Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

Protecting consumers in a changing economic landscape

April 2023

In November 2022, we issued a Dear CEO letter to all regulated firms setting expectations for how they support their customers in the face of the rising cost of living. We issued this letter to ensure consumers across the financial system were supported to the fullest extent of the regulatory framework for which the Central Bank is responsible. We have seen firms across the financial system respond to these expectations, and the challenges facing consumers in the current economic environment will remain a key area of focus for the Central Bank.

In the area of mortgages, where we have seen rising interest rates, since the November 2022 letter we have been engaged with lenders, credit servicing firms and other stakeholders in a phased and targeted body of supervisory work. This note summarises our work to date and ongoing on this matter, including work to ensure regulated firms:

- Enhance the supports available to borrowers in or facing arrears. This includes enhancing early warning indicators as rate increases impact on borrowers and the analysis conducted by firms to identify those borrowers who may require additional support;
- Have sufficient operational capacity in place to manage applications by borrowers to switch their mortgage or mortgage provider, and that there is no discrimination against borrowers based on where they currently hold their mortgage; and
- That increases in mortgage interest rates are in line with mortgage terms and conditions, firms' published variable rate policy statements and the regulatory framework for which the Central Bank is responsible.

A strengthened framework to protect mortgage borrowers

Our work on rising principal dwelling houses (PDH) mortgage interest rates builds on the actions the Central Bank has taken in recent years to enhance resilience in the financial system and strengthen the consumer protection framework. This has included a range of measures over and above the protections that apply under EU and domestic legislation to ensure the system supports and protects mortgage borrowers through all stages of the mortgage life cycle.

These protections run from the point of a borrower looking to take out a mortgage (including through our macro-prudential mortgage measures[1]), when examining options to switch to another mortgage

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[1] These measures introduce loan-to-value and loan-to income lending limits to ensure sustainable lending standards in the mortgage market. Details available here.

product or provider and when in, or facing, financial difficulty. In the case of borrowers on a variable rate mortgage, it includes requiring lenders to have a publicly available variable rate policy setting out their approach to setting variable interest rates, as well as requiring firms to provide specific information to a borrower when notifying them of an interest rate increase. The Central Bank is working to ensure firms apply all elements of this framework properly to support borrowers facing rising costs of living and rising interest rates. In 2022, for example, this included intervening to ensure lenders had sufficient resources available to process applications for mortgages within the timeframes specified in the Consumer Protection Code. We took this step because we identified delays arising from an increase in borrowers looking to switch their mortgage. These delays have since been dealt with by the firms concerned.

In the case of borrowers in or facing arrears on the loan secured on their home, the Code of Conduct on Mortgage Arrears (CCMA) provides a highly protective and effective framework. At end-December 2022, the number of accounts[2] in long-term mortgage arrears[3] (LTMA) had reduced to less than 23,000 for the first time since the Central Bank started its data collection on mortgage arrears.[4] This is significant in terms of indicating the systemic capacity to resolve arrears since LTMA are typically some of the most difficult arrears cases to resolve. This progress came after sustained supervisory engagement by the Central Bank, with the most progress being made by non-bank firms to whom distressed loans had been transferred, reflecting the higher concentration of LTMA being managed, and the resolution strategies and approaches of these firms.

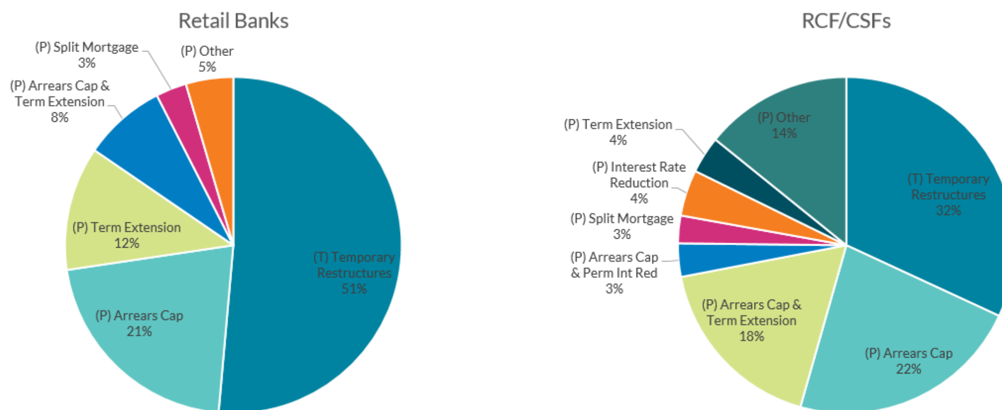
The current mortgage market

There are two main categories of firms that hold PDH mortgages – retail banks and the non-bank lenders. The non-bank sector is made up of retail credit firms (RCFs) and credit servicing firms (CSFs).[5] RCF/CSFs can be further sub-categorised into RCFs who themselves lend ('lending RCFs') and RCF/CSFs who do not lend and only service loans they hold ('non-lending firms').

[2] An account which records a loan to an individual for house or apartment purchase, renovation, improvement or own construction of housing, which is fully or completely secured by a mortgage on the residential property. The mortgage arrears statistics are presented at account level, rather than property level or customer level.
[3] Arrears greater than one year.
[4] Central Bank Residential Mortgage Arrears & Repossession Statistics Q4 2022
[5] For more information on retail credit firms, see here and for more information on credit servicing firms, see here.

Since they only service existing loans that are transferred to them by other lenders, non-lending firms do not have a range of generally available products the other firms would have. For example, a retail bank or a lending RCF would have a generally available fixed rate mortgage whereas a non-lending firm would not. On the other hand, non-lending firms do typically have amongst the widest range of Alternative Repayment Arrangements (ARAs) for cases where borrowers are in or facing arrears on their mortgage. This reflects that a key focus for non-lending firms is to take on and resolve non-performing loans.[6] Non-lending firms have been amongst the firms that have made the most progress in recent times in resolving LTMA. For example, when the impact of loan sales by retail banks is controlled for, banks and RCF/CSFs recorded a reduction in LTMA of around 3 and 14 per cent in 2021, respectively. Figure 1 shows the ARAs implemented by retail banks and RCF/CSFs over the three years to end-2022. As can be seen from the chart, RCF/CSFs utilised a higher proportion of permanent ARAs than retail banks over that period.

Figure 1 – ARAs Implemented 2020-2022 by Retail Banks and RCF/CSFs



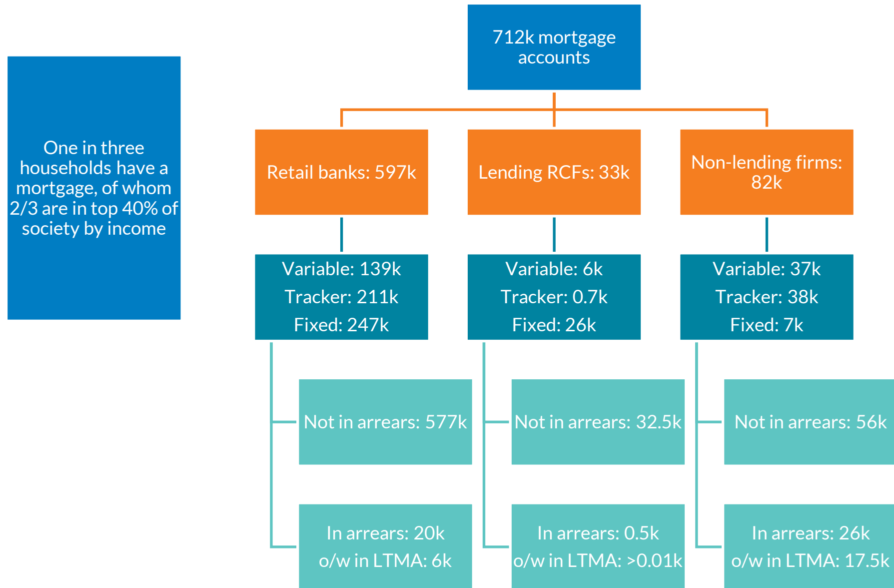
Source: Central Bank of Ireland Data, Mortgage Arrears and Repossession Statistics

As we commenced our work on foot of the November 2022 Dear CEO letter, retail banks held the vast majority of mortgage accounts

[6] That said, performing loans have also been transferred to non-lending firms. These could be loans that fell into arrears and were put on ARSs that were performing at the time of transfer. However, there are also loans transferred to non-lending firms that were always performing (e.g. when a lender was winding up their business in Ireland).

(597,000 at end-December 2022). The remainder were held by RCF/CSFs (around 115,000 mortgage accounts). Lending RCFs held around 33,000 accounts and non-lending firms around 82,000 accounts. Figure 2 illustrates the breakdown of the market as it stood at the end of December.

Figure 2 – The Mortgage Market in Ireland - December 2022



Source: Central Bank of Ireland Data, Mortgage Arrears and Repossession Statistics and internal calculations.

Among RCF/CSFs, 38 per cent of all PDH mortgage loans were on a variable rate at end-December 2022, 33 per cent on a tracker rate, and 29 per cent on a fixed rate. The weighted average interest rate for lending RCFs was 2.59 per cent at end-December, while a rate of 3.65 per cent was reported for non-lending firms. Comparable figures reported by retail banks was 2.93 per cent. Approximately 39 per cent of all mortgages were on a fixed rate. For non-lending firms this proportion was 9 per cent.

Table 1: Total PDH Mortgage Lending by RCF/CSFs as at end-December 2022

	Lending RCFs			Non-Lending Firms			Retail Banks
	Outstanding Amount (€000s)	Number of Accounts	Interest Rate (%)	Outstanding Amount (€000s)	Number of Accounts	Interest Rate (%)	Interest Rate (%)
Variable	880,052	6,322	3.59	5,118,007	37,138	4.74	3.50

Tracker	101,890	694	3.18	6,491,296	37,457	3.14	3.23
Fixed	6,181,122	26,257	2.43	739,833	7,391	0.53	2.69
Total	**7,163,064**	**33,273**	**2.59**	**12,349,136**	**81,986**	**3.65**	**2.93**

Source: Central Bank of Ireland Retail Interest Rates, January 2023.

The Central Bank's Approach

Our work on foot of the November 2022 Dear CEO Letter has been organised in phases. In Phase 1, we sought to gain assurance across the system that the regulatory framework is working in accordance with its terms across the topics of arrears, switching and interest rate increases. Having concluded this phase, we are now focused on Phase 2, to scrutinise more closely how the framework is delivering for consumers as we see rate increases begin to impact. Throughout this work the Central Bank has continued to engage with a wide range of stakeholders.[7]

Key actions in Phase 1

We have focused our Phase 1 work on three key areas:

(a) Arrears;
(b) Switching; and
(c) Interest Rate Increases.

Our approach has encompassed all borrowers whose loans are secured on their primary residence. This reflects that the impact of rising rates will be specific to an individual borrower's personal circumstances. It also reflects that interest rate increases will transmit differently depending on the specific terms and conditions of a mortgage and/or any alternative repayment arrangement in place.

For example, a borrower on a low rate (tracker) interest-only mortgage will have seen their monthly repayments increase at a greater rate than others, notwithstanding that their headline interest rate may still appear low relative to other rates in the market. This is because their monthly repayments are made up entirely of interest repayment, so an increase in interest rate affects them more than other borrowers. Similarly, the monthly repayment obligation of a borrower who is in the early years of their mortgage may be impacted

[7] This has included reviewing specific cases and scenarios put to us by consumer advocates and political representatives to ensure there was no breach of loan terms and conditions or regulatory requirements. We also met with stakeholders such as MABS, the Insolvency Service of Ireland and the BPFI on this topic, as well as engaging with the Department of Finance on an ongoing basis.

more heavily by an increase in their interest rate relative to a borrower on an equivalent product who is later in the term of their mortgage (where interest can form a smaller component of monthly repayments).

The work also included a focus on those borrowers who came into 2023 on a non-tracker variable rate of over 5 per cent with a non-lending firm, and who faced an increase in their mortgage rate. We included a focus on these consumers in our work due to the particular challenges they will now face as interest rates rise. At end-December there were approximately 18,000 such accounts. Of these 18,000, 6,500 had not made a repayment towards their mortgage in the last 90 days.[8]

Arrears

The Central Bank's sustained focus on all aspects of mortgage arrears continues. This includes to ensure firms' engagement approach and support for borrowers in, or facing, arrears is fit for purpose in the context of rising costs of living and interest rates. This has included firms putting appropriate early warning indicators in place and further enhancing the analysis of their borrower population. In Phase 2, we will be following up with firms to see that they use all the protections of the CCMA to the fullest extent (including with respect to pre-arrears cases). We continue to see that firms can do more to go deeper into their suite of options to support borrowers in or facing arrears.

From our Phase 1 work we would also highlight the following:

a) Firms should take a practical approach when considering the difficulties that may be faced by any borrower where the interest rate on their mortgage has increased, and of the supports those borrowers may need. This approach should be comprehensive of the scenarios where such an increase arises. Firms should be proactive in this regard, to the greatest extent possible, and not wait for financial distress to materialise before taking action to help these borrowers.
b) Where there are indications that the borrower's situation will deteriorate during the time needed for the borrower to complete, and the firm to assess, a Standard Financial Statement, firms should make effective use of Provision 38 ARAs as needed:
    i) Firms should have clear procedures for offering and putting in place temporary ARAs at the earliest necessary opportunity;

[8] Source: Data provided by firms.

ii) Firms should ensure that such ARAs are used for a limited period of time only, and not as a substitute for ensuring appropriate levels of resourcing to complete assessments of borrowers' individual circumstances in a timely manner; and

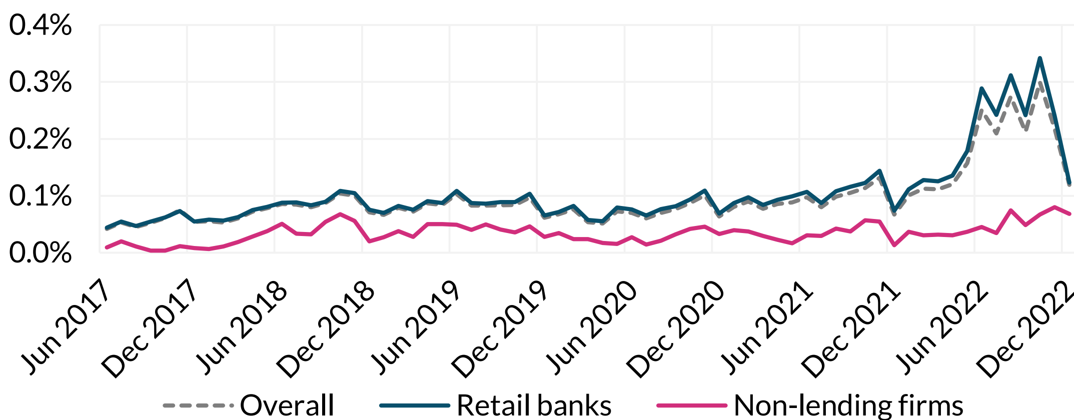
iii) Firms should explain to the borrower very clearly, and before the ARA is put in place, the terms of the ARA, including how it will be recorded on the Central Credit Register, and any cost of credit implications for the borrower.

Switching

The Central Bank scrutinised switching activity and the lending criteria of retail banks to ensure there is no discrimination based on who a borrower's current lender is (in particular considering the case of a borrower with a non-lending firm). This work identified no evidence to date of such discrimination. It also identified cases of borrowers from non-lending firms switching to banks, though the number of cases is small and specific to the individual circumstances of those borrowers. Figure 3 reports that this rate of switching away from mortgages at non-lending firms, while rising in 2022, has been consistently and substantially lower than switching rates away from mortgages at either retail banks or active non-bank lenders in recent years.

A key focus for our work in Phase 2 will be to see that those borrowers one should expect to be able to switch are supported to do so. We see that there is more capacity in the system for borrowers to switch than is being availed of, including in the case of borrowers at non-lending firms, while acknowledging credit criteria play a role in a borrower's ability to switch.

Figure 3 – Share of Contracts Switching Provider per Month, By Previous Provider



Source: Central Bank of Ireland calculations and Central Credit Register.

Notes: Estimated number of mortgage accounts switching away from different provider types each month, as a share of all mortgage accounts at that provider type. Estimates are based on output of an algorithm that identifies borrowers on the Central Credit Register who close one mortgage account and open another around the same time, while changing their mortgage provider. Excludes transfers initiated by providers, such as loan sales and transfers of engagements.

While our work on this topic is ongoing, we also highlight for firms the following expectations:

a) Given the demand for switching may increase, firms should remain vigilant to ensure they have sufficient operational capacity and resources in place to process switching applications within the timeframes set out in Provision 5.6a of the Consumer Protection Code.
b) Switching applications are assessed based on a prudent and consistently applied borrower creditworthiness and risk profile assessment, in line with the requirements of the European Union (Consumer Mortgage Credit Agreements) Regulations 2016 ('CMCAR') and the EBA Guidelines on Loan Origination and Monitoring. Firms should continue to apply these underwriting standards and ensure they do not discriminate against a borrower solely based on who their existing lender is, or has been in the past.
c) In providing advice to consumers interested in switching a mortgage, firms should be proactive in identifying any specific features where the consumer could make changes to their financial situation to either increase the likelihood of the current, or of a future, application being approved.
d) As required by Regulation 19(7) of the CMCAR, firms must inform the borrower without delay of the reasons for refusal of a mortgage credit application. In this context, firms should ensure the information provided is sufficient for the consumer to understand and identify what changes they may be able to make to their financial situation to increase the likelihood of a future switching application being approved.

Interest Rate Increases

Phase 1 included a preliminary review to ensure commercial decisions to raise interest rates are in accordance with the terms and conditions of the loans in question, the firm's published variable rate policy statements and the regulatory framework. It also included engagement with firms on their corporate governance around such commercial decisions including having regard to the expectations in our November 2022 letter and ECB and wholesale funding rates. The Central Bank's work will continue in this area, while recognising we do not have a statutory function to prescribe the rates firms charge or the products they provide.

We highlight to firms at this point in our work that:

a) Provision 6.6 of the Consumer Protection Code requires firms to provide specific information to borrowers when notifying them of a change in the interest rate on a loan. Firms should consider what additional information could be included in this letter that would be helpful for borrowers, and to ensure borrowers are fully aware of the supports available to them. At a minimum, this should include information on the options available to borrowers if they are having difficulty meeting the new repayment amount. In particular, information on MABS, the Insolvency Service of Ireland or any relevant State supports should be included in a prominent position.

b) Firms should consider whether a bespoke contact to specific borrowers is warranted over and above the Provision 6.6 letter notifying the borrower of the interest rate rise. Such contact would be with a view to reinforcing to borrowers that there are Alternative Repayment Arrangements available to support them if needed.

c) Firms should have additional supports available for borrowers who may be particularly affected by interest rate rises, such as those who are currently or were previously in financial difficulties, on an ARA, and/or who may encounter difficulties with switching to another lender. Firms should endeavour to identify these borrowers/groups of borrowers where possible, and have systems to track engagement and repayment profiles, in order to support borrowers as appropriate.

d) Information on the supports available to borrowers should be prominently displayed on the website of the firm.

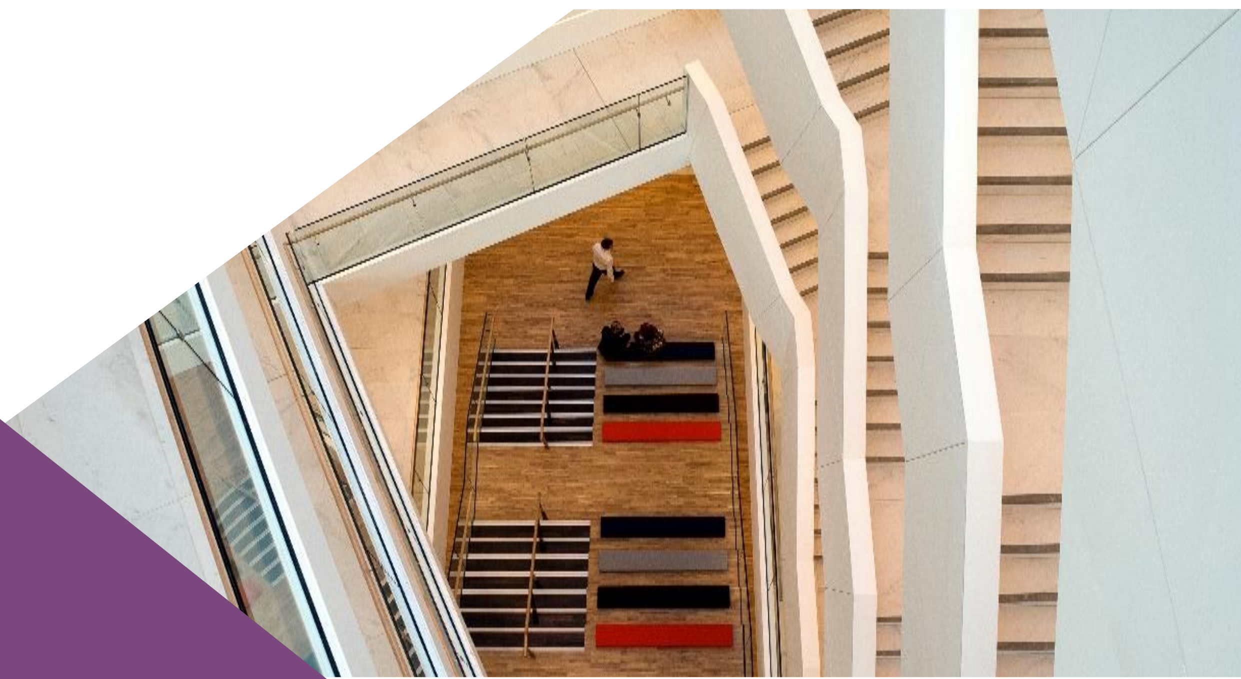
Next Steps

The Central Bank is taking a system wide approach to our ongoing work to support mortgage borrowers. This is done with a view to ensuring the outcomes delivered are consistent and fair for borrowers across the system, as well as having regard to the medium and long-term interests of consumers (including those looking to borrow now and in the future). It also recognises that borrowers across the financial system will face challenges in the face of rising costs of living and interest rates. The Central Bank is doing this work in close conjunction with our wider stakeholders and a full consideration of all the information and advocacy we receive (including specific cases or concerns that are raised with us).

Phase 1 of our work on foot of our Dear CEO Letter of November 2022 has established that, properly applied, the regulatory framework is well positioned to deliver for consumers in this context.

Having concluded Phase 1, the Central Bank is now focused on Phase 2, to scrutinise more closely how the framework is delivering for consumers as we see rate increases begin to impact. In particular, we will scrutinise the conduct of firms to ensure those borrowers who should expect to be able to switch product or provider are supported to do so. We will also continue our work to ensure borrowers facing financial difficulties are supported with alternative repayment arrangements, where appropriate, and that interest rate increases are in line with the terms and conditions of the loans concerned, published variable rate policy statements and the regulatory framework we are charged with supervising. This work will include a focus on lenders' approaches for customers who may require additional support from their lender due to rising interest rates.

Given the scale of the issues facing consumers, in addition to this ongoing engagement with individual firms, the Central Bank will arrange an industry engagement in the coming weeks to discuss more broadly how the system is responding to this challenge. This engagement will include a discussion of areas where consumers could be better supported through greater coordination amongst participants (e.g. in the area of switching) and where the information or options available to affected consumers could be enhanced.



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