Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

Tracker Mortgage Examination Progress Report – December 2017

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1. Executive Summary

A mortgage is the most significant financial commitment for most families and individuals. Consumers have a right to expect their lenders to treat them fairly. The Central Bank's role is to ensure that the best interests of consumers are protected in their dealings with financial firms. That is why, after pursuing tracker issues with a number of individual lenders through extensive supervisory and enforcement work, the Central Bank put in place a comprehensive framework for lenders and launched the industry-wide Examination. We did so because as issues were being detected in lenders, concerns were also being raised by individuals and consumer advocates, and we became more certain that those issues were potentially industry-wide.

As the largest, most complex and significant consumer protection review undertaken by the Central Bank to date, the Examination has exposed unacceptable failings by lenders on an industry-wide basis and a lack of a consumer-centred culture in lenders. These failings have had a detrimental and, in some cases, devastating impact on tracker mortgage customers, up to and including the loss of homes and properties. It is clear that all lenders did not sufficiently recognise or address the scale of those failings until intervention by the Central Bank. At every step of the way, we have been conscious of the hurt and damage the failings of lenders have caused for many customers, and the need for those customers to receive fair redress and compensation. Through the Examination Framework, the Central Bank is ensuring that lenders implement schemes to deliver appropriate redress and compensation to those affected. We are taking all possible actions to ensure lenders do the right thing.

As at mid-December 2017, following Central Bank challenge, c. 33,700 customers have been accepted by lenders as affected by tracker mortgage failings. This is an aggregate figure including both c. 26,600 affected customers accepted by lenders to date as part of the Examination as well as 7,100 tracker mortgage cases remedied following Central Bank intervention outside of the Examination. All redress and compensation schemes have been implemented with €297 million paid to customers to date. The redress and compensation paid is also an aggregate figure including both €250 million paid to mid-December and €47 million paid outside of the Examination.

Within these aggregate figures, the Central Bank can confirm that the five main lenders are on course to meet their October 2017 commitments, and that known issues around disputed groups in respect of lenders have now been resolved to the satisfaction of the Central Bank.

It is critical to stress that, in terms of consumer remedy, the Examination Framework has been designed in such a way as to ensure affected consumers have further options if they believe the redress and compensation offered by their lender is insufficient. In the first instance, lenders have been required to establish independent appeals panels, specifically to deal with customers who are not satisfied with any aspect of the redress and compensation offers that they receive from lenders. It is important to note that customers can accept the redress and compensation offered and still make an appeal – they can "cash the cheque" safe in the knowledge that what they have, they hold. Redress and compensation offers cannot be reduced in the event of a customer making an appeal.

Together with redress and compensation, affected customers will receive a separate payment which they can use to pay for independent advice regarding the adequacy of their lender's offer. Additionally, customers can refer to the Financial Services Ombudsman, who will deal independently with their concerns, or initiate proceedings in the courts.

Progress on the Examination

As at mid-December, following Central Bank challenge, lenders have included c.33,700 customers as affected by tracker mortgage failings. To date, €297 million has been paid in redress and compensation. This is broken down as follows:

1. 13,000 customers identified through the Examination to the end of September and who were the subject of lenders' October 2017 commitments. The Central Bank can confirm that 9,200 of these customers have been paid €170 million. The majority of the remaining customers can expect to receive redress and compensation by year-end.

2. A further 13,600 customers have been accepted by the lenders in their redress and compensation schemes since September. This has occurred as a result of the Central Bank's challenge of lenders. The Central Bank can confirm that 3,700 of these customers have been paid €80 million. The Central Bank will be vigilant in ensuring that payments to the remainder of these customers are progressed at pace.

3. This is in addition to 7,100 cases involving tracker mortgage issues which were remedied outside of the Examination. Redress and compensation of €47 million was provided by permanent tsb plc and Springboard Mortgages Limited.

While the Central Bank's view is that the vast majority of customers have been identified, we will continue to review, challenge and verify the work undertaken by the lenders and complete our intrusive on-site inspection programme.

Enforcement investigations are currently underway in respect of permanent tsb plc and Ulster Bank Ireland DAC. Further enforcement action at an additional lender has recently commenced. We expect that all of the main lenders will face enforcement investigations. In these investigations, the Central Bank will consider all possible angles, including potential individual culpability.

Unusually for a live supervisory examination, we have published regular updates on the Examination since its commencement in 2015, precisely because we realise affected customers need information. Nonetheless, the Central Bank, like any regulator, is limited by law in the amount of information we can publicly disclose about any financial institution that we regulate. Much of the pressure we exert on lenders in order to protect consumers must necessarily be done in private until outcomes are final and announced. Accordingly, we welcome the work of the

Minister for Finance and Public Expenditure & Reform and the Joint Oireachtas Committee on Finance, Public Expenditure & Reform, and Taoiseach, in further shining the public spotlight on those lenders involved in the Examination and adding to the sustained pressure we have exerted on the lenders since the commencement of the Examination.

The scale, range and complexity of the Examination, in addition to the material deficiencies in certain lenders' responses, has required robust and sustained Central Bank intervention. This has resulted in lenders significantly improving both their redress and compensation proposals and their independent appeals processes, to the benefit of affected customers. While this has meant that the Examination has taken longer than expected, the results are now becoming evident in terms of the numbers of people identified and the scale of redress and compensation being paid.

Engagement continues with all lenders to ensure all affected customers are identified and any emerging issues are addressed. On-site work will also assist in the gathering of evidence for enforcement investigations and informing potential additional actions that the Central Bank may take.

A further progress report will be submitted to the Minister on the basis of end-March 2018 data.

2. Introduction

This report is in response to a request from the Minister for Finance in his statement on the Tracker Mortgage Examination (the 'Examination') on 25 October 2017. The Minister requested that the Central Bank of Ireland (the 'Central Bank') prepare a report detailing whether the main lenders have made acceptable and sufficient progress in line with the commitments announced in their respective public statements on 25 October 2017. This report is also the latest in a series of updates provided by the Central Bank since it commenced the Examination[1].

To fulfil the Minister's request, Section 4 of this report will:

- detail the progress made by each of the five main lenders on redress and compensation since the Minister's engagement with these firms during October;[2] and
- provide an overview of progress made during that same period by the remaining six lenders that have redress and compensation schemes to implement.[3] [4]

The Central Bank is also providing an update in Section 4.2 of this report on its engagement with the lenders on disputed groups of customers.

3. Background

3.1 Scope of the Examination

Since 2010, the Central Bank has identified and pursued tracker mortgage related issues with lenders. Approximately 7,100 affected accounts were remedied outside of the Examination and redress and compensation of €47 million was provided by permanent tsb plc and Springboard Mortgages Limited. As new issues continued to emerge, the Central Bank decided that an industry-wide Examination was necessary, to interrogate whether all lenders were acting in their customers' best interests.

The Examination Framework (the 'Framework') requires lenders to conduct their Examinations in four phases:

- Phase 1: Development and Submission of Detailed Plan;

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[1] It is recommended that this report be read in conjunction with the Central Bank's October 2017 update and previous reports at https://www.centralbank.ie/consumer-hub/tracker-mortgage-examination

[2]
- AIB Group (Allied Irish Banks plc, AIB Mortgage Bank, EBS Limited, EBS Mortgage Bank and Haven Mortgages Limited)
- Bank of Ireland Group (The Governor and Company of the Bank of Ireland and Bank of Ireland Mortgage Bank)
- permanent tsb plc
- Ulster Bank Ireland DAC
- KBC Bank Ireland plc

[3] The remaining six lenders are:
- ACC Loan Management Limited
- Bank of Scotland plc
- Danske Bank
- IBRC
- Springboard Mortgages Limited
- Stepstone Mortgage Funding Limited

[4] 15 lending institutions were initially contacted as part of the Examination. Dilosk Limited, Leeds Building Society, Pepper Finance Corporation (Ireland) DAC and Start Mortgages Limited DAC are not covered in this report as they do not have affected customers and as a result redress and compensation schemes are not being implemented.

- Phase 2: Information Gathering/Review/Report Submission;
- Phase 3: Calculation of Redress and Compensation (where relevant); and
- Phase 4: Implementation of Redress Programme (where relevant).

The Examination is the largest, most complex and significant supervisory review that the Central Bank has undertaken to date in respect of its consumer protection mandate. The Examination involved an initial review of more than two million mortgage accounts by lenders to identify the number of in-scope accounts. Accounts in scope include all mortgage accounts from the date when the lender commenced offering tracker interest rate mortgages until 31 December 2015 in respect of both Private Dwelling Houses and Buy-to-Let properties:

(i) that originated on tracker interest rates;

(ii) that had tracker interest rates applied at any stage during the term of the underlying mortgage agreements; and/or

(iii) where the underlying mortgage agreements provided for contractual rights to or options for tracker interest rates at any stage during the term of the agreements.

3.2 Redress and Compensation

The Framework requires lenders to identify all affected customers and to address customer detriment in line with the Central Bank's Principles for Redress. These principles along with supplemental guidance clearly set out the Central Bank's expectations of the lenders to provide appropriate redress and compensation to affected customers when tracker mortgage related issues are identified. Key elements of the Central Bank's expectations in respect of redress and compensation for affected customers include:

(i) stopping further detriment to potentially affected customers;

(ii) redress to return customers to the position they would have been in but for the lenders' failures;

(iii) compensation to reflect the detriment suffered;

(iv) the establishment of an independent appeals process for affected customers;

(v) the provision of an independent advice payment for affected customers; and

(vi) guidance in respect of the manner in which lenders must communicate with affected customers.

Lenders' initial redress and compensation proposals fell short of the Central Bank's expectations to varying degrees. The material deficiencies in their proposals necessitated the Central Bank to challenge them repeatedly. This has resulted in lenders significantly improving both their redress and compensation proposals and their independent appeals processes, to the benefit of affected customers.

4. Update on progress made by the five main lenders

Under the Examination, data submitted by lenders is subject to review by the Central Bank. The following section details numbers reported as verified by the lenders to date and remaining numbers that will be verified by the lenders in due course.

4.1 Customers included up to 30 September 2017

Approximately 13,000 affected customers had been identified by lenders in their Phase 2 reports to end-September 2017. As at mid-December 2017, 9,200 of these customers have received redress and compensation to the value of €170 million. The majority of outstanding customers can expect to receive redress and compensation by year-end.

In their October 2017 statements, the five main lenders committed to certain schedules for payment of redress and compensation to customers drawn largely from this group and they are on course to meet these commitments.

4.2 Customers included since 30 September 2017

In October 2017, the Central Bank made clear that it had concerns that certain lenders had failed to identify groups of affected customers or failed to recognise that certain groups of customers had been affected by their failures – 'disputed groups'. Through a series of intensive engagements, intrusive supervision and challenge of senior board members, the Central Bank communicated these concerns to the relevant lenders prompting them to include an additional c. 13,600[5] customers as affected under the Examination. Of these, the Central Bank can confirm that 3,700 have already been paid €80 million.

The Central Bank will be vigilant in ensuring that payments to these customers are progressed at pace.

5. Progress update on remaining six lenders

In addition to work ongoing with the five main lenders, the Central Bank continues to engage with six other lenders who have identified c. 300 affected customers to date, and who were required to implement redress and compensation schemes. As at the date of publication of this report, five lenders have commenced payment of redress and compensation. Four of the five lenders' redress and compensation schemes are expected to be completed before year-end. The fifth is expected to have completed payment by end-January.

Through the financial arrangements around the liquidation, the sixth lender, IBRC will not be implementing a redress and compensation scheme in line with the Central Bank's Principles for Redress. The liquidator of IBRC has automatically admitted affected customers as unsecured creditors in the liquidation. Therefore, affected customers will not need to take any action.

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[5] The 13,600 is comprised of (i) 5,800 customers who have been formally reported as verified by lenders and included for redress and compensation; and (ii) an estimated 7,800 customers to be verified by lenders for inclusion in redress and compensation

6. Additional Data and Case Studies

While the range, complexity and variance of cases within the Examination is significant, for illustrative purposes, it is possible to break down affected customers of the five main lenders into two main categories:

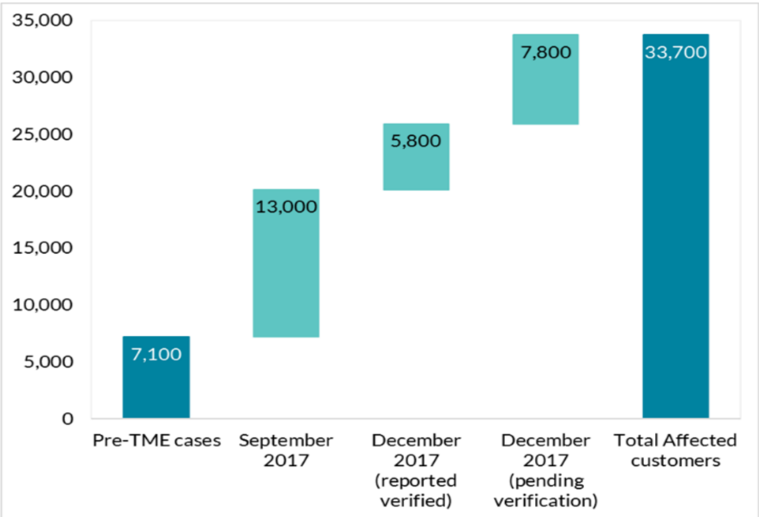
- affected customers who have lost a contractual right to or were not afforded an option of a tracker interest rate at any stage during the term of their agreements ('incorrect product'); and
- affected customers who were on an incorrect tracker margin rate[6] ('incorrect margin').

Figure 1: Breakdown of affected customers by wrong product and incorrect tracker margin

Customers who were on an incorrect product will in most cases receive more in redress and compensation than those on an incorrect margin rate because the rate differential is more significant. Customers in both categories will be returned to the correct rate of interest.

Figure 2 shows the progress made with respect to the identification of affected customers over the Examination period.

Figure 2: Customers identified as included in the Examination since commencement



6 Incorrect tracker margin rates have been identified as part of the Examination. Some customers were charged a higher tracker margin rate by their lender and are included in the lenders' redress and compensation schemes. Others were charged a lower tracker margin rate by their lender. In these latter instances, lenders are not adjusting the individual's rate of interest, as it would negatively affect the customer.

Examples of how customers have been affected

These examples serve to demonstrate the nuances of individual cases and are intended to be illustrative only. Whether a customer has been affected depends on the precise circumstances of their individual situation.

Background

For the purposes of the examples referenced below, the following statement applies: during the period between June 2005 and July 2008, the European Central Bank's interest rate increased incrementally from 2% to 4.25%. These increases in rates resulted in increases to tracker mortgage holders' repayments.

Example 1 - Contractual Issue Resulting in Loss of Tracker Product ('wrong product')

In 2003, Mary drew down a mortgage with a tracker rate of interest. In 2006, Mary, like many others, chose to fix her interest rate initially for one year. At the end of that year, Mary chose to fix her interest rate for a further two years. The loan documentation originally signed by Mary entitled her to return to a tracker interest rate at the end of every fixed rate period entered into during the term of the mortgage. However, at the end of the second fixed rate period, the lender failed to offer Mary the tracker rate. Instead, she was charged the standard variable rate that is higher than the tracker rate. Mary has now been put on the correct tracker rate of interest and has received appropriate redress and compensation.

Example 2 - Transparency Issue Resulting in Loss of Tracker Product ('wrong product')

Tom drew down a mortgage on a tracker interest rate in 2003. He subsequently moved to a fixed interest rate in 2006 for a three-year period. At the end of the three years, the mortgage rolled to a standard variable rate of interest, which was not a tracker rate. The documentation provided to Tom in advance of switching to a fixed interest rate was not clear with respect to the rate of interest to be applied to the mortgage account at the end of the fixed interest rate period and created an expectation that he would revert to the tracker rate. The lender placed Tom on the standard variable rate of interest rather than the tracker rate at the end of the fixed rate period. Tom has now been put on the correct tracker rate of interest and has received appropriate redress and compensation.

Example 3 - Other Communications Customers may have Considered Resulting in an Expectation of a Right to, or Option of, a Tracker Product

Ann drew down a mortgage on a tracker interest rate in 2003. The lender's marketing and/or sales material conveyed the right to, or the option of, a tracker rate of interest on expiry of a fixed interest rate period. Ann decided to move to a fixed rate for a period of two years. The information contained in the documentation signed by Ann when moving to the fixed rate did not provide for the right or option of a tracker rate of interest on expiry of the fixed interest rate period. As a result, a tracker interest rate was not provided to Ann at the end of the two-year period. Ann has now been put on the correct tracker rate of interest and has received appropriate redress and compensation.

Example 4 - Margin Issue Resulting in Wrong Margin applying to the Tracker Mortgage

In 2006, Pat received in-principle approval for a tracker mortgage with an interest margin of 0.5% on top of the ECB rate. One month later Pat drew down the mortgage and the tracker margin applied to his account at this time was 0.6%. It was not clear that the tracker margin referenced at the point of approval might differ from the margin rate to be applied when the mortgage documentation was signed. This rate change was not disclosed to Pat and he proceeded to pay the higher tracker interest rate. Pat has now been put back on the correct tracker margin rate and has received appropriate redress and compensation.

7. Independent Advice and Appeals Process

The Central Bank deliberately structured the Framework to ensure that affected customers have further recourse options if they are dissatisfied with any aspect of the redress and compensation offers made by their lender. First, under the Framework, affected customers receive an additional payment at the point of offer of redress and compensation from the lender, which allows them to take independent legal or other professional advice regarding the redress and compensation offers made to them. Second, an independent appeals process must be established by lenders to deal with customers who are dissatisfied with any aspect of the redress and compensation offer they receive from lenders.

Importantly, customers can accept their offer for redress and compensation while still making an appeal. Appeals panels cannot make a less favourable finding than any offer made to affected customers pursuant to the lenders' redress and compensation schemes. Customers can "cash the cheque" safe in the knowledge that what they have, they hold. This ensures that a customer's need to receive payment upfront is not a determining factor in deciding whether to appeal an offer. Further, lenders are to reimburse affected customers for their reasonable costs incurred in bringing appeals, in the event that they are successful in part or in whole of their appeals.

Appeals form an important part of the overall Examination process as they ensure an independent and transparent consideration of complaints from customers about any aspect of the redress and/or compensation they have been offered. In particular, customers who have suffered severe detriment, such as home loss, and feel that their personal circumstances have not been sufficiently taken into account, may wish to bring that information forward for consideration by the appeals panel. Panels must include appropriately qualified professionals and be comprised of an independent majority including an independent chairperson. All panels must include a consumer voice representative.

The Central Bank also expects that lenders will not raise any time limit defences that may otherwise apply provided the affected customers make complaints to the Financial Services Ombudsman ('the FSO') or initiate proceedings before the courts within a specified period of time. Where a customer appeals and remains dissatisfied with the outcome of the appeal, they also retain the option to bring a complaint to the FSO and/or to initiate court proceedings within a specified period of time.

8. Consumer Protection Framework in Ireland

The recourse options of the Examination seek to utilise in full the State's consumer protection framework in favour of affected customers. A number of agencies form part of that framework and are charged with the protection of customers of financial products. The mandates of these agencies vary from stand-alone consumer protection focused (e.g. Financial Services Ombudsman, Competition and Consumer Protection Commission) to the Central Bank which has a dual prudential regulation and consumer protection mandate. The Central Bank is working closely with these agencies.

The mission of the Central Bank is safeguarding stability and protecting consumers. The Central Bank's consumer protection mandate is focused on system-wide consumer protection issues rather than handling individual complaints. The Examination was initiated to address, to the greatest extent possible, a system-wide problem that arose in respect of tracker mortgages.

The FSO assesses the complaints of individual consumers against their financial services providers and can direct redress where the office finds against a firm. The FSO presents customers with a means of resolving their complaint in an independent, fair and transparent manner, which takes account of their unique personal circumstances. In the context of this Examination, the FSO has and continues to deal with individual consumer complaints where customers are not satisfied with their redress and compensation from lenders under the Framework or where they believe that they have been wrongly excluded from the Examination. The FSO has the power to direct both compensation and rectification, as appropriate.

9. Next Steps

9.1 Continued Supervisory Engagement

While the Central Bank's view is that the vast majority of customers have been identified, we will continue to review, challenge and verify the work undertaken by the lenders and complete our intrusive inspection programme. This work is to ensure that all affected customers are identified, all Framework requirements including stopping the harm have been met and that any emerging issues are addressed. On-site work will also assist in the gathering of evidence for enforcement investigations and informing potential additional actions that the Central Bank may take.

9.2 Regulatory Enforcement Actions

The Central Bank has utilised its enforcement powers and continues to pursue enforcement investigations actions in response to tracker mortgage issues that have been identified at certain lenders. It is expected that all of the main lenders will face enforcement investigations. Investigations are currently underway in respect of permanent tsb plc and Ulster Bank Ireland DAC. A further enforcement action with respect to an additional lender has recently commenced.

Enforcement measures will be deployed as appropriate, including investigating issues and taking cases under the Central Bank's Administrative Sanctions Procedure together with the use of our fitness and probity powers. In the enforcement investigations, the Central Bank will consider all possible angles, including potential individual culpability, and will thoroughly investigate and analyse these matters in the context of the legal framework.

Enforcement investigations are detailed and forensic, and routinely involve the scrutiny of thousands of documents and the conduct of interviews as part of the investigative process, to establish the exact circumstances of matters under investigation, including the culpability of regulated entities and individuals.

9.3 Investigating Lender Behaviour and Culture

The Central Bank's Consumer Protection Code requires that lenders act in the best interests of their customers. While many lenders publicly state that they put customers first, the evidence from the Examination firmly suggests otherwise. Accordingly, the Central Bank concurs with the Minister for Finance that significant behavioural and cultural issues and challenges in some of the lenders still appear to exist and that customer interests have not been sufficiently protected or prioritised.

The Minister has mandated the Central Bank to report on:

- The current cultures and behaviours in the retail banks today; and
- The risks associated with these cultures and behaviours.

Behaviour and Culture inspections will be undertaken at each of the five main lenders involved in the Examination. They will take account of elements of the Central Bank's Consumer Protection Risk Assessment framework. A detailed scoping exercise is currently being undertaken by the Central Bank and the inspections are expected to commence in January 2018.

A report to the Minister will be made in June 2018.

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