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Deputy Caoimhghín Ó Caoláin, TD
Chair, Joint Committee on Justice and Equality
Houses of the Oireachtas
Kildare St
Dublin 2
D02 XR20

27 October 2018

Dear Chair

I am writing to you following a request by your Committee to consider the Mortgage Arrears Resolution (Family Home) bill 2017. The bill is not proposing changes to the Bank's mandate or powers, therefore the Bank's comments are focused on the potential effects on existing restructuring activity and accompanying protections, as well as the possible longer-term effects on all borrowers.

Behind each arrears case, there are people undergoing distressing personal experiences. Given the length of time it has taken banks to deal with some aspects of this serious problem, the intent of the bill is therefore understandable. The Bank has taken various steps to address this by setting system-wide standards to ensure that borrowers are restructured sustainably and extending the protections of the Code of Conduct of Mortgage Arrears (CCMA) when loans have been transferred. The restructuring arrangements offered and implemented by lenders have improved significantly since 2013, with less reliance on short-term forbearance. The Bank has also taken a number of steps to strengthen the CCMA in 2013, and providing technical assistance to the Department of Finance in their development of the Consumer Protection (Regulation of Credit Servicing Firms) Act (the Credit Servicing Act) in 2015. Both are designed to ensure that borrowers whose loans are transferred from a regulated lender, have the same level of consumer protections they had prior to the sale.

Various policy changes have been made in recent years to improve the non-judicial debt resolution mechanisms available for distressed borrowers, including those encompassing the entirety of a borrower's debt. Recent legislative changes allow for rejected Personal Insolvency Arrangements (PIA) to be reviewed by the Courts. The bankruptcy term has been reduced to one year, consistent with other international jurisdictions whereas previously it was 12 years.

Nevertheless, given the slow pace of progression for some cases, particularly those in long-term arrears, it is understandable that the Oireachtas wish to address some aspects of the mortgage arrears through the legislative tools at its disposal.

While it is for the political and legal systems to balance property rights and legal contracts between borrowers and lenders or holders of mortgages, there are unintended risks with well-intended legislation. The bill will introduce additional complexity without regard for the existing restructuring processes, may not result in the desired outcomes, and some aspects need further development.



The most significant unintended consequence would be inhibiting the mortgage restructuring process that is currently working for the majority of borrowers. During Q2 2017, there were over 7,000 new restructures put in place across the system and over 120,000 mortgages restructured at end Q2 2017. This bill may result in borrowers currently in the restructure pipeline, potentially having restructures altered or activity ceasing.

The draft bill proposes various types of restructure to be imposed via a mortgage resolution order (MRO). It appears that the bill will impose MROs on an individual institution basis, without restructuring other non-mortgage debt incurred by the debtor with other institutions. It is also unclear how non-mortgage creditors would react to the bill. This is a particular concern for some borrowers in deep arrears, as they have substantial non-mortgage debt. A borrower's entire debt is taken into account within a PIA/bankruptcy as well as the totality of their assets, liabilities, and income.

The long-term implications of this legislation require further consideration by the relevant Government departments, as it results in non-recourse lending for the duration of the mortgage order. During Q2 2017, 231 of 340 properties or 66 per cent were voluntarily surrendered; 109 or 33 per cent were repossessed through a court order. While repossession is a last resort under the CCMA, the ability to undertake secured lending is ultimately dependent on the power to realise security if needed. This is a cornerstone of secured lending and, by extension, a functioning mortgage market. This bill may have significant ramifications for secured lending in Ireland, impairment provisioning, and capital depending on its final form and the numbers of orders granted. The bill may have important implications for mortgage pricing and mortgage supply for all borrowers, not just the group of borrowers covered by the bill.

Where debt-relief programmes have been used in other jurisdictions, such as a US HAMP-style programme, they have clearly defined entry criteria for borrowers, specific targets for sustainability of mortgage restructuring, and clear exit criteria. They were also subject to conditionality for both banks and borrowers, and the fiscal cost of this debt relief is monitored and apportioned.

The current draft of the bill is yet not clear regarding definitions of financially restricted mortgagor, the criteria for sustainability, and the exit criteria from the order. The bill needs to be clear regarding the criteria for where a debtor may not perform according to the terms of the MRO. Similar to the ISI, the MRO should regularly produce information on all restructures, including debt write-downs.

While it is for the Committee to decide on ECB consultation, the draft bill is applicable to financial institutions, and may materially influence the stability of financial institutions and markets. This is one of the areas of competency for ECB consultation.

I hope these views and the attached note are useful to the work of the Committee in its consideration of this bill.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Ed Sibley', written over a horizontal line.

Ed Sibley
Deputy Governor (Prudential Regulation) and
Registrar for Credit Unions

Encl.



The Mortgage Arrears Resolution (Family Home) Bill 2017

Overview

The mortgage arrears and debt resolution landscape has fundamentally changed in Ireland in recent years. Relative to 2012, the restructuring arrangements offered and implemented by lenders is significantly different and much broader. There has been a noticeable shift away from interest-only type arrangements to more sustainable solutions such as split mortgages. The Central Bank has also taken a number of steps to strengthen the consumer protection framework. This includes the Central Bank's enhancement of its Code of Conduct on Mortgage Arrears (CCMA) in 2013 and the Central Bank's technical assistance in the development of the Consumer Protection (Regulation of Credit Servicing Firms) Act (the Credit Servicing Act) in 2015 to ensure that borrowers whose loans are transferred from a regulated lender have the same level of consumer protections they had prior to the sale.

There are a range of other debt resolution mechanisms available for distressed borrowers that were not in place in 2012. Insolvent debtors can now avail of three types of insolvency arrangements. Recent legislative changes allow for rejected Personal Insolvency Arrangements (PIA) to be reviewed by the Courts. The bankruptcy term has been reduced to one year, consistent with other jurisdictions. The Mortgage to Rent (MTR) scheme has also undergone a number of changes, most recently in February 2017. There are now a range of advisory services available for borrowers in financial distress including MABS, Step Change, and the recently introduced "Abhaile" scheme for borrowers who may be at risk of losing their homes.

Importantly, principal dwelling home (PDH) mortgage accounts in arrears have reduced for sixteen consecutive quarters, representing a 48% reduction since the peak in June 2013. There are now approximately 70,000 accounts less in mortgage arrears. Where feasible, solutions are being found for borrowers that engage with their mortgage lender (or credit servicing firm). At end-June 2017, over 120,000 accounts were classified as restructured, and almost 9 in 10 (87%) are meeting the terms of the arrangement.

The positive momentum in relation to arrears reductions and the high levels of restructured accounts meeting the terms of their arrangements demonstrates the willingness and ability of borrowers and institutions to enter into solutions that address mortgage arrears.

The Mortgage Arrears Resolution (Family Home) Bill 2017 aims to “provide for the establishment of a Mortgage Resolution Office; to provide for a non-judicial Mortgage Resolution Order concerning mortgages over family homes; to provide for an independent appeals process against decisions of the Mortgage Resolution Office; and to provide for related matters.”

To provide some context, since September 2009, 7,799 properties have been repossessed in Ireland, 67% of which were voluntarily surrendered or abandoned by the borrower with the remainder attributable to court orders. This compares to over 120,000 restructured accounts at end-June 2017. As per the CCMA, repossession is a last resort.

A broad range of restructuring options are available to borrowers, depending on their individual circumstances. Some of these options have been subject to legislative changes in recent years to improve their efficacy.

While it is understandable that the Oireachtas wish to address some aspects of the mortgage arrears through legislation, introducing additional complexity without considering existing restructuring processes may not result in the desired outcomes. The proposals outlined in the bill will likely add complications to the existing suite of restructuring options, making the process more complex for borrowers without a clear delineation between both sets of policy tools.

This may have significant unintended consequences including inhibiting the mortgage restructuring process. This may affect those currently engaged in the restructure process, potentially altering the types of restructure offered, and diminish the effectiveness of the existing non-judicial debt settlement (PIA/bankruptcy). This may adversely impact property rights, contracts between banks and borrowers.

The draft bill proposes various types of restructure to be imposed via a mortgage resolution order (MRO). It appears that the bill will impose this on an individual institution basis, without restructuring other non-mortgage debt incurred by the debtor with other institutions. It is also unclear how non-mortgage creditors would react to the bill. This is a particular concern for some borrowers in deep arrears as they have substantial non-mortgage debt. The totality of a borrower’s debt would be taken into account within a PIA/bankruptcy as the totality of the assets, liabilities, and income are assessed.

The long-term ramifications of this legislation require further consideration by the relevant Government departments, as it effectively means non-recourse lending for the duration of the mortgage order. The ability to undertake secured lending is ultimately dependent on the power to realise security if needed. This is a cornerstone of secured lending and, by extension, a functioning mortgage market. This bill may have significant ramifications for secured lending in Ireland,

impairment provisioning and regulatory capital depending on its final form and the numbers of orders granted, if it becomes law. The bill may have important implications for mortgage pricing, and mortgage supply for all borrowers, not just the group of borrowers covered by the bill.

The objectives of the bill for borrowers should be clearly defined. Key concepts within the bill should also be clearly defined. The current draft of the bill is yet not clear regarding definitions of financially restricted mortgagor, the criteria for sustainability, and the exit criteria from the order. The bill also lacks a clarity regarding the criteria for a debtor to not meet the terms of the MRO.

Where alternative non-legislative solutions have been deployed in other jurisdictions, such as a US HAMP-style programme, they have clearly defined entry criteria for borrowers, specific targets for sustainability of mortgage restructuring, and clear exit criteria. As well as providing incentives, they were also subject to conditionality for both banks and borrowers, and have explicit fiscal costs.

In large-scale debt relief programmes, costs as well as benefits will be borne by various groups depending on the choices made. While these choices are a political decision, the allocation of costs of enforced debt write-offs that may occur as a consequence of MRO should be made explicit. Details of restructuring activity should be recorded and published by the MRO, similar to the ISI.

PDH Mortgage Arrears

Within the remit of the Central Bank's responsibilities, the approach to mortgage arrears resolution is focused on ensuring the fair treatment of borrowers through a strong consumer protection framework while ensuring banks have appropriate arrears resolution strategies and operations, are sufficiently capitalised and hold appropriately conservative provisions.

PDH mortgage accounts in arrears peaked in Ireland in June 2013, at 142,892. Since then, considerable progress has been made in addressing mortgage arrears (see Figure 1). June 2017 marked the sixteenth consecutive quarterly reduction, representing a 48% reduction since the peak, equivalent to almost 70,000 accounts less mortgages in arrears.

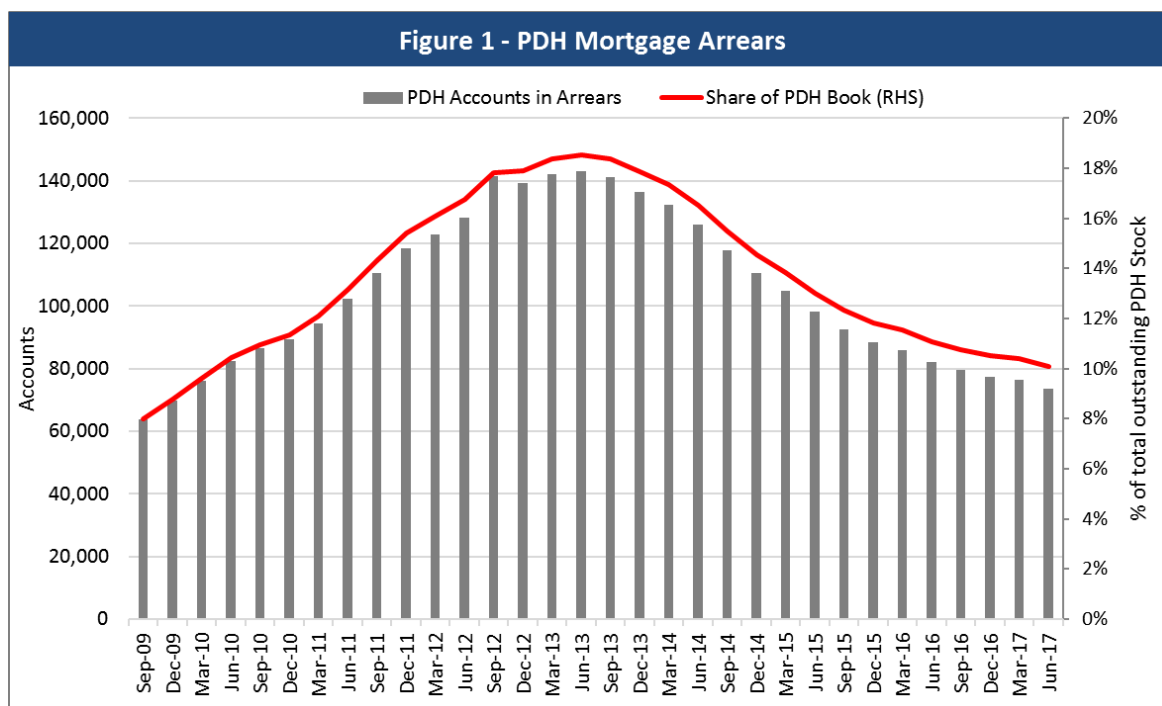


Figure 1 – Central Bank’s Mortgage Arrears and Repossession Statistics

Coinciding with the introduction of the Central Bank’s Mortgage Arrears and Resolution Targets (MART) in 2013, there has been a noticeable change in the composition of restructures agreed, with a shift away from interest-only type arrangements to more sustainable solutions such as split mortgages for example. Where feasible, solutions are being found for borrowers that engage with their mortgage lender (or credit servicing firm). At end-June 2017, over 120,000 accounts were classified as restructured, with over 87% meeting the terms of their arrangement.

Nevertheless, over 73,000 accounts remain in arrears, of which 70% are more than 90 days past due (a sign of more significant distress). Momentum needs to be maintained and it will take time for arrears levels to return to normalised levels. However, the positive momentum in relation to arrears reductions (including the improvements in recent years in accounts over 2 years past due) and the high levels of restructured accounts meeting the terms of their arrangements demonstrates the willingness and ability of borrowers and institutions to enter into solutions that address mortgage arrears.

Consumer Protections

The CCMA is part of the wider consumer protection framework in place for mortgage borrowers, which also includes the European Union (Consumer Credit Agreements) Regulations 2016 and the Consumer Protection Code 2012. The CCMA provides a strong consumer protection framework to ensure that borrowers in financial difficulty are treated in a timely, transparent, and fair manner by

regulated entities. Banks, retail credit firms and credit servicing firms servicing loans on behalf of unregulated loan owners are all required to comply with the CCMA. This includes requiring such regulated entities to proactively encourage borrowers to engage with it about financial difficulties which may prevent the borrower from meeting their mortgage repayments. It also requires regulated entities to consider the full circumstances of each borrower in seeking to resolve arrears cases.

The CCMA also provides protections to the borrower regarding when court proceedings can be initiated. Under the CCMA, a regulated entity may only commence legal proceedings for repossession of a primary residence where it has made every reasonable effort to agree an alternative repayment arrangement (ARA) with the borrower and other clear requirements are met. The CCMA requires firms to exhaust the options available from the suite of alternative repayment arrangements offered before taking action which may result in the borrower losing their home (whether by voluntary sale or repossession).

There is evidence that the Mortgage Arrears Resolution Process (MARP) set out in the CCMA is working for borrowers who engage with the Process. A bulletin published by the Central Bank in May 2016¹ showed that:

- Of those borrowers who completed the MARP with the credit institutions covered by the bulletin, the percentage who were offered an ARA ranged between 89% in H1-2014 and 87% in H2-2015.
- From H1-2014 to H2-2015, between 91% and 94% of ARAs offered by the lenders in question were accepted by the borrower.
- The proportion of appeals to the lender's Appeals Board relating to an offer of an ARA, or a lender's decision not to offer an ARA, that were upheld/partially upheld in favour of the borrower ranged between 33% in H1-2014 and 23% in H2-2015.²
- The proportion of appeals to the Lender's Appeals Board against being classified as not co-operating that were upheld/partially upheld in favour of the borrower ranged between 31% in H1-2014 and 39% in H2-2015.

Following the enactment of the Credit Servicing Act 2015, the Central Bank also developed a robust regime for the new regulatory category of 'credit servicing firm'. This includes the full application of

¹ <https://www.centralbank.ie/docs/default-source/Regulation/consumer-protection/compliance-monitoring/reviews-and-research/gns4-2-1-1-cpbullet-coc-mort-arrears-310516.pdf?sfvrsn=6>

² The CCMA requires a lender to operate such an Appeals Board and contains specific requirements on how it is to be operated.

consumer protections in the context of credit servicing firms' regulated activities, underpinned by an expectation of high standards and a professional and consumer-focused approach to compliance consistent with the Central Bank's consumer protection framework.

Other Debt Resolution Options

The Personal Insolvency Act 2012 introduced three types of debt resolution mechanisms for insolvent borrowers: the Debt Relief Notice (DRN), the Debt Settlement Arrangement (DSA) and the Personal Insolvency Arrangement (PIA). A PIA can include secured (e.g. a mortgage on a PDH or BTL) and/or unsecured debt. Legislative changes implemented in 2015 include provisions allowing for a personal insolvency practitioner (PIP) to request a review by the Court where a PIA was rejected by creditors. There has been a gradual upward trend in the number of PIAs approved per year, and since 2013, 1,842 PIAs were approved.

The PIA 2012 act modified the personal bankruptcy regime. One of the main changes reduced the duration of bankruptcy from twelve to three years. The bankruptcy term was subsequently reduced to one year via the Bankruptcy (Amendment) Act 2015, bringing Ireland's bankruptcy regime in line with other international jurisdictions. Between 2013 and June 2017, and there were 1,696 bankruptcy adjudications.

Debtor Advice

There are a range of independent advisory services available for borrowers in financial distress. For example, MABS, established in 1992, provides information, advice and assistance to borrowers in arrears. StepChange Debt Charity Ireland also provides an advisory service for people struggling with debt problems. Most recently, the "Abhaile" service was established in late 2016 and provides mortgage arrears support in the form of vouchers for free financial or legal advice.

Secured Lending

However, in some cases, loss of ownership of the PDH may be unavoidable. Indeed, the ability to undertake secured lending is ultimately dependent on the power to realise the security if needed. This is a cornerstone of secured lending and, by extension, an effectively functioning mortgage market. Relative to many other European jurisdictions, including those with lower levels of non-performing loans, the legal process through which lenders effect security is substantially longer in Ireland, and the repossession rate is much lower than in other comparable jurisdictions.

Since September 2009, 7,799 properties have been repossessed in Ireland, 67% of which were voluntarily surrendered or abandoned by the borrower with the remainder attributable to court orders. This compares to over 120,000 restructured accounts at end-June 2017.

During the most recent quarter (Q2 2017), court proceedings were initiated in relation to over 1,200 accounts. In comparison, over 7,000 new restructure arrangements were agreed during the same period.³ The initiation of legal proceedings does not ultimately imply that the borrower will lose their home. During the legal process, borrowers have opportunities to re-engage with lenders to find a solution and Central Bank aggregate data show that 13% of legal cases that have concluded (since the beginning of 2013) are due to terms and conditions being renegotiated.

ECB Consultation

It is worth noting that in accordance with Article 127(4) of the Treaty on the Functioning of the European Union and Article 4 of the ESCB Statute there is an obligation on national authorities to consult the ECB on certain draft legislative provisions. The framework for such ECB consultations is set out in Council Decision 98/415/EC and the ECB has published a guide on such consultations available [here](#). While it is for the Committee to decide this consultation, the draft bill does involve legislation applicable to financial institutions that may materially influence the stability of financial institutions and markets which is one of the areas in which the ECB should be consulted.

Conclusion

The Mortgage Arrears Resolution (Family Home) Bill 2017 aims to:

“provide for the establishment of a Mortgage Resolution Office; to provide for a non-judicial Mortgage Resolution Order concerning mortgages over family homes; to provide for an independent appeals process against decisions of the Mortgage Resolution Office; and to provide for related matters.”

As noted in the sections above, there already exists a broad range of options available to borrowers, depending on their individual circumstances. The positive momentum in relation to arrears reductions (which have reduced for sixteen consecutive quarters) and the high level of restructured accounts meeting the terms of their arrangements demonstrates the willingness and ability of borrowers and institutions to enter into solutions that address mortgage arrears. There are a number of other debt resolution mechanisms for distressed borrowers including three types of insolvency arrangements. Recent legislative changes have introduced an appeals mechanism for rejected PIAs.

³ This includes first-time restructures and further modifications of existing restructures.

The legislative proposals outlined in the bill will likely add unnecessary complications to the existing suite of options, making the process more complex for borrowers; may adversely impact property rights and legal contracts; and may have significant unintended consequences including the slowing of the mortgage restructuring process. Furthermore, the ability to undertake secured lending is ultimately dependent on the power to realise the security if needed. This is a cornerstone of secured lending and, by extension, an effectively functioning mortgage market. This bill could have significant ramifications for secured lending in Ireland, and consequently, important implications for mortgage pricing and the supply of credit to the wider economy.