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Deputy Pearse Doherty
Leinster House
Kildare St
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22 June 2020

Re: Interest accrual during payment moratoria

Dear Deputy Doherty,

I refer to your letter of 11 June 2020 requesting clarity on the application of the EBA Guidelines on legislative and non-legislative moratoria on loan repayments applied in light of the COVID-19 crisis (EBA Guidelines).[1]

I wish to set out a number of relevant regulatory considerations with respect to interest rates and provide you with a response to the questions you have posed, specifically:

1. How does the application of moratoria on repayments in Spain and Belgium, where interest does not accrue during the moratorium period for certain customers, interact with EBA Guidelines and associated regulations?
2. Does the application of moratoria on mortgage repayments for customers affected by the COVID-19 crisis, whereby interest does not accrue for the moratorium period, comply with EBA Guidelines and associated regulations?

[1] EBA Guidelines

3. Can moratoria on mortgage repayments for customers affected by the COVID-19 crisis, whereby interest does not accrue for the moratorium period, be applied without triggering forbearance classification?
4. Does the application of moratoria on mortgage repayments, as implemented in Spain and Belgium where interest does not accrue for the moratorium period, impact on the capital requirements on lenders?

The Central Bank of Ireland (Central Bank) continues to engage with regulated firms to ensure they give appropriate support to borrowers whose incomes and affordability have been affected by COVID-19. Payment breaks, extended under the Irish non-legislative moratoria programme, are being offered in this context and operate in a way that protects borrowers, in line with the relevant codes and regulatory requirements.

The Central Bank has set out its supervisory expectations, applicable to both bank and non-bank firms, for COVID-19 payment breaks extended under the Irish non-legislative moratoria programme.[2] The application of payment breaks and the treatment of borrowers in financial distress will continue to receive significant regulatory attention from the Central Bank.

The Central Bank does not have a statutory role to prescribe the interest rates charged by regulated firms and neither does it have direct powers under the non-legislative payment moratorium to instruct firms to amend commercial contractual agreements. Furthermore, the role of the Central Bank within the legislative process is limited to providing technical support to the Department of Finance, when requested to do so, and to enforce existing legislative requirements with respect to regulated firms.

Within the regulatory framework and the applicable accounting regulations, bank loans are classified according to a common set of standards. Changes to interest charging can, under these rules, result in forbearance implications and loans becoming classified as in default, which can have implications for both borrowers and banks. Within the Capital Requirements Regulation (CRR), non-accrual of interest is taken to be an indicator of a borrower's 'unlikeliness to pay' on a material credit obligation. If a borrower is classified as such, in line with the requirements of the

[2] Dear CEO Letter on payment breaks (8 June 2020)

definition of default, this borrower is classified as defaulted from a prudential perspective. Such classification would have implications from a provisioning perspective under International Financial Reporting Standard (IFRS 9).

As part of the EBA, the Central Bank has engaged fully in the regulatory policy on this matter. The EBA Guidelines seek to provide flexibility with respect to reclassification requirements. The EBA Guidelines prescribe the criteria which moratoria must meet in order to be classified as sufficiently general and broadly applied. Where these criteria are met, the guidelines clarify the prudential treatment of moratoria and, in particular, states that eligible moratoria do not trigger classification as forbearance or distressed restructuring. One of the conditions stipulated is that the moratorium envisages only changes to the schedule of payments, namely by suspending, postponing or reducing the payments of principal amounts, interest or of full instalments, for a predefined limited period of time. No other terms and conditions of the loans, such as the interest rate, should be changed.

The EBA is expected to provide further clarity on the specific issue of interest accrual under the EBA Guidelines. However, at present both net present value (NPV) neutral (implying interest accrual) and NPV negative solutions (in which interest does not accrue and where the lender experiences a loss due to the imposition of the payment break) is permissible. As a result, the approach taken by Irish banks, whereby interest continues to accrue on exposures subject to the COVID-19 moratoria, is acceptable within the context of the EBA Guidelines.

Regarding payment moratoria in other jurisdictions, and the divergent approaches across EU Member States with respect to interest accrual for mortgage exposures, it is the Central Bank's understanding that such decisions are attributable to many factors, including the nature of the moratorium in place and associated domestic legislative provisions which apply. Compliance with the EBA Guidelines is a matter for the EBA and relevant competent authorities in the respective Member States in line with relevant national legislation. Nonetheless, as noted above, the EBA guidelines do allow for payment moratoria to be applied whereby interest does not accrue for the moratorium period without, of itself, triggering forbearance classification or changes to capital requirements for the duration of the payment break.

The Central Bank will continue to engage with regulated firms to ensure that they give appropriate support to borrowers whose incomes and affordability have been affected by COVID-19. The Central Bank has required that regulated firms have plans and the operational capability to deliver an assessment of all borrowers on payment breaks to ensure that appropriate and sustainable solutions are identified in a timely manner for those borrowers who are not able to return to paying full capital and interest at the expiry of the payment break.

Yours sincerely,