interests in Land in Modern
of operative solutions (if not directly of legal rules). Thus, legal integration in this area of the law is experiencing a new momentum. This momentum takes the advantage of the contractual side of the mortgage relationship and addresses (mortgage) loan contracts, because legal harmonisation of contract law is easier to reach—particularly at the EU level—than that of property law. However, important proprietary aspects of the mortgage, such as the rules on the enforcement of the security, still remain unaddressed by legal integration efforts.

In order to carry out the assessment addressed above, this paper will first outline the broad contours of the state of the art of European mortgage laws by summarising the main differences (no. 2) and the main similarities (no. 3) that exist in the European landscape. Then, the way in which EU law is impacting the national mortgage laws (nos. 4 and 5) and the driving forces behind the EU actions will be dealt with (no. 5).

II. COMPARING MORTGAGE LAWS IN EUROPE: DIFFERENT NATIONAL APPROACHES

In order to give a general illustration of the diversity within policy choices and technicalities existing between the mortgage laws in Europe, I will now briefly refer to the outcome of a research that I have presented elsewhere, reviewing German, English and Italian laws’ approaches to the problem of land credit and security. Even though these systems certainly do not reflect the entirety of the European scenario, they can represent at least some of the most relevant diversities of approaches that may coexist in the EU, crossing the cultural divide between common law and civil law.

To be sure, the crucial issue that each legal system faces when dealing with mortgage credit is that of identifying and implementing control instruments capable of ensuring a proper balance between the conflicting interests at stake. In other words, the law is required to impede creditors from abusing their dominant position leading to the detriment of debtors and, at the same time, to grant creditors the best possible protection. Thus, in every legal system the policy challenge is to balance rigidity and flexibility overseeing secured transactions. To no surprise, the legal systems respond to these needs by developing different solutions that can be fully understood only in view of different legal traditions of whose current rules they are the offshoot.

a) German law has shown a tendency that can be defined as liberal. This means that it has been able to implement the idea that mortgage credit is a fundamental element to promoting a country’s economic development and strengthening its competitiveness, even beyond its national borders. The code has incorporated the needs of market operators pushing towards the mobility of the value of land, but also of those who fear the risks deriving to debtors from an excessive facility of the circulation of security rights.

The codification of 1900 (BGB) in fact regulates both security rights that are structurally accessory to a secured obligation (Hypothek) —deriving from the tradition of Roman law spread throughout the southern territories of the Reich— and a security right that is structurally not accessory (Grundschuld). The latter, which can also be created in favour of the property owner (Eigentümergrundschuld), represents the answer to the request for mobility of the value of immovables that developed in Northern Germany.

In the first case, the accessority of the security right is the primary instrument of control on the proportionality between the market value of the security and that of the secured obligation. In the second case, the structural absence of accessority with regard to the original obligation promotes the circulation of the security right, and enhances its economic market value by making the interest of protecting the debtor yield to the needs of creditors.

During the course of the twentieth century, however, the Rechtspraxis deviated from both the abovementioned models. The German practice developed and highly rewarded the recourse to a third option, the so-called Sicherungsgrundschuld. This is an original device that departs from the codified patterns, grounded as it is on a security agreement (Sicherungsabrede). This is a contract by which it is up to the parties to regulate themselves the terms and conditions under which the creditor may enforce the security right. The Sicherungsgrundschuld has been validated by German case-law, which has been able to control the flexible connection, established by the parties, between security right and secured obligation through the rules of the law of obligations.

German law shows how differently the accessority of the security right can be viewed from the dogmatic necessity dictated by the structure of property rights —as it is the rule in the Franco-Italian tradition—. This has also been made possible because, in Germany, it is the judge and not the Code that is the custodian and regent of the legal regime of the Sicherungsgrundschuld. It is a regime that, as noted, relies on the flexible law of obligations for the governance of problems that arise in practice, not on the more rigid rules of property law. Specifically, it is the general clause of the Sittenwidrigkeit (§ 138 I BGB), corroborated by the principle of Treu und Glaube set forth in § 242 BGB, that acts as an elastic control criterion of the proportionality between secured obligation(s) and security right.

In Germany, the interpretative formants supported and regulated the preferences of practice, thereby promoting a flexible control over secured transactions, which has been carried out by exploiting the potential interrelation between the law of property and the law of obligations.

b) English law reveals a pragmatic approach to mortgage credit. The system has certainly given space to the policy option that wishes to enhance mortgage credit as an indispensable incentive for economic development. However, this has occurred only through the filter of professional technocrats who have always monopolized the development of property law.

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6 F. Fiorentini, Le garanzie immobiliari in Europa, 105-121.
In comparison to the German model, English law of mortgage offers an example of the disadvantages that can derive from regulating multiple forms of security, when such plurality is not fitting substantially different interests. Notwithstanding the reform of the Law of Property Act of 1925, which aimed at simplifying the legal scenario, the rules originating from this ‘codification’ provide for a multitude of security rights over immovables (mortgage, charge, charge by way of legal mortgage). These rights are diversified not only in the ways in which they are created, but also, within certain limits, vary in ways in which they become effective against third parties. By contrast, the powers granted to the parties, as well as the control techniques of the secured relationship, are the same in each of these devices. Thus, it is difficult to comprehend the usefulness of the forms of security rights over land that English law has preserved, and which result in complications and irrationality, charging greater costs upon their users.

The high degree of complexity and apparent incoherence of the English law of mortgage must be understood in light of the historical context that determined the origin of the entire law of property. In particular, the English law of mortgage depends on the intimate relationship between the current rules and the feudal past and can only be valued in the light of the substantive distinction between «law» and «equity». At present —as in the past— proprietary equity rules are the driving forces of the regulation of secured relationships in the field of immovable assets 7. In England, through the particular flexibility granted by equity rules, it has always been property law that performs the control function, which in Germany judges draw from the use of the law of obligations 8.

While the role of case law as a leading formant in the English law of mortgage is unquestionable, it should be stressed that the role played by the professionals involved with immovable assets transactions —the conveyancers, is equally incisive—. During the transition from the Middle Ages to the modern times and during the course of the twentieth century, they have maintained a de facto control over the law of mortgage. The interests of this professional class have been so pervasive that it is possible to deem them responsible, not only for the initial development of rather effective rules for the protection of creditors, such as those related to the extrajudicial sale of encumbered immovable assets, but also for the significant delay —between the xix and the xx century— in the rationalization of this field of law. This is the reason for the modernization «in spurts» of the English law of mortgage —also as far as title registration is concerned— 9.

An overall assessment of the English law of mortgage cannot omit to point out the evident contradictions on which it is still dependant. On the one hand, it

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7 For the rules of equity that have the strongest impact on practice and the development of English law in this sector, see F. Fiorentini, Le garanzie immobiliari in Europa, 292-306.
8 F. Fiorentini, Le garanzie immobiliari in Europa, 204-222.
appears to be a system whose modernization is required more than ever before, also in view of the developments required by EU law in the process of creation of a cross-border EU mortgage market. On the other hand, the English law of mortgage shows an intrinsic flexibility that can be appreciated under various crucial aspects. For example, there are no limits to the possibility of securing future obligations that will arise between the parties, even if they do not derive from a pre-existing legal relationship. Additionally, the usual recourse to extrajudicial enforcement of the security allows for the best balanced outcome, in that it enables the sale of the asset at the highest obtainable price and in a rather short period of time.

c) Italian law has more conservative characteristics in comparison to the other systems considered above. To be sure, the Italian leading formant in the law of security rights over immovables is the civil code. However, the operative effectiveness of the civil code provisions is most often determined by the interpretive action of legal scholarship rather than by their wording. This exacerbates the rigidity and dogmatism of the solutions. On its part, case law produces no original solution and has often been reluctant to adjust written law to the changing needs of law users.

The Italian civil codification (1942) crystallizes a conservative interpretation of the Roman tradition, regulating only one type of security right over immovables, which is established as accessory to the credit (art. 2.808 Civil Code). The legislator’s monistic choice imposes a clear limitation on the interests that can be protected: the arguments in support of a debtor who is seen a priori as the weaker party prevail over the interests of the creditor, as well as over those of the debtor who cannot be qualified as a weak party in need of protection. For this reason only a «stable and secure» security right is regulated, which is accessory to the secured credit. Different solutions experimented abroad have been rejected.

This approach is particularly evident in relation to the crucial issue of control of the proportionality of transactions involving loans secured by immovable assets. On the one hand, this control essentially rests on rigid concepts of the structural accessority of the security right, as well as the specificity of the security in relation to the secured credit. While it is true that the latter characteristic is established by art. 2.852 of the Italian civil code, which precludes any recognition of omnibus security rights, the rule has gone under-debated. The majority of legal scholarship has simply accepted such a rigid concept of accessority that also prohibits the autonomous circulation of the security separately from the original secured obligation. On the other hand, the rigidity of the interpretative idiosyncrasies in this field is confirmed by the exclusive recourse, by courts and academics, to the law of property and «patrimonial liability» —through an

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10 See below sub no. 4.  
13 F. Fiorentini, Le garanzie immobiliari in Europa, 384 ff.  
14 Omnibus mortgages, i. e. mortgages securing all present and future obligations arising between a debtor and a creditor, are instead possible in Germany and England, see F. Fiorentini, Le garanzie immobiliari in Europa, 395-431.
extensive interpretation of the prohibition against forfeiture clauses (art. 2.744 of the Italian Civil Code)—, thereby excluding from the interpretative perimeter any resort to the flexibility of the law of obligations.15

The conclusion regarding the scarce operative success—from a comparative viewpoint—of the Italian system of security rights over immovables is further corroborated by taking into account the characteristics of the enforcement phase. No space is granted for private enforcement of the security, and this has led to a huge overload on the judges. The result is average timeframes that are fairly lengthy for completion of foreclosures: while in England the judicial enforcement procedure is de facto inoperative due to the practice of extrajudicial sale, in Germany 12 months at the most are required to complete a foreclosure. In Italy, the secured creditor is forced to wait 5-7 years on average.

III. THE «COMMON CORE» OF EUROPEAN MORTGAGE LAWS

The historical-comparative perspective briefly accounted above (no. 2) has revealed how differences in methods and approaches to the issue of mortgage credit have led to a lack of homogeneity in the results in the analysed countries. However, the same analysis has revealed some transversal commonalities that can be identified with the «common core» of the European mortgage laws.

1. Principle of publicity and speciality of the security in relation to the asset

The first common factor is that, in order to protect the conflicting interests of both parties, as well as third party creditors (current and potential), there must be adequate publicity of the creation of the security right, as well as of the events that might affect its existence and extinction. This is not only the direction in which Germany and Italy were already moving during the XIX century, but also the course England prepared itself to follow by means of the Land Registration Act 2002.

2. The accessority of the security right

The second factor common to all of the above-mentioned systems (and to other European countries) is the existence of a link between the opposite poles of the security right and the secured obligation. It is this connection that enables, in every system, the control over the balancing of interests between the parties of the secured relationship. Such a link can be embodied in the structure of the security right—and it is thus considered a rigid accessority governed by the law of property and «patrimonial» liability. Otherwise, it might be made dependent on the law of obligations—and it is therefore considered a flexible accessority of the security right, which allows the parties to calibrate their interests with

15 F. Fiorentini, Le garanzie immobiliari in Europa, 471 ff.
greater autonomy, within the elastic perimeter of the general canons of «good faith» and «public morality».

The trend currently emerging in Europe on this issue goes towards a flexible interpretation of the accessority of the security. This allows the security right to secure different obligations with respect to the original one, with no other limits than those deriving from the maximum amount of the encumbrance on the immovable assets (limits that are dictated by the rules concerning registration). It is towards this kind of accessority that national reforms 16, as well as EU law 17, are moving.

3. Proportionality between security right and secured obligation

The uniform presence of the principle of publicity and the accessority of security shows how the basis of the security relationship rests on the concept of proportionality between the amount of the secured obligation(s) and the value of the security in each system. This proportionality —which is expressed by the prohibition against forfeiture clauses, by the rule no clogs on the equity, and by general clauses of the law of obligations— has the ultimate goal of preventing the creditor from obtaining more than what he/she is entitled to receive. In every legal system, proportionality is the guiding principle of the operative solutions to the conflict between creditors and debtors 18.

IV. EU LAW FOR AN INTERNAL MORTGAGE MARKET: TOWARDS A NEW CONVERGENCE

During the past decades, European mortgage laws started to experience a new phenomenon that undeniably pushes toward convergence. It is the gradual implementation of EC/EU actions and measures in the mortgage markets that ends up affecting the similarities and diversities of the domestic regimes mentioned above.

As a matter of fact, despite the ban against EU actions in the area of property law (art. 345 TFEU), especially since 2005, the EU institutions began addressing European mortgage markets with the aim of strengthening the internal market (art. 114 TFEU) and increasing consumer protection (art. 169 TFEU). For the EU institutions, these goals shall be achieved also through the creation of an internal market for mortgage credit. Thereby, a specific EU policy action has been shaped and mise en œuvre 19.

16 With reference to France and Spain, Hungary, Estonia, and Slovenia, see F. Fiorentini, Le garanzie immobiliari in Europa, 426 ff.
17 F. Fiorentini, Le garanzie immobiliari in Europa, 493 ff.
18 F. Fiorentini, Le garanzie immobiliari in Europa, 154-159 for German law; 292 ff. for English law; 471 ff. for Italian law.
19 The interest of the European Community institutions for the mortgage markets of the member states began already in the 1960’s, and addressed the feasibility of substantial rules harmonization between member states. This had to be done by means of the creation of a Euro-mortgage. For a recent account of this story, see V. Sagaert, «Harmonization of Security Rights on Immovables: An Ongoing
The starting point of this policy can be considered the Green Paper on Mortgage Credit\(^{20}\) of July 2005, issued by the European Commission, with the purpose to beginning an evaluation on whether EU «legislative» intervention in this sector would be advisable. According to this document, in August 2005 the EU Commission entrusted the London Economics consultancies with a study on the costs and benefits of EU integration of the mortgage markets\(^{21}\). Following the Commission’s evaluation of this study, a White Paper was published in December 2007\(^{22}\), setting new EU’s strategies, goals and measures to promote efficiency and competitiveness in the European mortgage market.

The White Paper shows that the EU institutions have adopted a multi-level approach to these issues. In other words, the EU Commission intends to achieve an efficient single mortgage market by removing, through the means of «legislative» instruments, relevant legal and economic obstacles to its growth. These obstacles are identified in national divergences on consumer protection standards in the mortgage credit; in a still lacking diversity of mortgage products; in insufficient infrastructures supporting the mortgage credit (like credit reporting systems); in the existence of different domestic legislations on land registration and enforcement of security rights over immovables\(^{23}\).

In the White Paper, the Commission supports the prospective introduction of «legislative» innovations in the contractual terms of mortgage loans that should sound very similar to those contained in the new Directive on Consumer Credit Agreements: Directive 2008/48/EC. In this case, the White Paper promotes a responsible lending, i.e. a lending system based on a series of measures, like a detailed assessment, in the pre-contractual stage, of the creditworthiness of the devised borrower\(^{24}\) and the institution of independent legal advice for consumers seeking access to mortgage credit\(^{25}\). These measures are regarded as essential, not only to the integration of the EU mortgage market, but also to the protection of the latter from dangerous and spreading phenomena like that of the USA sub-prime turmoil\(^{26}\).

It is precisely this direction that the last follow-up of the White Paper, i.e. the Proposal for a Directive of the European Parliament and the of the Council on credit agreements relating to residential property [COM(2011)142 final] of 31March 2011\(^{27}\), took.

\(^{23}\) White Paper fn. above, pt. 3.
\(^{25}\) White Paper, quoted above, fn. 23, pt. 3.3.
\(^{26}\) White Paper, quoted above, fn. 23, pt. 3.1. and 3.3.
\(^{27}\) This document has been issued with three accompanying Commission Staff Working Papers: the Summary of the Impact Assessment [SEC(2011)355 final]; the five annexes to the Impact Assess-
Without going into details of the Proposal for a Directive, it is sufficient to mention that it focuses on mortgage credit to consumers (limited to residential property), as well as on certain prudential and supervisory requirements for creditors and credit intermediaries that, during the financial crisis, have been lacking in many quarters of Europe (arts. 19-23). The core contents of the document aim at implementing, in the states of the European Economic Area, the principles of «responsible lending» and «responsible borrowing». This is done through the provision of precontractual duties of information, obliging creditors and credit intermediaries to make general information available on the range of credit products. Creditors and, where applicable, credit intermediaries will also have to provide personalized information to the consumer on the basis of a European Standardized Information Sheet (art. 9). Moreover, creditors and credit intermediaries will have to provide explanations on the proposed credit agreement(s) to the consumer at the pre-contractual stage, which is determined by the level of consumer’s knowledge and experience with the credit (art. 11). As a general measure, the creditor will have the obligation to assess the creditworthiness of the consumer, by taking into account the consumer’s personal circumstances based on sufficient information provided. In a case that the results of the creditworthiness assessment are negative, the creditor is not to grant the credit, as explicitly spelled out (art. 14). On the consumer’s end, the borrower will also have a disclosure obligation; in other words, it will have to provide all necessary and correct information to enable the creditworthiness assessment to be carried out (art. 15). It is interesting that, in order to limit the general costs incurred by creditors from the implementation of the EU rules, the Proposal for directive does not introduce creditor’s obligation to provide legal advice to the borrower, but is limited to introducing standards of this advice when it is given by creditors (art. 17). In the same way, there is a provision that early repayments must be assured, but member states are left free to regulate extent and conditions of this right (art. 18).

It is important, to the purposes of the present analysis, to bear in mind that the EU policy in the mortgage market is leading toward the gradual emergence of a new level of common rules, prepared or being prepared by EU institutions, which overlap national laws and approaches to the issue of land credit and security. With regard to the private law sphere, these rules tackle the substantial rules of the mortgage loan regimes, introducing minimum standards of pre-contractual obligations on both sides. Thereby, they affect the contractual side of the mortgage loan, and not the proprietary right. While offering the clear advantage of sidestepping the problem of legislative competence of the EU to «intrude» into matters relating to national property law, this strategy —that I call the strategy of the «contractualization» of mortgage law— leaves a series of open issues.

28 The major costs deriving to creditors from the implementation of the EU rules will be shifted to borrowers in terms of higher interest rates. This is the so-called «passing on»: R. CRASWELL, «Passing on the Cost of Legal Rules: Efficiency and Distribution in Buyer-Seller Relationships», 43 Stan. L. Rev., 361 (1991).
V. THE «CONTRACTUALIZATION» OF MORTGAGE LAW. OPEN ISSUES

First, the question regarding a need for harmonisation, extending over the substantial rules of the proprietary security, i.e. the mortgage, is still unanswered. Since the White Paper of 2007, it is clear that the EU institutions have left aside any intention of introducing the Euro-mortgage as substantial law device to be used in cross-border mortgage loans, in addition to the devices already in place in the national laws. However, the abandonment of this perspective has not been explained nor debated. On this issue, the results of the comparative analysis, briefly outlined above (nos. 2 and 3), can offer some arguments. Indeed, the comparison shows that the operative results of the various national approaches to mortgage law lead to similar results in the core aspects of this sector, i.e. the need of an accessory security (although this accessority should be flexible), the need of publicity requirements, and the need of an equitable control over the proportionality of the secured relationship. The differences that result in a disparity of protection of borrowers and creditors in the EU, as well as in an uneven efficacy of the mortgage law regimes, lie (mostly) outside the substantial rules of property and mortgages. They depend both on the mentality of the interpreters of the single systems, and on procedural laws, rules and practices. In this perspective, the introduction of a new common mortgage for European states is not an urgent measure, nor could it give assurances of its capability to overcome the two kinds of diversities just mentioned, that truly impact the applied law.

However, the minor relevance of substantial law aspects of the proprietary side of the mortgage finds a notable exception. This drives us directly to the consideration of the second issue at stake, which is the way to enhance efficacy and standardisation in the field of mortgage enforcement (possibly including insolvency). As indicated in the White Paper, and as resulting from comparative law studies, it is on these points that the EU systems still widely differ. It is here that legislative action is more needed, be it from national legislators or from the EU.

Finally, a third point should be addressed. Among the consequences of the current EU actions in the national mortgage markets of Europe, there is a notable outcome to which legal scholars will have to pay attention to in the future. It is the tendency of modern reforms to shift the problems lying at the core of the mortgage relationship from the proprietary side to the contractual side. If compared with property law, contract law offers clear advantages of regulation in terms of flexibility. This is not a discovery by the EU institutions, but a German achievement that has been delivered to Europe as a legacy for further reforms.

30 See White Paper fn. 23 above, pt. 3 and F. Fiorentini, Le garanzie immobiliari in Europa, 133 ff. for German law, respectively; 269-284 and 310-320 for English law; 446-471 for Italian law.
31 F. Fiorentini, Le garanzie immobiliari in Europa, 99-126 and passim.
It seems that recent attempts by the most part of the European legal systems to overcome the increase in number of mortgage foreclosure actions and their destructive consequences for the society (creditors, borrowers and their families) go exactly in this direction. They make recourse to a variety of special forms of negotiations in the stage prior to commencement of foreclosure proceeding, thereby exploiting the potentialities of the law of contracts and obligations.

VI. THE «FINANCIALIZATION» OF MORTGAGE LAWS: THE FRONTLINE BATTLE

Another point deserves further attention. It concerns the economic forces that guide the European integration of the mortgage markets referred to above (no. 4). The EU mortgage markets policy is not only strongly affected, but also directly led by the so-called «financialization» of the economy. This global phenomenon has the potential to adversely affect the categories, rules and institutes of the national legal traditions—even without a global financial crisis—.

The interest of the finance for the mortgage markets is explained by the stability of the value of immovables. The finance aims at transforming immovable assets—and especially the regular cash-flows deriving from the mortgage loans—in circulating wealth in the capital market. Since the 1980’s, this has happened both in the United States and in Europe (though with different modalities and intensity) through the so-called originate-to-distribute model (OTD) of banking business.

As it is known, the most famous structure of OTD is the securitization of mortgage loans. Through this method, banks or credit institutions do not hold the mortgage loans they originate until maturity, but they distribute them to different types of investors through the issuance of structured financial products (called asset-backed securities). Specifically, a bank or credit institution (the Originator) that seeks to raise funds, gathers and pools existing or future mortgage loans arising from its business activities. A special purpose vehicle (SPV) is created as a bankruptcy-remote trust or corporation. The SPV plays the role of intermediary by purchasing the mortgage loans from the Originator and repackaging the mortgage loans to support (or back) asset-backed securities, to be then issued by the Originator to the investors. The cash proceeds from the sale of the asset-backed securities to the Investors are used to purchase the mortgage loans from the Originator. Investors are willing to purchase securities bearing interest at attractive rates, if the risk of default is reduced to an acceptable level. Rating agencies play a key role in determining the risk level—legal and economic—

32 See the summary of national ways to reduce foreclosure actions by the Commission Staff Working Paper «National measures and practices to avoid foreclosure procedures for residential mortgage loans» [SEC(2011)357 final], accompanying the Proposal for a directive COM(2011)142 final, of 31 March 2011.

which affects the coupon and other terms of the security. Without going into further details, it should suffice to underline that securitization grants a number of benefits to the Originator. It provides an alternative source of financing at lower costs than traditional bank loans. The maturity on an asset-backed security is often longer than a traditional bank loan. The assets sold to the SPV are removed from the balance sheet which may help the Originator achieve certain accounting goals ³⁴.

Despite the global financial crisis, market operators believe that the originate-to-distribute model will still be used by banks and credit institutions as a crucial refinancing technique. Indeed, when the model functions correctly, it has the capacity to distribute risks widely and efficiently. At the same time, it diversifies the revenue streams of the banks that still form the core of the global financial system ³⁵.

It must be underlined that these developments in the international finance inevitably push for the regulation of the traffic of immovable assets and mortgages, which is beneficial to secured lenders who need to make recourse to securitizations, also by repackaging mortgage loans that have originated in different jurisdictions. This is the reason why the financial lobbies are pressuring legal regimes of security rights over immovables to provide techniques that are as uniform as possible for the appraisal of immovable assets, and are also based on increasingly convergent land registration rules. If these are homogeneous needs, it is likely that all legal systems (not only within the European borders) will look for a way to adapt their internal structures to these imperatives that are also compatible with their own traditions ³⁶.

Yet, «financialization» of the economy is not always a virtuous phenomenon. The sub-prime experience clearly demonstrates that the interaction among credit risks, market risks and liquidity risks can produce a dangerous trans-national domino effect, facilitated by the growing integration of financial markets around the globe. In this context, the open challenge for (not only) European financing is now to rebuild, or strengthen, a regulation framework suitable to recover market confidence in relation to securitizations of mortgage loans. The EU is now aware ³⁷ that among the technical difficulties surrounding securitizations many other factors are relevant. Reference must be made to the unsuitab-

³⁶ The most notable example of this is the English way of reform of its land registration system, by way of Land Registration Act 2002 and subsequent implementations. This reform is leading the UK outside the traditional system of land transfer without registration, based on the interrelation of common law and equity rules. The unsuitability of such system to the needs of modern structured financial operation is evident. See F. Fiorentini, Le garanzie immobiliari in Europa, 249-258 and above sub no. 2(b).
³⁷ On 20 July 2011, the Commission adopted a proposal for a legislative package to strengthen the regulation of the banking sector. The proposal replaces the current Capital Requirements Directives (2006/48 and 2006/49) with a Proposal for Directive [COM(2011)453final] and a Proposal for a Regulation [COM(2011)452 final] and constitutes another major step towards creating a sounder and safer financial system. The directive governs the access to deposit-taking activities, while the regulation estab-
ity of supervisory authorities on financial markets and the imperfections of the regulations governing rating procedures and companies; along the same lines, the lack of transparency regarding financial instruments that hinder investors’ easy evaluation of profitability and the risks connected to such products.

The frontline on financial battle will be world-wide regulation of supervisory systems on banks and financial institutions, improvement of risk measurement techniques to be applied to financial operations and instruments, and in general better transparency of the financial system. After the global financial crisis, the EU policies of «responsible lending» and «responsible borrowing», which are centered on the standardization of selected aspects of the mortgage loans, will never suffice to assure the economic splendors as envisioned by the EU institutions as a direct consequence of the expansion of an internal mortgage market.

lishes the prudential requirements institutions need to respect. See http://ec.europa.eu/internal_market/bank/regcapital/index_en.htm.


40 The economic quantification of these advantages is lastly to be found in the Proposal for a Directive of the European Parliament and the of the Council on credit agreements relating to residential property [COM(2011)142 final] of 31 March 2011 (at p. 6 and 7): the estimated total benefits of the measures envisaged by the Proposal for directive are in the range of EUR 1272-1931 million. The expected total one-off and ongoing costs are in the range of EUR 383-621 million and EUR 268-330 million respectively.