Foundation Mortgage Guarantee Fund for Homeownership in the Netherlands (Stichting Waarborgfonds Eigen woningen)

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Introduction

The Mortgage Guarantee Fund for Homeownership (MGFH) in the Netherlands is a non-profit private foundation. This foundation is established in 1994 as successor of the municipality guarantee with a backing support of the central government.
Main objectives of the foundation are to promote homeownership and to improve the quality of owner-occupied dwellings. To realize these objectives the MGFH is issuing the National Mortgage Guarantee (NMG) which is a guarantee for the timely and fully repayment of mortgage loan obligations of consumers towards their financier.

Background

The MGFH is a lean and efficiently operating organization, which is managed by a board of supervisors. The Government, the union of municipalities, a union of financiers and the national consumers-organization of owner-occupants appoint the five members of the board, including an independent chairman.

The guarantee structure is based on a set of terms and rules that can be changed each year only with the approval of the Minister of Housing and the board of the union of municipalities.

The MGFH guarantee doesn't involve the whole Dutch mortgage-market. The guarantee is limited for loans aimed at purchasing an existing or newly build own house to about Eur200,000. Guaranteed loans for renovation fall under the same guarantee conditions. According to the government policy higher priced houses are excluded from the guarantee-system. Buyers of houses are supposed to be able to possess enough financial opportunities.

In terms of market share guaranteed loans cover nearly 80% of total yearly mortgage-transactions. Within the bounded reach of the guarantee this means that more than 40% of the mortgages supplied, is financed with NMG. As a result since the start of the instrument (from 1995) more than 300.000 guarantees are supplied.

Consequently and blessed by few losses the value of the fund capital has accumulated to Eur170 million or about 0,45% of total guaranteed debt at the end of 2000. The total guaranteed outstanding loan value at the end of 2000 reaches Eur35 billion, up from Eur3,5 billion in 1995. Under normal economic conditions the build-up reserves are adequate to counter debt claims. Although one can't exclude any housing downturn future expectations indicate a relatively strong business profile for the most desirable type of housing tenure namely private homeownership.

Essentials

The guarantee structure means that financial risks dedicated to mortgage loans have been transferred to the MGFH. In that way the foundation is acting as surety pursuant to deeds of surety between the fund and participating financiers. The deeds of surety serve to secure the payment of claims when a consumer is not capable of fulfilling his loan obligations to the lender.

Central government and participating municipalities behave as a catcher providing the fund interest-free loans to top up the guarantee-reserves if they fall below a minimum obliged level.

To operate efficiently the issuing of the NMG is delegated to the participating financiers. This takes place on the basis of a set of uniform conditions applying to all households living in the Netherlands. The MGFH's tariff and contract structure must each year be approved by the Ministry of Housing and the union of municipalities.

Relations
Between MGFH and Financier

The relation between the MGFH and the financier is embodied in a deed of surety to cover the loan obligations from the borrower. This guarantee document becomes manifest in case of default by the eligible consumer.

The MGFH starting point for its policies is that each financial institution with which it has a guarantee arrangement acts in good faith and that breaches of the conditions and terms which do not have a material influence on the occurrence and the size of the loss, lead to a payment of the submitted claim.

Part of the agreement is that the MGFH delegates to financiers the checking procedure on borrowers wishing to have their mortgage guaranteed. The assessment is computerized and fully integrated within the tender procedure getting a loan for buying a house or for renovating. So by providing guarantee and financial means in one hand (the financier) benefits the handling through which waiting time has dropped to a minimum.

The lender must register a mortgage loan that is backed by the guarantee with the MGFH within two weeks after the guaranteed mortgage loan has been extended to the borrower.

In case of a foreclosure by way of a private or a public sale of the mortgaged property the financial institution must make a formal request to the MGFH for payment of the deficit accompanied by the financial institution's file in respect of the mortgage loan concerned.
Consequently the guarantee structure can be conceived as a system with repressive supervision.

Between MGFH and government

The relation between the foundation and the central government including the participating municipalities is structured in a backstop agreement. This agreement serves to secure the

payment of debts from lenders in case the fundreserves are drifting down into a state of illiquidity. Emerging such a state the MGFH enjoys the contractual support of the central government and participating municipalities. They provide the foundation unlimited interest-free loans to carry out the accepted debt claims. Ultimate liability for the liquidity of the guarantee, therefore, is a matter of political support.
Due to the backing of the government, the Dutch Central Bank considers the NMG as a government guarantee. In effect guarantee-backed loans favor a zero solvency. This will enlarge the possibilities for off-balance activities by means of securitizing loan portfolios as guaranteed loans can be considered as triple A rated. This kind of selling is a growing phenomenon in the Netherlands as well as in the Euro-zone.

Capital position

A strong economic development since the mid nineties as well as a stimulating private homeownership encouraged by housing policies to enlarge private homeownership around a wished 65% in 2010, are the main factors for a steady growth of the fund's equity capital. This capital has been build up through guarantee premiums paid by the borrower, which are cashed through the mediation of the associated financial institutions.

Premium

The premium has to be paid only once and is recalculated each year on basis of an actuarial paragon. For 2001 the borrower pays 0,30% of the loan amount. Thanks to the Dutch fiscal policy this premium is completely deductible for the income tax. Another consumer's benefit is laid in the lower than market interest rate for guaranteed loans due to the risk transfer. All together the costs of the premium for the consumer are recovered within a year.

Risk allocation

Through the introduction of a guarantee system for homeownership risks of repayment the outstanding principal, interest and costs on default by the consumer are taken over by the MGFH. Financiers benefit from this risk reduction by means of a zero solvency.
Housing consumers wishing to have their loan obligations guaranteed will be assessed by the lender to ensure that they satisfy the guarantee rules. An important issue is that there must be a sound ratio between the loan and value and the loan and the household income. If so, borrowers can finance the purchase of a house within the framework of conditions completely without having own resources. Furthermore the guarantee-instrument serves as a safety net for owner-occupants. That is the case when the borrower can't satisfy his loan obligations. With an eventually forced sale followed by a resting debt claim from the financier, the borrower can be responsible for the debt. However when the borrower cannot be blamed for the forced sale, the claim is remitted. Remission is granted in situations of unemployment, incapacity for work and divorce.

Conclusions

The substitution of risk from the lender to the fund is an efficiently way to improve the mechanism of the housing and mortgage market. Seen in that respect the NMG is not only an instrument to promote homeownership and to mitigate micro-economic risks.

In a more extended sense it becomes an instrument that also limits the macro-economic risks. Especially in times of recession the NMG can contribute in stabilizing the economic development.

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