

Mortgage Arrears and Personal Debt Group

Final Report
16th November 2010

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Foreword

This Report is presented at a challenging time for Ireland. We recognise at the outset the distress of many mortgage holders and over-indebted consumers. Our work over the past nine months has been focussed on developing proposals which will improve their situation and help alleviate their distress. We have been conscious that any proposals which we examined or developed required assessment across a broad set of policy considerations, taking into account the latest available data. We are confident that our recommendations represent a balanced and measured set of proposals which will improve the situation for those in mortgage and personal debt difficulties and simultaneously best serve the national interest.

The Group has engaged in a consultation process which included a large number of submissions and presentations. The Group would like to thank all those who have contributed to our consultation process. We have taken into account the information and reflections which we have received in our consideration of all of the issues.

As Chairman, I also wish to thank all of the members of the Group for their commitment and professionalism since we first met in February 2010. Like any large group, we have different views and perspectives. It is to the members' credit that they remained focussed on delivering a balanced and measured set of recommendations, based on the Group's collective deliberations.

Hugh Cooney
Chairperson of
the Mortgage Arrears and Personal Debt Group

Chapter 1: Executive Summary

The Expert Group on Mortgage Arrears and Personal Debt was established by the Government in February 2010 and was tasked with making recommendations to the Minister for Finance on options for improving the current situation for families with mortgage arrears on their principal private residence and with personal debt.

The Group published an Interim Report in July 2010 and its recommendations were accepted by the Government. These recommendations have formed a very important part of the overall work of the Group. Many of these recommendations are currently being implemented. This includes publication by the Central Bank of a consultation paper to amend the statutory Code of Conduct on Mortgage Arrears (CCMA).

In the final phase of its work, the Group focussed on the three key areas of advanced forbearance, social housing and personal debt. The Group actively sought the views of practitioners in these areas to add to its understanding of both complex technical matters and general issues of policy.

The Group reviewed international practices in regard to all of the main issues which it considered. A critical part of the Group's work was to evaluate the potential applicability of solutions, which are in operation elsewhere, to an Irish context.

This Report is based on the current level of information available. However, the Group is conscious of the range of factors which may impact on future developments in the economy. Accordingly, we suggest that arrangements be made for ongoing monitoring of the situation to ensure that policy responses continue to be relevant and appropriate.

Key Findings

The key findings are set out below and described more fully in the main body of the report.

- Mortgage arrears data from the Central Bank at the end of June 2010 show that 36,438 residential mortgage accounts, representing 4.6% of the total number of accounts, are in arrears for over 90 days. This compares with 3.3% at the end of September 2009.
- The Group concluded that arrears levels will persist for some time and may get worse before they get better. Forthcoming data from the Central Bank is expected to show that 5% of all mortgage accounts are in arrears for over 90 days. This has informed the Group's thinking in relation to proposals for advanced forbearance.
- The Central Bank, as an input into the work of the Group, conducted a survey of lenders in regard to the level and type of loan rescheduling. It is estimated from the survey that the number of rescheduled mortgage accounts is up to 45,000. There is an overlap of 20- 25% between rescheduled mortgages and arrears cases, giving an estimated total of 70,000 who are either in arrears or have rescheduled.

- The Group estimates, based on the Central Bank's quarterly data on mortgage arrears and the lenders survey, that around 90% of mortgage accounts are being repaid in accordance with the contract. Two thirds of rescheduled mortgage accounts are paying at least full interest.
- The Group notes that repossession levels in Ireland remain substantially lower than those experienced in the UK and found that lender forbearance is working and is having a beneficial impact.
- The Group notes that the Exchequer is already providing significant assistance through the Mortgage Interest Supplement (MIS) scheme to borrowers on low incomes who are in difficulty. The Group notes that, at present, MIS assists almost 17,800 borrowers.
- The Group, during the period of its research, could not identify any arrangements internationally that could be characterised as mortgage debt forgiveness schemes, with the exception of parts of the US where non-recourse mortgage lending applies.
- The Group noted that Mortgage to Rent Schemes operating in the UK are based on very different funding models than that which would pertain in Ireland. The Group also noted that lenders who participated in leasing type arrangements with local authorities, in respect of properties held under unsustainable mortgages, would face adverse capital implications.
- The Group noted that the development of personal insolvency law in many jurisdictions would indicate that Ireland requires reform in this area as a matter of urgency.
- The Group recognises that in the event of a sale of a home, a mortgage shortfall debt, where such arises, becomes an unsecured personal debt still owed to the mortgage lender. In all judicial and quasi judicial proceedings such debt is treated on an equal basis with all other forms of unsecured debt.

Key Recommendations from the first phase of the Group's work

In July 2010, the Group made 41 recommendations – see Chapter 2 for a full list of recommendations from both phases of the Group's work. The following are among the key recommendations from the Interim Report:

- All lenders must develop a Mortgage Arrears Resolution Process (MARP) to provide a framework for handling arrears and pre-arrears cases.
- Lenders must not apply penalty interest or arrears charges to borrowers who are taking part in the MARP.
- A Standard Financial Statement (SFS) should be developed for use by all lenders and MABS. This should be used to assess a borrower's financial position and to identify a best course of action.
- Lenders must not require the borrower to give up their low cost tracker or other existing product if to do so would put the borrower at a financial disadvantage.

- All lenders must establish a centralised and dedicated Arrears Support Unit (ASU) to manage pre-arrears under the MARP.
- The complaints handling procedures of the Consumer Protection Code should apply to the CCMA including the decisions of the ASU relating to the application of the lender's MARP.
- The Department of Social Protection should introduce an alternative and more equitable approach to achieving the Mortgage Interest Supplement (MIS) objectives and maintaining its sustainability in light of changes in the economic climate and the mortgage market.
- Consideration should be given to the effective implementation, in the shortest possible timeframe, of measures for the comprehensive reform of both judicial bankruptcy proceedings and the establishment of a non-judicial debt settlement process.
- A more comprehensive system of credit reporting should be put in place. The Group welcomed the Financial Regulator's announcement of a review of credit reporting arrangements in Ireland.

Key Recommendations from the final phase of the Group's work

Debt Forgiveness

- We do not recommend a formal debt forgiveness scheme having regard to the broad range of policy considerations which are outlined in the main body of the report.

Advanced Forbearance

- All mortgage lenders will be requested to commit to the proposed Deferred Interest Scheme (DIS) or an equivalent scheme. Lenders representing the majority of the market have already indicated their willingness to implement this or an equivalent scheme and the remaining lenders will be requested to do so.
- The DIS should enable borrowers who can pay at least 66% of their mortgage interest (but less than the full interest) to defer payment of the unpaid interest for up to 5 years.
- When the accumulated amount in the deferred interest account is equal to a total of 18 months interest, or when the borrower has participated in the DIS for up to 5 years, the mortgage may be deemed to be unsustainable.

Social Housing

- The Department of the Environment, Heritage and Local Government should swiftly implement new regulations (currently being developed) which will enable borrowers whose mortgage has been deemed unsustainable, to become eligible for social housing assessment before a repossession order has been made or repossession has actually taken place.
- The Group recommends that a mechanism be put in place which would enable, where appropriate, the borrower and lender agree to a voluntary repossession, with actual repossession deferred for a specified maximum period or until such time as the housing authority has sourced appropriate accommodation, whichever comes sooner.

- The Group recommends that an Exchequer funded mortgage to rent scheme should not be introduced given the current budgetary and fiscal environment and existing waiting list for social housing. However, should these constraints ease, it may be appropriate to reconsider a mortgage to rent scheme.

Personal Debt

- That reform of Ireland’s personal insolvency regime should consist of two main parts:
 - (i) new and modernised bankruptcy legislation with a less punitive approach; and
 - (ii) a non-judicial debt settlement and enforcement system which would be an alternative to bankruptcy in most cases.
- That the time period for discharge of the debt under a non-judicial debt settlement mechanism should vary according to the quantum of the debt, with a large quantum of debt having a longer discharge period than a smaller one.

Trade Down¹

- The Group notes that, for some mortgage holders who are in negative equity, trading down would produce a reduction in mortgage debt and more affordable monthly payments. The Group recommends that further consideration should be given by lenders to facilitating trading down by borrowers in this situation. Such options would have to meet relevant prudential standards, with appropriate controls in place, and be in the customers’ best interest.

Assisted Sales and Cost of Sale

- The Group recognises that an early assisted sale may have advantages over a formal repossession in the case of an unsustainable mortgage. We recommend that lenders develop a protocol setting out their practices, procedures and charges in this area.

Monitoring and Reviews

- Having regard to the fact that the MARP and the DIS represents a new approach designed to address a specific problem, the Group believes that all its main constituent parts will require close monitoring from their commencement. It recommends that the MARP, the DIS and the Appeals Process be formally reviewed within 18 months of commencement.

Structure of Report

Chapter 2 combines the recommendations of the Interim Report and the Final Report in one complete list.

Chapter 3 provides a statistical analysis of the mortgage debt problem. This highlights the extent to which lenders are offering forbearance but also identifies borrowers for whom standard forms of forbearance may be insufficient beyond a short term horizon.

¹ Trading Down occurs when a mortgage-holder sells their property and buys a property of lower value.

The Group sets out its views on the key concept of a sustainable mortgage. Chapter 3 also outlines a number of issues which the Group considers worthy of future consideration by relevant authorities.

Chapter 4 sets out the Group's analysis of the options for applying more advanced forms of forbearance in the Irish market. In coming forward with proposals designed to help mortgage holders in difficulty, the Group is also conscious of its responsibility to evaluate the likely impact of any such proposals on the taxpayer, the broad spectrum of mortgage holders and lending institutions. The Group sets out the broad policy considerations which shape its proposals.

The Group is proposing that lenders extend present levels of forbearance to those mortgage holders who can make substantial part payments on the interest portion of their mortgage ('Deferred Interest Scheme' or DIS).

Chapter 5 focuses on households whose mortgage is deemed to be unsustainable and who may be eligible for social housing. The Group considered a number of options, including voluntary repossession with a lender then leasing the repossessed property to a housing authority, an Exchequer funded mortgage to rent scheme and the use of private equity funds.

In Chapter 6, the Group sets out its consideration of the personal debt issue. The Group recognises that the issue of the reform and modernisation of the personal insolvency system is now urgent and sees the reform as consisting of two main parts: (1) the replacement of the Bankruptcy Act 1988 with new and modernised bankruptcy legislation with a less punitive approach and (2) a statutory non-judicial debt settlement and enforcement system.

Chapter 2: Complete List of Recommendations

2.1 Introduction

- 2.1.1 The following is a full list of the Group's Recommendations combining the recommendations in the Interim Report with those of this Final Report.

2.2 Interim Report Recommendations

Mortgage Arrears Charges and Penalty Interest

1. Lenders must not apply penalty interest or arrears charges to borrowers who are taking part in the Mortgage Arrears Resolution Process (MARP).

Code of Conduct on Mortgage Arrears (CCMA)

2. The CCMA should be admissible in legal proceedings.
3. The one-year moratorium on legal action in the CCMA should not be extended.
4. The CCMA, when amended, should apply to Credit Unions. The Department of Environment, Heritage and Local Government should update the recent guidance provided to housing authorities based on the existing CCMA to fully reflect the amended CCMA.

The CCMA should be amended to:

5. Facilitate the implementation of a standard industry-wide MARP (see recommendations 22 to 34).
6. Require that lenders do not encourage borrowers to change mortgage products, such as low cost trackers, if it would put the borrowers at a financial disadvantage and must not use forbearance measures or the MARP to transfer borrowers to less favourable terms.
7. Require increased and improved communication with borrowers (see recommendations 10 to 21).
8. Provide specific instructions on how, when and what to communicate to the borrower.
9. Apply as soon as a borrower first contacts a lender concerning possible repayment difficulties (pre-arrears cases).

Communication

10. Borrowers are encouraged to contact their lender at an early stage before an arrears problem develops.
11. All stakeholders working with borrowers in arrears or pre-arrears should agree a common high-level message in their communication.
12. The Citizen's Information Bureau / Money Advice Budgeting Services website (www.keepingyourhome.ie) must be the main information portal for all communication with borrowers and with links to and from other sites.
13. All lenders must have a dedicated section of their website for borrowers in financial difficulty.
14. All 'at risk' mortgage holders must receive a periodic mailing from their lender concerning options for dealing with financial distress, encouraging early action by borrowers etc.
15. Lenders must be required to inform borrowers of the implications of loan

- rescheduling or modification for their credit record.
16. Lenders must be required to publish all their current loan rates on their website.
 17. Lenders must be required to publish all approved charges which they are applying to arrears for those who are not co-operating with the MARP.
 18. Lenders must be required to provide information about State supports to borrowers in distress and provide assistance in applying for such supports in the MARP.
 19. Lenders must ensure that written communication with borrowers does not discourage engagement with the lender. Standards must be considered in this area under the CCMA.
 20. Lenders must prepare an information booklet explaining their MARP (see below).
 21. The Financial Regulator and National Consumer Agency should prepare an information booklet explaining the CCMA.

Mortgage Arrears Resolution Process (MARP)

22. All lenders must develop a MARP to provide a framework for handling arrears and pre-arrears cases. They should publish the MARP procedures.
23. All lenders must publish the types of forbearance that are available under MARP and the guidelines they are employing for decision making on which approach is appropriate for typical sets of financial circumstances.
24. Under the MARP, lenders must agree appropriate forbearance with each borrower following an assessment of the full circumstances and characteristics of each borrower. However, where it is concluded that the mortgage is unsustainable then forbearance is unlikely to be appropriate and voluntary surrender may be necessary.
25. The CCMA 12 month protection from legal action should not apply to borrowers who refuse to co-operate with the MARP.
26. A Standard Financial Statement (SFS – Appendix C) should be developed for use by all lenders and MABS. This should be used to assess a borrower's financial position and to identify a best course of action.
27. Borrowers, lenders and State bodies should take the necessary steps to ensure that all appropriate documentation to corroborate the SFS is made available.
28. MARP agreements and the SFS information must be subject to periodic review by the lender and the borrower.
29. All lenders must establish a centralised and dedicated Arrears Support Unit (ASU) to manage pre-arrears and arrears cases under the MARP.
30. ASUs must maintain appropriate contacts with MABS and the Departments of Social Protection and Environment, Heritage and Local Government to ensure effective communication on arrears and pre-arrears cases.
31. Lenders must provide training and issue regular internal communication to front line staff on how to deal with borrowers in financial difficulty.
32. Lenders must proactively carry out regular assessments of existing customers to identify those experiencing or likely to be at risk of financial distress in order to target communication efforts to offer assistance and encourage participation in the MARP.
33. Lenders must put in place management information on case handling under the MARP and report to the Financial Regulator on a quarterly basis.

34. The complaints handling procedures of the Consumer Protection Code should apply to the CCMA including the decisions of the ASU relating to the application of the lender's MARP.

Credit Reporting

35. The Irish Credit Bureau should expand its database for its members to include all loans including personal guarantees.
36. The Group welcomes the Financial Regulator's announcement of a review of credit reporting arrangements in Ireland, including the proposal for compulsory reporting by all lenders.

Data

37. The Financial Regulator should amend its quarterly public report on mortgage arrears to record, amongst other things, the number of mortgages that have been rescheduled.

Mortgage Interest Supplement (MIS)

38. The Department of Social Protection should introduce an alternative and more equitable approach to achieving the MIS objectives and maintaining its sustainability in light of changes in the economic climate and the mortgage market. This should cover issues such as:
- No legal action should be taken by the lender while MIS is being paid and the borrower is cooperating with the lender.
 - The ban on paying MIS to a couple where one person is in full-time employment should be removed and a revised means test developed.
 - The current rule which excludes the payment of MIS when a house is for sale should be suspended.
 - The State should not provide MIS where the lender is charging interest above the market rate.
 - MIS should only be payable where no capital is being repaid.
 - MIS should be paid directly into the mortgage account of the borrower.
 - Lenders should agree forbearance options with borrowers for a period of six months and ensure the SFS is completed before the State shares the responsibility by providing MIS support to the borrower.
 - An overall time limit for MIS should be considered to ensure that the scheme does not act as a disincentive to seeking or retaining work.
 - The scheme should remain as a short term income support.
 - Where a borrower's situation is or becomes unsustainable, they should be facilitated, if necessary, in applying for social housing appropriate to their needs.

Recommendations on Money Advice and Budgeting Service (MABS)

39. The recommendations from the ongoing review of the demand for MABS services should be considered for implementation as soon as possible.

Personal Debt

40. Urgent consideration should be given to the effective implementation, in the shortest possible timeframe, of measures for the comprehensive reform of both judicial bankruptcy proceedings and the establishment of a non-judicial debt settlement process.

41. In this context the recommendations to be contained in the Final Report of the Law Reform Commission on Personal Debt Management and Enforcement, expected later this year, will be crucial to the reform process.

2.3 Final Report Recommendations

Debt Forgiveness

42. We do not recommend a formal debt forgiveness scheme having regard to the broad range of policy considerations which are outlined in the main body of the report.

Deferred Interest Scheme

43. A deferred interest scheme should be put in place so that borrowers who can pay at least 66% of their mortgage interest (but less than 100%) can defer payment of the balance for up to 5 years.
44. When the accumulated amount in the deferred interest account is equal to a total of 18 months interest, or when the borrower has participated in the DIS for up to 5 years, the mortgage may be deemed to be unsustainable.
45. All mortgage lenders will be requested to commit to the proposed DIS or an equivalent scheme. Lenders representing the majority of the market have already indicated their willingness to implement this or an equivalent scheme and the remaining lenders will be requested to do so.
46. The Group recommends that the lender has recourse to any accumulated deferred interest in the event of a mortgage shortfall arising.

Mortgage Interest Supplement (including interaction with DIS)

47. The Group recommends that the Department of Social Protection, in its development of the qualification criteria for the revised MIS scheme, should consider how a gradually reducing rate of assistance may apply in certain cases, following a timebound period.

Trade Down

48. The Group notes that, for some mortgage holders who are in negative equity, trading down could produce a reduction in mortgage debt and more affordable monthly payments. The Group recommends that further consideration should be given by lenders to facilitating trading down by borrowers in this situation. Such options would have to meet relevant prudential standards, with appropriate controls in place, and be in the customers' best interest.

Assisted Sales and Cost of Sale

49. The Group recognises that an early assisted sale may have advantages over a formal repossession in the case of an unsustainable mortgage. The Group recommends that lenders develop a protocol setting out their practices, procedures and charges in this area.

Access to Social Housing Support

50. The Group recommends that lenders and the local authorities should communicate at an early stage in relation to unsustainable cases.

51. The Group recommends that the Department of the Environment, Heritage and Local Government should swiftly implement new regulations (currently being developed) which will enable borrowers whose mortgage has been deemed unsustainable, to become eligible for social housing assessment.

Mortgage to Rent

52. The Group recommends that an Exchequer funded mortgage to rent scheme should not be introduced given the current budgetary and fiscal environment and existing waiting list for social housing. However, should these constraints ease, it may be appropriate to reconsider a mortgage to rent scheme.

Tenancy at Will Arrangements²

53. The Group recommends that a mechanism be put in place which would enable, where appropriate, the borrower and lender agree to a voluntary repossession, with *actual* repossession deferred for a specified maximum period, or until such time as the housing authority has sourced appropriate accommodation whichever comes sooner. The Group recommends that mortgage lenders and the Department of the Environment, Heritage and Local Government work together to put in place such a mechanism early in the New Year.

General Considerations and Features of a Debt Settlement System

54. The Group recommends that the relevant Departments and Agencies concerned bear in mind the following considerations in regard to developing new debt settlement systems, both judicial (bankruptcy) and non-judicial:

- (i) General considerations
 - appropriate qualification criteria for entry to a non-judicial debt settlement system;
 - affordability (in regard to costs, fees, taxes, etc), accessibility and ease of understanding;
 - the time limits and conditions that might apply to discharge from a bankruptcy or insolvency process;
 - how an "earned fresh start" and an appropriate future credit rating can be achieved for the debtor who has made all efforts in good faith to comply with the terms of the debt settlement agreement;
 - the protection of the property rights of creditors;
 - the ending of any system of preferential payments to certain creditors, Revenue or otherwise;
 - the restrictions that might apply to the person in an insolvency process in regard to engaging in business, obtaining credit or being elected to public office, etc;

² The envisaged type of tenancy at will arrangement will allow the former owner to remain in the home, as a tenant, for a limited period.

- ⊖ the development of effective and transparent enforcement mechanisms; and
 - ⊖ avoidance of inappropriate incentives for potential misuse of new insolvency arrangements.
- (ii) Specific considerations
- that at least 60% of creditors by value, vote in favour of the scheme;
 - the debt discharge period in a formal debt settlement system should be related to the quantum of debt outstanding; and
 - where a debtor subject to a debt settlement arrangement refuses to abide by the agreement, creditors have the right to pursue other legal remedies, including an application to the court either to have the debt enforced or the debtor declared bankrupt.

Mortgage Shortfall and Debt Settlement

55. The Group recommends that Government consider carefully the maximum discharge periods for different levels of total indebtedness, having regard to the factors outlined below.

The time period for discharge of the debt under a non-judicial debt settlement mechanism should vary according to the quantum of the debt, with a large quantum of debt having a longer discharge period than a smaller one. The reasoning behind this is as follows:

- (i) even if a debtor quickly recovers their employment or income, the amount of money they could repay per year is unlikely to permit repaying all, or most, of a large debt within a short period;
- (ii) if the period is extended then there is a far more realistic scenario for dealing with large debts, such as mortgage shortfall;
- (iii) it is important, socially and economically, that debtors are encouraged to work, earn and live a normal lifestyle; and
- (iv) the debt settlement system should not materially increase, or appear to increase, the risk that debts will not be paid where borrowers are able to do so.

Informal Methods of Debt Settlement

56. The Group recommends that informal methods of debt settlement, such as contractual arrangements between debtor and creditor(s) or debt repayment plans negotiated through MABS continue to be utilised. Such informal arrangements provide for the repayment of debt over a period of time or for part payment for a temporary period until the debtor has sufficient resources to resume normal full repayment.

Extension of IBF-MABS Operational Protocol

57. The Group recommends that the voluntary engagement model of informal debt management operated through the IBF-MABS Operational Protocol be now developed as a template for extension to other credit providers, utility

companies, etc, who are concerned with the issue of personal over-indebtedness.

Standard Financial Statement (SFS)

58. The Group recommends that the completion of a SFS should be a mandatory requirement.

Role of MABS

59. Having regard to the scale of the personal debt problem, the Group considered the contribution that MABS could make in the context of enhancing the current informal debt settlement arrangements, or supporting any new arrangements that might be approved by Government. MABS currently assists persons with debt problems to agree (non-statutory) arrangements with creditors. The Group is aware of an ongoing review of MABS, following assignment of MABS to the Citizens Information Board (CIB), and would suggest that, if possible, any future development of a MABS role, including adequacy of resources, should be considered in this context.

Regulation/ Licensing of Debt Collectors

60. The Group recommends that a licensing system, containing a fit and proper person test and covering code of behaviour requirements, be considered for those engaged in the collection of debt.

Appeals Process

61. In its Interim Report, the Group proposed that the Financial Services Ombudsman (FSO) should undertake this role. The Group, upon further consideration, remains of the view that the FSO is the body best placed to fulfil this role.

Monitoring and Reviews

62. Having regard to the fact that the MARP and the DIS represents a new approach designed to address a specific problem, the Group believes that all its main constituent parts will require close monitoring from their commencement. It recommends that the MARP, the DIS and the Appeals Mechanism be formally reviewed within 18 months of commencement.

Chapter 3: Update since Interim Report

3.1 Statistical Analysis of the Mortgage Arrears Situation

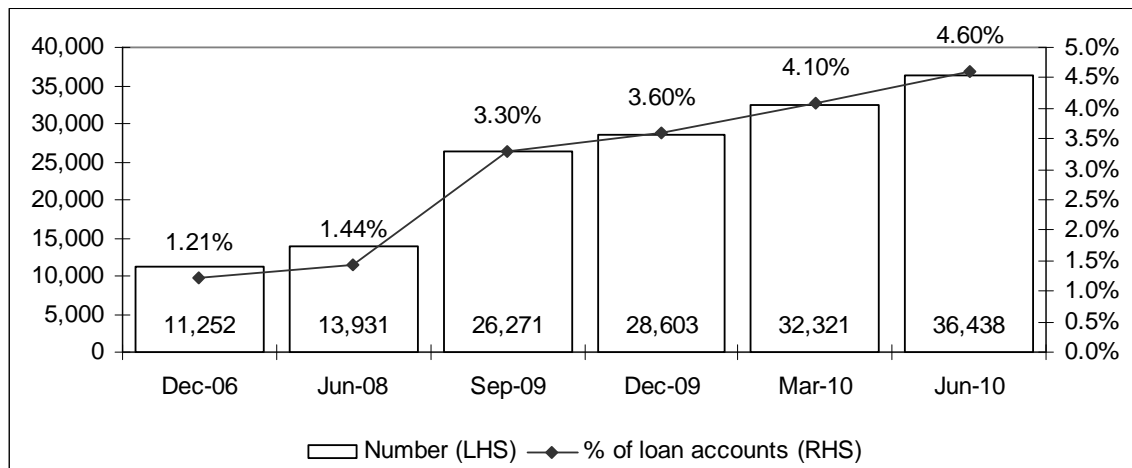
Arrears

3.1.1 Since the Interim Report of the Group was published, the Central Bank has released residential mortgage and arrears statistics for the quarter to end-June 2010³. The statistics show that the number of outstanding mortgage accounts at the end of the second quarter 2010 amounted to 789,814. Mortgage accounts in arrears for greater than 90 days rose to 36,438, up by 12.7 per cent on the previous quarter. Of this total, 68 per cent were in arrears for over 6 months.

Trend in Arrears

3.1.2 Figure 1 shows the trend in mortgage arrears number since December 2006. From September 2009, the Central Bank commenced a quarterly series on mortgage arrears data.

Figure 1, Volume of Mortgage Arrears and % of loan accounts:



Sources: December and June 2006, Financial Regulator, “Findings of Arrears and Repossessions Handling Procedures Examination”, Press Release, 16 December 2008. Other data from Financial Regulator “Residential Mortgage Arrears and Repossession Statistics”

Restructuring

3.1.3 As an input to the work of the Group, the Central Bank surveyed the lending institutions to estimate the level of restructuring at the end of June 2010. It is estimated from the survey that the number of rescheduled mortgage accounts is up to 45,000. The survey suggests that two thirds of restructured mortgages are paying at least the full interest. There is an overlap of 20- 25% between rescheduled mortgages and arrears cases, giving an estimated total of 70,000 who are either in arrears or have rescheduled.

³ Section 3(a) of the Code of Conduct on Mortgage Arrears states “a mortgage arrears problem arises as soon as the borrower fails to make a mortgage repayment by the due date”. Includes cases where only partial payments are made. Excludes (1) cases where the value of the property has been realised but an amount remains outstanding on which the lender is seeking repayment, and (2) any costs, fees or charges, e.g., legal costs, which have not been added to the amount outstanding.

Repossession Data from the Central Bank

3.1.4 Central Bank data on repossessions at end-June 2010 shows that the stock of repossessed properties in the possession of lenders increased to 496 properties, compared with 331 properties at end-September 2009. It is noticeable from the data in Table 2 below that the number of dwellings that are being repossessed as a result of a court order has been reducing since quarter 3, 2009.

Table 2: *Repossessions*

	Q3 2009	Q4 2009	Q1 2010	Q2 2010
Residential properties repossessed on foot of an Order during this quarter	31	27	26	20
Residential properties voluntarily surrendered/abandoned during this quarter	79	74	65	66
Residential properties disposed of during the quarter	22	35	32	45

Residential properties in possession at end of quarter¹

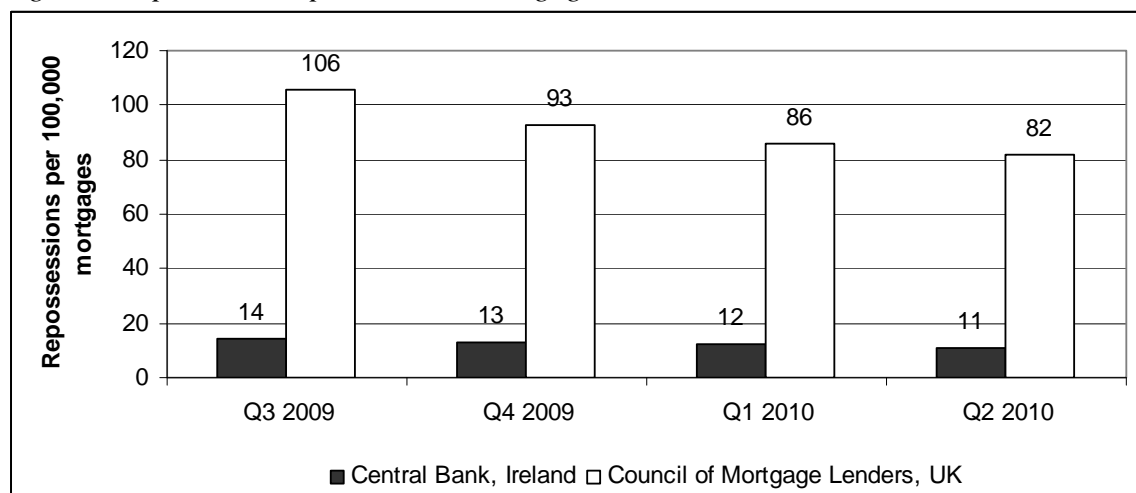
331 397 456 496

¹Cumulative residential properties in possession at the end of a quarter is based on the stock of properties in possession at the end of the previous quarter plus any properties repossessed or abandoned during the quarter less properties disposed of during the quarter. Thus, the number of properties in quarter 2 2010 is calculated by $(456+20+66)-45=496$.

Source: Central Bank, *Residential Mortgage Arrears and Repossession Statistics*

3.1.5 It should be noted that repossession levels in Ireland remain substantially lower than those experienced in the UK. For example, there were 11 repossessions per 100,000 mortgages in the second quarter of the year. This compares to 82 repossessions per 100,000 mortgages in the UK over the same period. See Figure 2 for illustration.

Figure 2 *Repossessions per 100,000 mortgages:*



Source: Irish Banking Federation/ Central Bank

Borrower Profile in Repossession Cases

3.1.6 While micro-data on repossession cases is difficult to obtain, data from 540 repossession cases listed for hearing in the High Court provides some insight into the

profile of borrowers in this position⁴. These are cases for repossession that are in the High Court system and so represent a mix of new cases and cases that remain on the list having previously been adjourned. The time line for completion of a repossession case is generally between 6 and 12 months. Factors impacting on the timeline include how quickly the lender can serve the summons on the borrower, whether the lender can demonstrate compliance with the code of conduct, whether the defendants are entering an appearance to the summons and if so, whether they have had an opportunity to consult MABS. As a result, cases that commenced in 2009 are still making their way through the system. According to the High Court, 105 of the cases listed before the Master during the months of June and July 2010 had not previously been listed before any court, i.e. they could be described as "new" cases.

3.1.7 Sub-prime lenders⁵ account for the majority of the 540 cases, although this probably reflects the fact that these lenders have, to date, primarily used the High Court for repossession cases. The data show that the majority of those listed for a repossession case borrowed late in the housing boom – mortgages taken out in 2006 and 2007 account for over 72 per cent of total cases.

3.1.8 The data show that for repossession cases the average loan on a borrower's residence is nearly €36,000. Average arrears are nearly €30,000. The average ratio of arrears to original loan size is 13.2 per cent. The average loan size peaked for those mortgages drawn down in 2007 at €61,400 but average arrears are highest for mortgages drawn down in 2008, at over €35,000.

3.2 Groups Views on the Sustainability of Mortgage Accounts

3.2.1 The Group considers that arrears cases and restructuring cases will vary widely in terms of their sustainability. The depth of arrears or restructuring is a critical determinant of the sustainability or otherwise of a mortgage. However, individual circumstances will also strongly influence whether a mortgage is sustainable or not. The Group considers that while a structured response to the mortgage arrears problem is necessary, lenders should be allowed the flexibility, within any proposed scheme in which they are participants, to make determinations on a case-by-case basis, regarding the long-term sustainability of a mortgage.

3.2.2 The Group recognises that borrowers who are provided with a substantial amount of additional time in order to secure the sustainability of their mortgage, may also be accumulating further debt in the process. The Group does not consider that it would be in the best interests of borrowers or lenders to allow unreasonable levels of debt accumulation. This forms the basis of the Group's proposal for an unsustainability test for such borrowers, set out in Chapter 4.

⁴ The lending institutions in these repossession cases were asked by the Master to provide information on the location of the property, whether or not it was the borrower's primary residence, the marital status of the borrower, the type of residence, the extent of the arrears, the size of the original mortgage and year of loan drawdown, as well as the type of lending institution. The anonymised raw data were given to the ESRI for analysis. These cases may not be representative of arrears or repossession cases as a whole.

⁵ Sub-prime lending is generally lending where a higher rate of interest than normal market rates is charged on the loan on the basis that the applicant borrower is perceived to be a greater credit risk.

Interest-Only Arrangements

3.2.3 While the objective is that borrowers should be able to pay off their mortgage in full, according to the original schedule, if a borrower is able to service the full interest on their mortgage, their position is not deteriorating. The amount which they owe the lender is not increasing. Therefore, the Group considers, over a medium term period, depending on individual circumstances, that interest-only arrangements are indicative of a sustainable mortgage.

3.2.4 We must stress that we are not recommending that borrowers switch to interest-only mortgages. Borrowers must pay off their mortgage according to the original schedule if they can afford to so do. What we are suggesting here is that a borrower who can afford to pay the interest on their mortgage should be given time to resume normal capital repayments.

Unsustainable Mortgage

3.2.5 The Group considers that the inability to make interest-only payments over a significant period of time, depending on individual circumstances, is indicative of an *unsustainable* mortgage. However, the Group considers that mortgage holders who can make substantial part-payments on the interest portion of their mortgage may have the capacity to secure the sustainability of their mortgage if they are given sufficient time. The Group draws from this understanding, and from its term of reference to improve the current situation for families with mortgage arrears, as the basis for proposals made in Chapter 4.

3.3 Negative Equity and Mortgage Sustainability

3.3.1 The Group does not consider the loan to value (LTV) ratio to be directly relevant in regard the determination of the sustainability of a mortgage. While we recognise the difficulty for people whose homes are currently worth substantially less than their mortgage, if they can service that mortgage it is considered a sustainable mortgage. In the absence of any affordability issues, negative equity only becomes a significant problem if a mortgage holder wishes to sell their home.

Trade Down

3.3.2 The Group considers that there may be potential to improve the position of some mortgage holders who are in negative equity, where households would be willing to trade-down. Trading down would produce a reduction in mortgage debt and more affordable monthly payments.

3.3.3 Where a borrower in negative equity trades down, the LTV would increase, although the cash value of the negative equity should not increase by more than the transaction costs of the move. However, the reduced payments would create a more secure scenario in that the income of the borrower would now more easily cover the mortgage payments. Depending on the size of the trade-down, the gains in affordability could be very significant. Lenders would also gain significantly from the reduced capital value and the immediate cash repayment.

3.3.4 Such options would only be available in limited circumstances to certain borrowers and would need further development by lenders who would need to satisfy themselves that the new mortgage would be securely affordable and that such a

product would meet relevant prudential standards and would be in the best interest of customers. In cases where a customer is already in difficulty and arrears already exist significant additional controls would need to be in place.

3.3.5 The Group recommends that further consideration should be given by lenders facilitating trading down by borrowers in negative equity, where this results in a significant reduction in mortgage debt and the cash value of the negative equity does not appreciably increase. Cost of trade-downs can be high and all parties to these transactions should endeavour to minimise them.

3.4 Appeals Process

3.4.1 The Group has considered the issue of appeal mechanisms for borrowers who are dissatisfied with decisions taken under the MARP. The Group is of the view that a substantive appeals mechanism, made available to all borrowers participating in the MARP, would provide protections to borrowers against unfair treatment and, more generally, provide trust and confidence in the integrity of the MARP.

3.4.2 The Group recognises that establishing and maintaining trust and confidence in the integrity of the MARP is best served through designating a critical adjudication role to a competent independent third party. In its Interim Report, the Group proposed that the Financial Services Ombudsman (FSO) should undertake this role. The Group, upon further consideration, remains of the view that the FSO is the body best placed to fulfil this role⁶.

3.4.3 The Group notes that appeals regarding the MARP are likely to impact on the number of cases going to the FSO. In addition, as arrears cases relate to the family home, the FSO is likely to want to deal with cases quickly. Given these factors, the Group would be anxious that the FSO would be sufficiently resourced in that regard.

3.4.4 The Group would now like to elaborate on its proposals for how a MARP appeals mechanism would work in practice:

1. A borrower, who is dissatisfied with decisions made under the MARP, or with their treatment within the MARP, or in relation to aspects of the amended CCMA, can seek a review by a separate unit within each lender's organisation.
2. Such a unit is to be established *separate* to the ASU and will consist of three senior personnel from within the lenders organisation. There must be at least one representative from the lenders Audit Committee on the review panel.
3. If, following the issuing of the lenders decision, a resolution has not been found, the borrower may refer the matter to the FSO for examination.

3.4.5 The Group is recommending that a review of the appeals process takes place within 18 months of the MARP becoming operational. This review should be undertaken by the Central Bank, with the co-operation of the FSO.

⁶ The Group acknowledges that the member representing Free Legal Advice Centres would have preferred to see a new appeals body set up to deal with the full range of potential appeals arising out of the MARP.

3.5 Issues for Future Consideration

3.5.1 The Group considered a range of issues which, while relevant, were not central to its remit or which may have more long term application. The Group recommend that the examination of the following issues should be taken forward by the relevant authorities.

Mortgage Lending Practices

3.5.2 The Group notes the findings from the Central Bank's review of the new mortgage market and the fact that follow-up action will take place on a lender by lender basis.

3.5.3 Similar to the approach adopted in regard to the work of the Law Reform Commission in the area of personal debt, the Group saw little added value to undertaking a parallel exercise to that being conducted by the Central Bank.

3.5.4 The Group notes that, in the Central Bank's strategy paper, "Banking Supervision: our new approach", a commitment was made to explore the scope and need for direct regulation of consumer credit policy. The Group understands that this project has now commenced and a paper will be published by the Central Bank in the first half of 2011 outlining the findings and proposed actions.

Mortgage Repayment and Indemnity Insurance

3.5.5 The Group is aware of the availability of various products in the market such as mortgage repayment insurance and mortgage indemnity insurance. However, given the current housing market and lending conditions, the Group does not consider that imposing such products are necessary or a priority. However, the Group considers that such issues should be reviewed in the future.

Chapter 4: Advanced Forbearance Options

4.1 Background

4.1.1 The terms of reference of the Group included the following commitment:

Having regard to the commitments in the Renewed Programme for Government to protect the family home and help those in personal debt to make recommendations to the Minister for Finance on options for improving the current situation for families with mortgage arrears and personal debt.

4.1.2 This Chapter outlines the Group's recommendations in relation to protecting the family home, by way of minimising the level of repossessions, having regard to a broad range of policy considerations, as set out in section 4.3.1. Chapter 5 discusses the options for cases where even advanced forbearance will not be adequate.

Standard Forbearance

4.1.3 The Mortgage Arrears Resolution Process (MARP) provides a framework for lenders to make an individual assessment of a borrower in mortgage arrears (or pre-arrears) and consider whether or not forbearance arrangements should be proposed. As noted in the Interim Report, in some cases mortgages will be unsustainable and voluntary surrender may be appropriate.

4.1.4 Where forbearance is appropriate, the MARP requires lenders to set out a menu of different forbearance approaches and to explain the criteria that they will use in suggesting a particular option for an individual borrower. The Group is aware of a range of forbearance techniques that are currently employed by lenders, typically comprising the following:

- a switch to an interest only mortgage;
- a temporary deferral of payment;
- extending the term of the mortgage; and
- capitalising arrears amounts and related interest.

4.1.5 The Group describes these as "Standard Forbearance" techniques: while they vary in their approach, they typically have the common characteristic of rescheduling principal or interest repayments, rather than reducing them. The Group is aware that standard forbearance is being offered and is working. However, in some circumstances standard forbearance techniques may be insufficient because the income of the borrower is too low to make payments, even on an interest-only basis, and the borrower's position is deteriorating as the interest is compounding.

4.1.6 The Group, in seeking to minimise the level of repossessions, has explored the potential application of more advanced levels of forbearance.

4.2 International Overview

4.2.1 The Group has reviewed the various schemes in place in other jurisdictions to provide support to borrowers in mortgage arrears. These are summarised in Appendix 2.

Government Debt for Equity Schemes

4.2.2 Government debt-for-equity schemes operate in Scotland and England and were considered by the Group. These schemes are generally dependent on the owner having a loan not exceeding 75% of the value of the home. Such schemes have a very low take-up in other countries and would have even less application in Ireland where a significant number of mortgages are in negative equity.

Loan Modification Schemes

4.2.3 Loan modification schemes involving permanent principal and interest reduction were identified in the US and have been considered by the Group. It should be noted that while these provide for a variety of standard forbearance and loan modification techniques, they involve federal government financial incentives to borrowers and lenders, and lenders are only obliged to offer forbearance or modification if the incentives mean it is in their financial interest to do so.

4.2.4 The Group could not identify any other arrangements internationally that could be characterised as debt forgiveness schemes. Our conclusion is that there is limited use of debt forgiveness approaches by other countries and that in the one country where this is adopted, the US, it is narrowly focussed, subsidised by government and there are important differences in market structure compared to Ireland⁷.

Potential Applicability in Irish Context

4.2.5 Most US mortgages are on a non-recourse basis which means that comparisons with Ireland, where the mortgage lender has recourse to the borrower in the event of any realised shortfall, need to be approached with caution. Non-recourse lending means that US borrowers have a stronger incentive to ‘hand back the keys,’ with the lender (not the borrower) facing losses arising from negative equity. As a result, US lenders have an added incentive to keep borrowers performing and to support loan modification programmes as an alternative to repossession. Even so, the US programmes involve a high level of government incentive contributions, with an average payment of over \$20,000 per borrower.

4.2.6 It should also be noted that most US mortgages are covered by Federal Guarantee Programmes, such as Fannie Mae and Freddie Mac. This means that the US government already has a direct financial interest in the performance of mortgages and the costs of federal expenditure to provide debt forgiveness can be considered against the cost of losses incurred under the guarantee programmes.

⁷ A recent amendment to the US HAMP scheme has provided for principal reduction for certain classes of mortgage. However, in the US HAMP scheme, the federal government provides a payment to the relevant lender of, typically, 15c for every \$1 of principal reduction. The Group is concerned of the potential cost of such a scheme in an Irish context.

4.3 Advanced Forbearance in Ireland - Policy Considerations

4.3.1 The Group has carefully weighed the merits of proposing advanced forbearance, or loan modification, techniques in Ireland. There are a number of factors to be considered, including:

- The fact that standard forbearance techniques will be inadequate for some borrowers who have insufficient income;
- The perceived fairness of providing support to individuals and households given that State support has been extended to financial institutions;
- Avoiding a persistent drag on the economy from an overhang of servicing high levels of mortgage debt;
- The perceived fairness of asking taxpayers who (a) do not own a home or (b) have modest mortgage outlays, to assist mortgage holders in arrears, including those who own a high value property;
- Any scheme should take into account the individual's personal and financial circumstances and the extent to which individual circumstances are likely to vary;
- The 'moral hazard' of providing an incentive for borrowers to fall into arrears or more severe arrears;
- The cost of any Government-sponsored incentives, in addition to MIS support, given the significant fiscal constraints facing the Irish Exchequer and at a time of pressure in sovereign debt markets;
- The cost to lenders following severe lending losses and the need to avoid adverse capital implications should an advanced forbearance scheme cause losses to exceed provisions or regulatory capital requirements;
- The impact on lenders' funding costs (and therefore on the interest rates they will be required to charge *all* borrowers) as a result of any adverse impact of advanced forbearance on wholesale funding and also securitised mortgage debt; and
- The impact of changes to the legal structure of existing mortgage accounts in terms of lender appetite to conduct new mortgage lending.

4.3.2 The Group considered whether any proposed advanced forbearance scheme should be compulsory but concluded that there are likely to be significant legal impediments to such an approach. These relate to the nature of the contract between the borrower and the lender and whether such contracts can be effectively set aside or altered by the imposition of an advanced forbearance scheme. The Group noted schemes such as those in the US are not compulsory. The Group concluded that the most feasible option is to introduce a voluntary scheme with the support of as many lenders as possible.

4.3.3 For reasons outlined above, the Group is of the view that lender participation in any advanced forbearance scheme should be voluntary and recognises that lenders may wish to adopt the proposed scheme in a manner which best fits with their own requirements. However, the Group believes that any scheme adopted by lenders should have, at its core, the objective of extending forbearance to borrowers who cannot make the full interest payments on their mortgage but who can make substantial part payments. The Group also believes that any scheme adopted by lenders should not expose participating borrowers to interest on unpaid interest.

4.4 Proposed Deferred Interest Scheme (DIS)

4.4.1 In reviewing possible advanced forbearance techniques, the Group believes that the approach that would work most effectively as a complement to existing standard forbearance techniques would be a Deferred Interest Scheme (DIS). The proposed scheme is a form of advanced forbearance or loan modification and is not debt forgiveness. The Group considers that the overriding objective of a DIS is to provide more time for borrowers in difficulty to secure the sustainability of their mortgage, while limiting the extent to which they can fall further into arrears. It would also mean that borrowers would not have to pay interest on unpaid interest. While the financial benefits to the borrower of this may be modest, the Group believes that it provides a degree of comfort to borrowers to know that any interest repayments which they cannot afford to pay will remain static.

Features of a Deferred Interest Scheme (DIS)

4.4.2 In summary, the scheme would work as follows:

1. DIS is made available to borrowers who cannot afford to pay the full interest on their mortgage and who meet the eligibility criteria set out in 4.4.3.
2. The borrower should pay as much interest as they can afford but as a minimum they must pay 66%. The amount which the borrower could afford to pay would be determined via the MARP and Standard Financial Statement (SFS).
3. The lender calculates the amount of interest which the borrower cannot afford to pay each year and this is deferred.
4. The deferred interest accumulates in a non-interest charging deferral account.
5. The deferred interest continues to be secured on the property.
6. The point of exit from the DIS should occur when the accumulated amount in the deferred interest account is an amount equal to 18 months interest (inclusive of any interest arrears accumulated before a borrower entered a DIS scheme) or when the borrower has participated in the DIS for a total of 5 years, whichever comes sooner.
7. A lender may choose to offer the borrower a further period of DIS when the point of exit has been reached, if individual circumstances warrant such a decision.

Eligibility Criteria to DIS

4.4.3 The borrower must meet all of the following criteria:

1. The mortgage was taken out to purchase, improve or re-mortgage the borrower's principal place of residence only (as defined in the CCMA);
2. The mortgage was taken out prior to the introduction of the Code of Conduct on Mortgage Arrears, i.e., before 27 February 2009;
3. The borrower has entered and co-operated with the MARP, with asset disposals taking place as necessary and any guarantees taken into account;
4. There has been a minimum period of 6 months in which the borrower and lender must seek to address repayment difficulties. Specifically, the borrower must have been unable to pay the full amount of interest due under an interest only arrangement. This period could involve, for example, asset disposals, or it

could involve a lender offering the borrower a period of some form of standard forbearance;

5. The borrower cannot afford to pay the full interest on their mortgage but can, at a minimum, pay 66% of the interest due on the mortgage;
6. The borrower agrees not to take out any further loans. There should, however, be a degree of flexibility in this regard, for example where a self-employed individual has made a compelling case that a new business loan would significantly improve, over time, his/her financial position.

4.4.4 It is envisaged that DIS will be closed to new entrants after a period of three years.

Determination of an Unsustainable Mortgage for DIS Participants

4.4.5 The Group's consideration of a test for an unsustainable mortgage involved striking a balance between enabling borrowers as much time as possible to secure the sustainability of their mortgage (while limiting the extent to which they are exposed to accumulating further debt), without undermining the commercial position of lenders, while having regard to the wider implications for the taxpayer and indeed the broad spectrum of mortgage holders. The Group is recommending that the following test be used as the basis determining the sustainability of a mortgage for DIS participants: when a borrower has accumulated an amount equal to 18 months interest (including any unpaid interest accumulated before the borrower entered into the DIS scheme) he/she may be deemed to hold an unsustainable mortgage. This test will be used as the basis for determining whether to discontinue with borrower participation in the DIS and explore options such as those set out in 4.4.10.

4.4.6 The Group considers that an amount equal to 18 months interest provides a very significant time benefit to borrowers who can demonstrate sufficient repayment capacity. For a borrower who can afford to pay, for example, a constant 70% of his/her interest repayments, it would take 5 years before an amount equal to 18 months interest was accumulated, assuming no interest arrears occurred before entering DIS. The Group does not believe that participation in the scheme should be open-ended and is recommending a maximum 5 year time limit for participation in the scheme. This would not preclude lenders from extending forbearance beyond 5 years, or indeed beyond an amount equal to 18 months interest. However, consistent with our view set out in Chapter 3, any such extension must have regard to the exposure of borrowers to accumulating further debt.

Status of Accumulated Deferred Interest

4.4.7 In the event of a sale of the property, the deferred interest is added to the principal outstanding on the mortgage in order to determine the total outstanding debt. Where the proceeds of sale do not cover the total outstanding debt, this residual amount ('the mortgage shortfall') will be treated as an unsecured debt still owed to the mortgage lender. Therefore, the Group is recommending that the lender has recourse to the borrower in relation to any accumulated deferred interest.

Options Following Annual Review

4.4.8 There should be periodic reviews, at a minimum annually, of the borrower's circumstances, as with all forbearance arrangements under the MARP. However, there should be an immediate review if the borrower's circumstances substantially changes

and the borrower is obliged to inform the lender of any such changes. Any review must have regard to exposing the borrower to further debt. In this regard, borrowers should not continue in a DIS unless they have been deemed to have reasonable prospects of securing the sustainability of their mortgage over a period of time.

4.4.9 If the borrower's financial situation improves, to the extent that he/she is in a position to pay *more* than the full interest amount, this excess income can be used to either (a) pay down the principal or (b) reduce the accumulated deferred interest. The Group notes that a normal mortgage contract would mandate the borrower in such a position to pay down the interest first.

4.4.10 If a review concludes that the borrowers' situation has continued to deteriorate, the mortgage may be deemed to be unsustainable and may be deemed to be ineligible for entry to, or continuance in, the DIS. At this point, a number of options may be considered, including:

1. Voluntary Surrender;
2. Assisted Sale;
3. Trade Down; and
4. Repossession.

Some of these options may trigger a social housing needs assessment and this area is discussed in Chapter 5.

Period between Repossession and Sale

4.4.11 In Chapter 6, the Group has set out its view that a mortgage shortfall crystallises when a repossessed property is sold by the lender for less than the amount owed by the borrower. The Group however recognises that there may be a significant gap in time between the conclusion that a mortgage is unsustainable and the sale of the repossessed property.

4.4.12 Important questions remain as to how the amount owed to the lender should be treated in the meantime. In the case of costs incurred in the course of sale, the Group recommends that lenders must be transparent in terms of the information provided to the borrower on such costs both in advance of repossession and when the sale takes place.

4.4.13 The Group recognises that an early assisted sale may have advantages over a formal repossession in the case of an unsustainable mortgage. We recommend that lenders develop a protocol setting out their practices, procedures and charges in this area.

DIS and Capital Implications for Lenders

4.4.14 Under a DIS, or other advanced forbearance approach, care would need to be taken concerning the financial impact on the lender so that it does not undermine compliance with regulatory capital requirements, given the fragile condition of lenders' balance sheets.

4.4.15 Given the dependence of some lenders on Government support for their capital position, a high degree of advanced forbearance could effectively constitute a scheme

directly funded by taxpayers for the benefit of certain borrowers in arrears (i.e. it would represent an additional cost above and beyond the provision of MIS). This would also have fiscal implications.

4.5 Participation by Lenders in a Deferred Interest Scheme

4.5.1 The Group believes that all mortgage lenders should participate in the DIS, or equivalent scheme, for the following reasons:

- It would provide an industry-wide approach to address a defined segment of the mortgage arrears problem and a consistency of treatment for borrowers who fall into this segment; and
- The DIS approach is a balanced and measured approach to advanced forbearance compared to some of the policy responses that could be considered. By demonstrating a firm commitment to working through problems with borrowers eligible for DIS, lenders can show they are adopting an approach which is responsible and recognises the extent of the problem.

4.5.2 The Group is encouraged that lenders representing the majority of the market have already indicated their willingness to implement DIS or an equivalent scheme and the remaining participants will be requested to do so.

Periodic Review of DIS

4.5.3 The Group is proposing that DIS should be closed to new entrants after a period of 3 years. However, the scheme itself should be subject to a review within 18 months of its commencement in order to inform whether alternative policy actions are required. Relevant indicators of the operation of the DIS would include the level of take up of the DIS approach; the operation of the MARP and the utilisation of standard forbearance techniques; and the general approach of mortgage lenders and mortgage holders.

4.6 Mortgage Interest Supplement (including interaction with DIS)

4.6.1 The payment of Mortgage Interest Supplement (MIS) represents a significant and valuable State intervention that provides an essential support for borrowers who are having difficulty in repaying their mortgage. Indirectly, lenders also benefit under the scheme. In 2008 MIS assisted around 8,100 borrowers. However, at present, MIS assists almost 17,800 borrowers, at an estimated cost of €64 million in 2010. As set out in our Interim Report, it is expected that this level of support will continue.

4.6.2 In our Interim Report, we made certain recommendations for changes to the MIS and we also approved of the proposed changes put forward by the Working Group on the Review of the MIS. The Group welcomes the Government's acceptance of the recommendations of both reports and considers that, when implemented, the revised scheme will be more equitable and targeted. While the Group considers that the provision of short term income support remains valid and should be timebound, it suggests that the support provided should not be terminated without some period of adjustment. Therefore, the Group recommends that the Department of Social Protection, in its development of the qualification criteria for the revised MIS scheme, should consider how a gradually reducing rate of assistance may apply in certain cases, following the timebound period.

Cessation of MIS and Interaction with DIS

4.6.3 The MIS means test determines how much of the interest the borrower must contribute towards their mortgage. If the borrower does not pay their contribution, they would be in breach of the conditions of MIS, which would be withdrawn. Information sharing protocols would have to be agreed between all appropriate authorities to deal with such cases, having regard to the legislative and data protection requirements.

4.6.4 For the first period of MIS support, the total amount of interest due will be paid through a combination of MIS and the borrower's own contribution. Therefore, the loan is deemed sustainable and the borrower does not need, and will not be eligible, to participate in DIS.

4.6.5 During any period of tapering of MIS, the borrower may then be eligible to participate in DIS. On cessation of MIS and any tapering arrangement, the borrower may continue to be eligible for DIS, depending on the qualification criteria.

Chapter 5 – Social Housing Supports

5.1 Background

5.1.1 The terms of reference of the Group included the following commitment in relation to long term housing supports:

To examine the state support schemes and to make recommendations as appropriate for improvement having taken into account Mortgage Support Schemes in operation in other jurisdictions.

5.1.2 In its Interim Report, the Group recommended that the MARP should provide that where an arrears case has been determined to be unsustainable in the long term, even with forbearance, “a voluntary surrender of the property may take place or the lender may agree that the borrower put the property up for sale”. This reflects one of the underlying principles adopted by the Group in its Interim Report, which states that “Repossessions should be minimised but it is acknowledged that in some cases, voluntary surrender may be the best option for both borrower and lender”.

5.1.3 This Chapter outlines the Group’s recommendations for those who have been deemed to hold unsustainable mortgages and who are not in a position to meet their accommodation needs from within their own resources. Existing housing supports and the potential application to Ireland of supports available in other jurisdictions are also considered.

5.2 Coherence with Evolving Social Housing Policies

5.2.1 Local authorities remain the main providers of housing for those in need who cannot afford their accommodation needs from their own resources. Long term social housing supports, delivered to households in need of social housing, can be either through (a) direct provision by local authorities, or (b) indirectly, with local authorities regulating the provision of social housing, provided by approved housing bodies or accommodation providers (including private landlords). The Group also noted the substantial support provided by the Department of Social Protection through the rent supplement scheme.

5.2.2 In the past “housing need” has been closely approximated with a permanent need for a local authority house. The range of long term social housing supports has broadened significantly in recent years. This has allowed for the development of a more graduated system of flexible supports that is capable of being tailored to take specific account of the particular needs of households at various stages in the life-cycle. Social housing supports now include the provision of accommodation through:

- A. arrangements with private landlords for long or short leases, for single or multiple units;
- B. units owned or leased by the voluntary and co-operative sector; and
- C. units owned or leased by the local authority which they have built, procured or acquired, for example, under Part V of the Planning and Development Act.

5.2.3 The Group considers that, within these broad categories and subject to some modification (in particular, to allow for proactive communication to local authorities during the MARP), sufficient flexibility exists to support the transition out of home-ownership into social housing for households with unsustainable mortgages and who are not in a position to meet their accommodation needs from within their own resources.

5.2.4 The Group is also of the view that households already on housing authority waiting lists should expect equal treatment to households that emerge from the MARP with “unsustainable mortgages”. In that context, the overriding objective for the “unsustainable mortgage” household category should be that their long term accommodation needs are appropriately met at reasonable costs. The Group understands that this is the case with all other households on housing authority waiting lists. Maintaining a household in their existing accommodation would be an aspiration, but, in the context of rising social housing need and a difficult budgetary situation, necessarily a subsidiary one.

5.3 Access to Social Housing Supports

5.3.1 Where a household applies to be assessed for social housing support, the housing authority must then decide whether the household is eligible for and in need of social housing support. Accommodation is then allocated to eligible households in order of priority, taking all of the households’ circumstances into account.

5.3.2 The current assessment process provides that households with accommodation available to them (i.e. if they own a property in which they can reside) would not be classed as being in need of social housing support. This means that only where a household loses access to their existing accommodation (i.e. were the house to be the subject of a repossession order or, in some cases, actually reposessed) can they then be considered to be eligible for, and in need of, social housing support (other criteria also apply). The Group is of the view that this situation is not in the best interests of the household deemed in need of social housing support, could add to their distress and does not allow local authorities to adopt a planned approach to dealing with the unsustainable cases presenting for support.

5.3.3 The Group therefore welcomes the work ongoing within the Department of the Environment, Heritage and Local Government (DoEHLG) on the development of a new needs assessment process. This will allow a household deemed to hold an unsustainable mortgage and in need of social housing, to be considered eligible for social housing supports at an earlier stage.

5.3.4 New regulations and guidance currently being developed in the context of the social housing reform programme will provide that housing authorities can disregard the household’s current accommodation for the purposes of determining eligibility for social housing support (The relevant provision in the Housing (Miscellaneous Provisions) Act 2009 provides that ownership of accommodation is one of the criteria which determines eligibility).

5.3.5 As part of this new assessment process, the DoEHLG will develop a protocol to facilitate early communication between lenders and local authorities. This will enable a needs assessment to be undertaken proactively and the relevant local

authority be given as much time as possible to identify the possible numbers of unsustainable cases that may ultimately require supports. The Group would recommend that lenders constructively engage with the Department in relation to this matter. The Department will also receive regular information from the Department of Social Protection on the number of MIS recipients whose period of support is nearing an end.

5.4 Social Housing Support Options

The Groups considered a number of social housing support options which are set out below. The issue of the mortgage shortfall, arising from the sale of the property for an amount less than that remaining on the mortgage, is dealt with in Chapter 6.

Existing Social Housing Stock

5.4.1 The Group is of the view that it is in the interests of the borrower and lender that the household would be accommodated within the existing social housing stock where (a) a mortgage has been deemed unsustainable; (b) the household in question is deemed eligible for long term social housing support; and (c) the relevant local authority has available suitable accommodation to immediately meet that household's need.

Leasing Repossessed Homes from Lenders

5.4.2 The Group considered possibilities for local authorities to enter into lease-type arrangements with lenders in respect of properties held under unsustainable mortgages. Such an arrangement would see the lender acquire the property following a voluntary repossession or surrender, then agreeing to make the property available to the relevant local authority, for a consideration. The local authority would in turn let the property to the former owner (now tenant). Like any other local authority tenant, the household would pay a differential rent to the local authority. The lease payment paid by the local authority would be based on market rent. However, the rent would be adjusted to take account of the local authority assuming responsibility for the management and maintenance of the property as well as guaranteeing the lender against vacant periods.

5.4.3 However, close examination of this option revealed a number of complexities which could ultimately give rise to significant additional costs to the lender and, as a consequence, to the State. These additional costs arise out of the requirements on lenders to treat different financial products and transactions differently in terms of the capital set aside to mitigate risk. Under the Capital Requirements Directive, the capital weighting assigned to a commercial loan (which would be used by a lender to acquire the property) requires a higher level of capital weighting than a mortgage. In the case of standard repossessions this additional capital requirement does not arise because a lender does not actually take ownership of the repossessed property. Instead, it is held by the lender until such time as it can be sold at the best price obtainable.

5.4.4 From an equity point of view, it would be important that any such option fit within the financial model of the leasing initiative. At one level, this approach would achieve that, with the local authority providing a lease payment based on a market rent. However, the ultimate costs of any additional capital weighting requirements arising could largely fall upon the Exchequer and the wider taxpayer. The Group

considered that the leasing option, as set out above, would not be appropriate as there are other mechanisms available that can realise the objective of meeting the accommodation needs of households with unsustainable mortgages within the financial framework of existing social housing supports.

Leasing from Private Sector - Mortgage Relief Funds

5.4.5 In addition, the Group noted that a number of proposals had been made to lenders and a number of government departments by entities proposing to acquire significant residential portfolios, including the acquisition of properties currently owned by households with significant levels of arrears. These properties would be repossessed then be leased back, under the Social Housing Leasing Initiative (SHLI), to the relevant local authority, with the former home owners remaining as tenants. The Group noted the willingness of the DoEHLG and the Irish Banking Federation to further explore these proposals and recommends that this be expedited.

5.4.6 The Group was of the view that there was potential for synergies between the work of the National Asset Management Agency (NAMA), in ensuring the stability of the financial system, and the role of the Department of the Environment, Heritage and Local Government (and housing authorities), in responding to social housing needs. In that regard, the Group welcomed the ongoing engagement by the Department with NAMA to discuss a means of securing a social dividend through the long-term leasing of suitable residential units for social housing purposes, while providing an economic return in line with NAMA's mandate.

Agreed Stay on Repossession / Tenancy at Will Arrangements

5.4.7 The Group recommend that lenders and the local authorities should communicate at an early stage in relation to unsustainable cases.

5.4.8 The Group understands that, in general, housing authorities do not have a sufficient stock of properties into which households who lose their homes can be transferred. It noted that while there have been reports of large numbers of vacant, completed and unsold housing units across the country, the DoEHLG has reported that progress to date in rolling out the leasing initiative, - which had targeted vacant new units at the outset – has been slower than anticipated.

5.4.9 The Group is of the view that housing authorities should be given time to plan and properly provide for meeting long term social housing supports for households in need. In that regard, the Group recommends that a mechanism be put in place which would enable, where appropriate, the parties (borrower and lender) agree to a voluntary repossession, with *actual* repossession deferred for a specified maximum period, or until such time as the housing authority has sourced appropriate accommodation, whichever comes sooner. The Group recommends that mortgage lenders, the DoEHLG and other relevant departments work together to put in place such a mechanism early in the New Year.

5.4.10 The option of a 'stay' period allowed would not be envisaged to apply following a period of forbearance or extended forbearance. Instead, such an arrangement would apply in those cases where a determination had been made *early* in the arrears process that a mortgage was unsustainable. This would have to be followed by a decision by the relevant local authority that the particular household

would be eligible for social housing. A significantly reduced period would be required for households which have gone through a significant period of forbearance but which have ultimately required social housing supports. This would be on the basis that the protocol referred to in section 5.3.5 would have provided sufficient notice for the relevant housing authority. In cases where a housing authority has suitable property on hands, repossession would not be deferred.

5.4.11 It is important to note however that none of these options would constitute a mortgage to rent scheme. The primary objective of these mechanisms would be to allow the relevant housing authority a period of time in which to source suitable long-term accommodation for a particular household. A subsidiary benefit of this approach is that it also gives the household a further period to remain in their former home.

Potential Role of a Mortgage to Rent Scheme

5.4.12 The Group considered the potential role of a mortgage to rent scheme in Ireland and looked at the operation of such schemes in other jurisdictions. The Group noted that mortgage to rent schemes operating in the UK are based on very different funding models than that which would pertain in Ireland - see Appendix 3 for analysis on this point. The Group concluded that the current budgetary and fiscal environment and existing levels of social housing need⁸ meant that the introduction of an Exchequer funded mortgage to rent scheme would neither be feasible nor equitable.

5.4.13 The Group noted, however, that a mortgage to rent scheme, involving the use of loan finance obtained by approved housing bodies (AHBs) and backed by the stream of revenue funding under the Social Housing Leasing Initiative, could be worthy of further consideration, were the general fiscal position and conditions in funding markets to significantly improve.

⁸ At the last formal count, some 56,000 households were assessed as being in need of social housing. Indications from local authorities would suggest that current levels of need are in excess of this figure.

Chapter 6: Personal Debt

6.1 Background

Extent of the Personal Debt Problem in Ireland

6.1.1 Central Bank data for September 2010 show €20.4bn outstanding in consumer loans and a further €10.8bn outstanding in “other loans” within the household sector⁹. This data does not include what is likely to be a substantial amount of personal debt owed to entities not captured by Central Bank statistics, such as utilities, catalogue companies, some car finance companies, licensed moneylenders and others.

6.1.2 Unlike owner-occupier mortgage debt, there is no official data that measures the incidence and extent of arrears in this area. However, notwithstanding trends which have seen outstanding personal debt reduce over the last year, there are strong indications that a large number of people are facing serious difficulty meeting loan repayments on various forms of non-mortgage personal debt¹⁰.

Group Consideration of the Personal Debt Issue

6.1.3 The information gathering and consultation approach adopted by the Group in regard to its consideration of the personal debt issue was guided by the relevant terms of reference, as follows:

“To have regard to ongoing deliberations by the Law Reform Commission on personal debt. In particular to consider how to reform personal insolvency and bankruptcy regulations and to establish as far as possible how non-judicial settlement proceedings can be formulated.”

6.1.4 The Commission produced a very extensive Consultation Paper on Personal Debt Management and Debt Enforcement in September 2009 and an Interim Report in May 2010. The Group understands that the Law Reform Commission (LRC) will, before the end of 2010, publish its Final Report containing recommendations on the comprehensive long term reform of the system of personal insolvency law and procedures for the enforcement of judgments in Ireland. The Interim Report of the Group noted that the recommendations to be contained in the Final Report of the LRC will be crucial to the reform process.

6.1.5 The Commission’s Consultation Paper criticised the inappropriateness of the Bankruptcy Act 1988 in a number of respects. It identified particular features – the 1988 Act fails to deal with modern consumer over-indebtedness, excessive costs of bankruptcy proceedings, very onerous conditions for discharge and suggested that personal insolvency law in Ireland should be reformed.¹¹ In addition the Commission

⁹ Source: Table A.1 of the Central Bank’s ‘Money & Banking’ statistics September 2010. “Other loans” incorporate a substantial amount of loans which are not considered as “pure” consumer loans but which are related to a persons (often a sole trader or a partner) business or a personal investment. Present bankruptcy law in Ireland does not, as a general rule, distinguish between “pure” consumer debt and “other” consumer debt.

¹⁰ For example, Court Service data show that there has been a 40% increase in the total number of judgments against debtors registered for the first nine months of 2010 versus the same period for 2009. The total figure has increased from 4,128 to 30/09/2009 to 5,784 to 30/09/2010.

¹¹ See Law Reform Commission Consultation Paper on Personal Debt Management and Debt Enforcement (LRC CP 56-2009) at paragraph 3.159 -3.177

was critical of the debt enforcement system in Ireland which failed to distinguish between ‘can’t pay’ and ‘won’t pay’ debtors, fails to address the problems of multiply-indebted consumers and it stated that legal enforcement procedures are contained in outdated legislation and are inefficient and costly.¹² The Commission therefore provisionally recommended that a non-judicial debt settlement system should be introduced into Irish law (a non-judicial system should be preferred over a court based system for personal insolvency proceedings), that the law should reflect and support a holistic approach to debt management and debt enforcement. The Commission relied on a number of European studies and recommendations.¹³

6.1.6 The Group has not conducted an extensive examination of the issues relating to non-mortgage personal debt, as it saw little added value to undertaking a parallel exercise to that being conducted by the LRC. The Group has, however, addressed the issue of mortgage shortfall in the context of debt settlement outlined in this Chapter.

6.2 International Overview

6.2.1 In a European Report of 2003 it was acknowledged that consumer insolvency law had become part of a European legal tradition and that ten out of the then 15 Member States had consumer insolvency legislation in place.¹⁴ It was noted that both Italy and Portugal were in the process of preparing such laws while only Greece, Ireland and Spain had not yet commenced a serious legal policy discussion on consumer insolvency regulation.

6.2.2 In most European countries there is a two tiered approach to consumer insolvency proceedings which include both out-of-court procedures and a formal court insolvency procedure. There are also similar non-judicial insolvency procedures in other jurisdictions, including Australia and Canada. In many jurisdictions it is only possible to enter into a formal judicial procedure in court if the non-judicial route has first been used. In some countries the informal insolvency procedure is overseen by a court, for example in Belgium, as distinct from Germany and Sweden, where such procedure is overseen by a Debt Enforcement Authority.

¹² See Law Reform Commission Consultation Paper on Personal Debt Management and Debt Enforcement (LRC CP 56-2009) at paragraph 3.317 – 3.335

¹³ The Council of Europe Final Report on Seeking Solutions to Debt Problems (CJ-S-Debt) 18 January 2007 and Effective Enforcement of Judgments in the European Union: The Transparency of Debtor Assets (European Commission Green Paper COM(2008) 128 final 2008)

Also see Recommendation CM/Rec (2007) 8 of the Committee of Ministers to member states on legal solutions to debt problems which ‘Recommends that the government of member states, when formulating their internal legislation and practice and when seeking legal solutions to debt problems and over-indebtedness:....Introduce mechanisms necessary to facilitate rehabilitation of over-indebted individuals and families and their reintegration into society in particular by: establishing mechanisms for extra-judicial settlements and encouraging such settlements between debtor and creditor’.

¹⁴ Reifner, Kiesilainen, Huls, Springeneer Consumer Overindebtedness and Consumer Law in the European Union (Report presented to the Commission of the European Communities, Health and Consumer Protection Directorate-General Contract Reference No. B5-1000/02/00353) at 246. Consumer Insolvency law is referred to as laws that provide for a partial or total discharge of debt, that are accessible to consumers and other private debtors at a reasonable cost and that include debtor’s assets, future income and all debts in the same arrangement.

Features of Consumer Insolvency Law in other Jurisdictions

6.2.3 A feature of European consumer insolvency law is that a discharge from debt is earned by the debtor entering into a repayment or settlement plan over a period of years. The debtor is obliged to use all income that is not required for living costs to pay off debts that are owed. Across Europe the living costs of the debtor and his/her family are calculated using the minimum level of social assistance as a starting point. The average length of the plan in Member States is five years.¹⁵ Belgium, Denmark, Finland, the Netherlands and Sweden all have five year payment plans. The duration of the plans is not regulated, for example, in Denmark, but in practice they are between three and five years. In Belgium and the Netherlands, the minimum duration is three years and the maximum is five years. The legislation in Sweden prescribes five years but the law also allows some discretion in the duration of the plan. In Germany the duration of the plan is 6 years. In Austria the normal duration is seven years although the duration may depend on the ability of the debtor to pay. If the debtor pays more than 50% of the outstanding debt, a discharge may be granted after three years.

6.2.4 A feature of the non-judicial procedure in many jurisdictions is that there is a stay on debt enforcement proceedings by creditors either to protect the negotiations leading to a debt settlement plan (examples are Sweden, France and Luxembourg) or for the duration of the debt settlement plan (examples are Austria, Finland and Germany).

6.2.5 There is an insolvency test in European countries but the test varies from ‘the manifest impossibility for a debtor in good faith to meet his/her debts taken as a whole as they fall due and payable’ in France to more long term financial difficulties in Luxembourg. In Sweden the requirement is that (other than a temporary inability) the debtor is unable to pay debts as they fall due. There is also an obligation for debtors to act in good faith and there are restrictions for those who do not act in good faith. The legislation in some countries specify behaviour that will exclude access such as non-disclosure, giving false information to obtain credit or has run into debt with a debt arrangement procedure in mind for example Finland.

6.2.6 The equality of creditors, or the *pari passu*¹⁶ treatment, is one of the primary rules in European consumer insolvency legislation.

Treatment of Mortgage Shortfall Debt in other Jurisdictions

6.2.7 In many countries consumer insolvency proceedings do not affect the right of secured creditors to enforce the debt even where there is a stay on proceedings for personal consumer debt. There is specific provision in the Australian legislation which provides that nothing in a debt agreement will affect the right of a secured creditor to realise or otherwise deal with the creditor’s security.

6.2.8 There is no special protection for homes in Member States in Europe in insolvency proceedings. This means that the home may be sold to realise any equity in

¹⁵ Ibid at 189

¹⁶ *Pari Passu* is taken to mean ‘equal in all respects, at the same pace or rate, in the same degree of proportion, or enjoying the same rights without bias or preference’

the home and mortgage debt may fall within debts arrangements. However where this is so, such as Finland and Germany, the right to payment is secured to the creditor up to the value of the mortgage debt. In France, the home mortgage debt which exceeds the value of the house can be discharged in a debt settlement arrangement.¹⁷ Generally, where there is a forced sale or repossession, secured creditors are not affected by a debt settlement arrangement, but to the extent that a secured claim (including mortgage debt) is not satisfied out of the proceeds of sale, the balance (i.e. the mortgage shortfall) ranks with all other unsecured debts.

6.3 The Reform Perspective for Personal Insolvency

Informal Methods of Debt Settlement

6.3.1 The Group is aware that informal methods of debt settlement, such as contractual arrangements between debtor and creditor(s) or debt repayment plans negotiated through Money Advice and Budgeting Services (MABS), are currently being negotiated and utilised. The Group fully endorses these approaches which should continue to be utilised. Such informal arrangements provide for the repayment of debt over a period of time or for part payment for a temporary period until the debtor has sufficient resources to resume normal full repayment.

Role of MABS

6.3.2 The Group recognises the current valuable role of the MABS in providing information and advice to assist an increasing numbers of persons with debt problems. MABS also has an advocacy role in regard to dealing with indebtedness.

6.3.3 Having regard to the scale of the personal debt problem, the Group considered the contribution that MABS could make in the context of enhancing the current informal debt settlement arrangements, or supporting any new arrangements that might be approved by Government. MABS currently assists persons with debt problems to agree (non-statutory) arrangements with creditors. The Group is aware of an ongoing review of MABS, following assignment of MABS to the Citizens Information Board (CIB), and would suggest that, if possible, any future development of a MABS role, including adequacy of resources, should be considered in this context.

IBF-MABS Operational Protocol on Debt Management

6.3.4 The Group has had the opportunity, in regard to personal debt, to consider the valuable contribution of the Irish Banking Federation-Money Advice and Budgeting Services (IBF/MABS) Operational Protocol ('Working Together to Manage Debt') in dealing with debt arrears. Both the IBF and MABS recently completed a comprehensive review of the operation of the Protocol, output from which included a system of statistical reporting by MABS on the use of the Protocol, agreement on escalation processes and further clarification on the conditions to avoiding legal actions.

¹⁷ See also Law Reform Commission Consultation Paper on Personal Debt Management and Debt Enforcement (LRC CP 56-2009) at paragraph 5.159 -5.164

Extension of IBF-MABS Operational Model

6.3.5 The Group recommends that the voluntary engagement model of informal debt management operated through the IBF-MABS Operational Protocol be now developed as a template for extension to other credit providers, utility companies, etc, who are concerned with the issue of personal over-indebtedness. In that regard, the responsible Departments and agencies should facilitate an engagement with such non-IBF creditors, etc, so as to bring forward an agreed Operational Protocol similar to that of IBF-MABS.

6.3.6 The Group also recommends that such a new, more comprehensive Operational Protocol, (notwithstanding the future establishment of a statutory non-judicial debt settlement system), could potentially operate as the first, informal, element of that system.

Standard Financial Statement (SFS)

6.3.7 In the context of implementing solutions to both mortgage and non-mortgage related personal debt, the development and central role of an agreed Standard Financial Statement (SFS) is a critical tool. While the SFS is addressed in more detail in the Group's Interim Report, given its critical importance in relation to the assessment of all personal debt cases, the Group recommends that the completion of a SFS should be a mandatory requirement.

Regulation/Licensing of Money Advisors

6.3.8 The Group also recognises that, in the context of the development of new debt settlement arrangements, there may be an increasing role undertaken by debt advisory/management service providers operating for profit. In that regard, the Group notes and welcomes the intentions of the Minister for Finance to provide for the regulation of debt advisors and would advocate the development of a licensing regime to ensure best practice and conduct.

Regulation/Licensing of Debt Collectors

6.3.9 The Group is of the view that the regulation of debt advisors should be a separate and distinct process from the regulation of persons or organisations who are engaged in the collection of debt. The Group recommends that a licensing system, containing a fit and proper person test and covering code of behaviour requirements, be considered for those engaged in the collection of debt. The Group is aware of the media reports of unscrupulous persons becoming involved in this activity and of allegations of threatening or intimidating behaviour. The existing criminal law - the Non-Fatal Offences against the Person Act 1997 - specifically provides for sanctions against such behaviour.

Reform of Bankruptcy Legislation

6.3.10 The Group welcomes the proposals for certain limited reform of the bankruptcy legislation made by the Minister for Justice and Law Reform in the Civil Law (Miscellaneous Provisions) Bill 2010, published on 30 August 2010. These proposals provide, for the first time in Irish law, for an automatic discharge from bankruptcy. While the proposed period of 20 years for automatic discharge is, relative to many other jurisdictions, very lengthy, the Group understands that further reform of the law is likely in this area. The Group also welcomes the proposed reduction in the

application period to the Court for discharge from bankruptcy from 12 to 6 years, albeit with the current conditions continuing to apply.

6.3.11 While not wishing to anticipate the recommendations of the LRC Final Report, the Group is of the view that significant reform is now required in regard to Ireland's personal insolvency regime. Such reform must have the broad objective of bringing about an efficient and cost-effective process for the settlement of arrears of personal debt. The Group would see the reform as consisting of two main parts:

- (i) new and modernised bankruptcy legislation with a less punitive approach, in cases where fraud or culpable negligence is not at issue, to replace the Bankruptcy Act of 1988; and
- (ii) a non-judicial debt settlement and enforcement system which would be an alternative to bankruptcy in most cases.

6.3.12

The rationale for a non-judicial debt settlement system is that it would provide an out of court alternative to debt enforcement procedures where there is no dispute as to the liability and where a debtor who has acted in good faith is insolvent and owes multiple debts. For such debtors the bankruptcy regime may not be appropriate but a formalised debt settlement system would provide the best possible solution for both creditors and debtors in cases of over-indebtedness. There is an incentive for creditors to participate in a non-judicial debt settlement arrangement in that the costs are lower than court proceedings leading to a higher dividend available to creditors. There is an incentive for debtors in that once a specified majority of creditors agree to a debt settlement arrangement there is a specific timeframe for the repayment of debt with the possibility of some 'write off' at the end of the period provided the terms of the agreement are complied with. However, if the terms of the agreement are not complied with there is no facility for any debt forgiveness.

6.4 General Considerations and Features of a Debt Settlement System

6.4.1 The reform of Ireland's personal insolvency law and developing new arrangements that might apply to both judicial (bankruptcy) and non-judicial systems will require a "whole of Government" approach.

6.4.2 The Group, recommends, that the relevant Departments and Agencies concerned bear in mind the following considerations in regard to developing new debt settlement systems, both judicial and non-judicial;:

- (i) General considerations
 - appropriate qualification criteria for entry to a non-judicial debt settlement system;
 - affordability (in regard to costs, fees, taxes, etc), accessibility and ease of understanding;
 - the time limits and conditions that might apply to discharge from a bankruptcy or insolvency process;
 - how an "earned fresh start" and an appropriate future credit rating can be achieved for the debtor who has made all efforts in good faith to comply with the terms of the debt settlement agreement;
 - the protection of the property rights of creditors;
 - the ending of any system of preferential payments to certain creditors, Revenue or otherwise;

- the restrictions that might apply to the person in an insolvency process in regard to engaging in business, obtaining credit or being elected to public office, etc;
 - the development of effective and transparent enforcement mechanisms; and
 - the avoidance of inappropriate incentives for potential misuse of new insolvency arrangements.
- (ii) Specific considerations
- that at least 60% of creditors by value, vote in favour of the scheme;
 - the debt discharge period in a formal debt settlement system should be related to the quantum of debt outstanding; and
 - where a debtor subject to a debt settlement arrangement refuses to abide by the agreement, creditors have the right to pursue other legal remedies, including an application to the court either to have the debt enforced or the debtor declared bankrupt.

6.5 The Mortgage Shortfall and Debt Settlement

6.5.1 The Group, following its consideration of the broad issues involved in regard to mortgage arrears and in the context of reform of our debt settlement arrangements, recognises that:

- a mortgage shortfall debt is crystallised when the property of the former mortgage-holder is sold for an amount less than that remaining on the mortgage;
- in the event of a sale, the mortgage shortfall debt becomes an unsecured debt still owed to the mortgage lender. In all judicial and quasi judicial proceedings, such debt is treated on an equal basis with all other forms of unsecured debt; the mortgage shortfall debt is likely, in cases where a mortgage shortfall co-exists with other forms of unsecured personal debt, to substantially increase the overall quantum of debt outstanding and any debt settlement process must have regard to this factor.

6.5.2 The Group is conscious that many debtors, especially those who have lost their homes, face a difficult situation, and one that can have damaging impacts on all aspects of their lives. It is likely that mortgage shortfalls, and other debts coming under the debt settlement regime could involve large sums of money. The modernisation of debt settlement in Ireland must take account of this and must seek a reasonable balance between the interests of borrower and lender.

6.5.3 We recommend that Government consider carefully the maximum discharge periods for different levels of total indebtedness, having regard to the factors outlined below.

6.5.4 The time period for discharge of the debt under a non-judicial debt settlement mechanism should vary according to the quantum of the debt, with a large quantum of debt having a longer discharge period than a smaller one. The reasoning behind this is as follows:

- (i) even if a debtor quickly recovers their employment or income, the amount of money they could repay per annum is unlikely to permit repaying all, or most, of a large debt within a short period;
- (ii) If the period is extended then there is a far more realistic scenario for dealing with large debts, such as a mortgage shortfall;
- (iii) It is important, socially and economically, that debtors are encouraged to work, earn and live a normal lifestyle; and
- (iv) the debt settlement system should not materially increase, or appear to increase, the risk that debts will not be paid where borrowers are able to do so.

6.5.5 The Group believe that in a debt settlement system debtors should retain a reasonable income, to cover basic living costs, and an appropriate percentage of what they earn above the minimum, and that the time period should not be so long that debtors can see no end to it

6.6 Pensions

The Group understands that a basic principle of personal insolvency law is that a debtor's assets are available to discharge debts.¹⁸ Where a mandatory payment plan forms part of a debt settlement arrangement the debtor's future income is also made available for distribution to creditors. Assets and income would include for example a lump sum pension payment realised and pension income receivable during the period of the debt settlement arrangement. The Group did not consider in any great detail the more complex issue of access to pension funds, which have not matured during the period of the debt settlement arrangement and which would have more long term implications.

¹⁸ Reifner, Kiesilainen, Huls, Springeneer Consumer Overindebtedness and Consumer Law in the European Union (Report presented to the Commission of the European Communities, Health and Consumer Protection Directorate-General Contract Reference No. B5-1000/02/00353)

Appendix 1: Terms of Reference of the Mortgage Arrears and Personal Debt Group

- Having regard to the commitments in the Renewed Programme for Government to protect the family home and help those in personal debt, to make recommendations to the Minister for Finance on options for improving the current situation for families with mortgage arrears and personal debt. Such recommendations to be issued on a rolling basis as appropriate.
- To bring together the latest information held by relevant government departments and elsewhere on mortgage arrears and personal debt.
- To consult with experts both within and outside the Group where necessary regarding latest facts regarding the mortgage arrears and personal debt problem.
- To make recommendations to the Financial Regulator in relation to the Code of Conduct on Mortgage Arrears (CCMA).
- To take account of the proposed Review of the Operational Protocol between the IBF and MABS and to submit observations and recommendations to that Review.
- To examine the state support schemes and to make recommendations as appropriate for improvement having taken into account Mortgage Support Schemes in operation in other jurisdictions.
- To have regard for the ongoing deliberations by the Law Reform Commission on personal debt. In particular, to consider how to reform personal insolvency and bankruptcy regulations and to establish as far as possible how non-judicial settlement proceedings can be formulated.
- To take account of the Report on Indebtedness by the Joint Committee on Social and Family Affairs, together with the ESRI report on negative equity in the Irish housing market.

Appendix 2: International Mortgage Support Schemes

The information in the tables included in this appendix was compiled in April-2010 based on information available at that time. Certain information may have changed since that date.

These tables are set out in the following four pages.

Appendix 3: Comparison with Mortgage to Rent Schemes in the UK

Mortgage to rent schemes have been introduced in a number of other jurisdictions, including England and Scotland. A similar scheme is also under consideration in Northern Ireland. In England, the Mortgage Rescue Scheme (MRS) introduced in January 2009 provides an exit route out of home-ownership for households who, if repossessed, would be in priority need for homelessness assistance. Uptake to date has been quite low. Despite almost 20,000 applications being made under the scheme between Q1 2009 and end Q2 2010, only 629 offers were accepted, with 613 households becoming tenants of housing associations.

The main source of funding for the MRS is the Homes and Sustainable Communities Agency (HSCA). This agency is the principal funder of new social housing in England and is funded in turn by the Department of Communities and Local Government. The current grant rate available to housing associations from the HSCA is 55% of the acquisition price. Households availing of MRS are also required to contribute 3% of the property's value, with the balance (42% of the acquisition cost) being provided by housing associations from their own reserves. It is important to note that the funding position of housing associations in the UK is generally very different to that of approved housing bodies in Ireland. While many housing associations in Ireland would have designated reserves for planned maintenance etc. for work on different estates, generally speaking they would not have the same scale of reserves as their UK counterparts. In essence, this means that any mortgage to rent scheme in Ireland along the lines of those schemes in other jurisdictions would have to rely 100% on Exchequer funding.

The Social Housing Leasing Initiative (SHLI) adopted in Ireland, was extended in September 2009 to allow for the direct provision of dwellings by approved housing bodies. This arrangement, originally conceived as a means of enabling approved housing bodies procure units themselves, either directly from a private owner or by purchasing/constructing units using private finance, which they then make available under the leasing programme to persons in need of social housing support, could also be applied to the acquisition of units from households deemed to have unsustainable mortgages and assessed as being in need of social housing. The Approved Housing Body (AHB) would take ownership of the property which it would then lease to the relevant local authority on a long term basis (e.g. 20 – 25 years) under the SHLI. The household would become a tenant of the AHB, paying a differential rent, calculated on the basis of their ability to pay. The local authority would provide a payment under the leasing initiative to the AHB which could then use this stream of funding to service the borrowing costs incurred in acquiring the property.

In order for this approach to achieve value for money (relative to other social housing delivery mechanisms) and not result in the inequitable treatment of other households in need of social housing, costs must be fully met within the existing social housing leasing framework. This requires that the costs incurred by the AHB (the borrowing costs as well as the ongoing costs of management and maintenance) must be met from a payment that is based on market rent. In light of ongoing volatility in financial markets and the impacts of this on funding costs, the scope for mortgage to rent is limited at present but may have greater potential in the future if funding costs ease. The Department of the Environment, Heritage and Local Government has indicated to the Group that it is open to receiving proposals from approved housing bodies for mortgage to rent cases within the overall SHLI mechanism.

Country	Ireland	Ireland	Ireland	Ireland	Ireland
Scheme	Mortgage Insurance Supplement (MIS)	Shared Ownership Loan	Mortgage Allowance Scheme (tenant purchase scheme)	Affordable Housing scheme	Home Choice Loans (HCL)
Year			2009	2000	2009
Administration	Social Assistance; Government;	Social Assistance; Local Authorities, Government	Social Assistance; Local Authorities, Government	Social Assistance; Local Authorities, Government	Local Authorities, Government
Types	Interest Support	Purchase scheme	Purchase scheme	Purchase scheme	Purchase scheme
Eligibility	Must have been able to afford initial mortgage repayments; home is not for sale; subject to not exceeding what the HSE considers reasonable residential needs. No contributor to the mortgage can be in full time employment (>29hrs)	Income < €40,000 (single) or <€100,000 (couple). Registered on a housing waiting list with local authorities or in local authority tenants	Income < €28,000; Mortgage > €38,093.	First time buyer; employed for at least 12 months. The properties offered are available at prices significantly lower than the market value, with affordable prices currently ranging from €165,000 to €235,000 depending on the area in which one is purchasing.	Must be FTB purchasing a new build or building their own home.
Conditions	Assistance is only available on the interest section of the mortgage; interest is calculated as gross monthly interest less mortgage interest relief, mortgage allowance or subsidy payable towards the interest element by local authorities.	Max allowance = €220,000; must purchase < 40% of the property; must have bought out local authorities in 30yrs	Max allowance = €11,450 payable over 5yrs. The allowance may not exceed mortgage repayments. Not eligible if participating in the Shared Ownership scheme	Income < €55,000 (single) or €75,000 (couple) Savings < €3,000. The claw back is quite simple: when you sell your home, you repay to the Council a percentage of the sale price and this is known as the claw back. This percentage is directly linked to the initial discount that you received when you purchased your home	It will provide up 92% of the market value of the property. Max loan = €285,000; normal Capital & Interest bearing mortgage; Max term = 30yrs; earning >€35,000 (single) or €45,000 (couple)
Assistance	Short-term allowance, with special retention arrangements where gross earnings from returning to work are < €317.43 per week	Mortgage payments are made on the portion of the home being bought, while rent is paid to local authorities for the rest at 4.3%	The allowance is paid directly to the mortgage provider, with repayments reduced accordingly for the first 5 yrs of the mortgage	FTBs receive a discount on the cost of their mortgage subject to their income	Local Authority loans

Country	Ireland	UK	UK	UK	Scotland
Scheme	Mortgage Interest Relief	Support for Mortgage Interest (SMI)	Homeowner Mortgage Support (HMS)	Mortgage Rescue Scheme (MRS)	Mortgage Rent
Year	Ending 2017	2009	2009	2009	2003
Administration	Revenue; Government	Social Assistance; Government;	Social Assistance; Government;	Social Assistance; Government;	Social Assistance; Government;
Types	Tax relief scheme	Interest support	Short-term government loan	Mortgage to rent	Mortgage to Rent
Eligibility	All new mortgage holders, including mover mortgage households	Need to be a homeowner and you should be claiming Income Support, Job Seekers Allowance or an income related Employment Support Allowance.	Households who have experienced a temporary loss of income and do not qualify for SMI.	It targets those families with dependent children, elderly, pregnant woman & those with physical or mental disability & illnesses.	Need to live in an area; in danger of repossession, can't trade down locally.
Conditions	Current rates: Non-FTB 15% relief; FTB 25% in yr 1&2; 22.5% yr 3-5; 20% yr 6&7; 15% on subsequent relief.	Satisfy means tests and have suffered a loss in income.	They must be owner-occupiers, and have been making regular payment to their lender in the last five months. Outstanding mortgage value of less than £400,000, and savings of less than £16,000.	To qualify for the mortgage to rent option the claimant must have a mortgage LTV of between 75 and 95 per cent. For the shared equity scheme the LTV requirement for this option is at least 75 per cent.	Max Price = local average; Max Capital (exc. House) = £8,000 (£12,000 if 60+) Outstanding repairs under £6,000
Assistance	Mortgages: 1 Jan04 - 31 Dec11 will continue to qualify for MIR end of 2017 at current rate. Mortgages: 1 Jan12 - 31Dec12, there will be a 15% rate of relief for FTB and a 10% rate for non FTB. max = €6,000 (married)& €3,000 (single) Mortgages after 1Jan13 will not qualify MIR will be abolished after 31 Dec '17.	2 yr limit on payment of mortgage interest.	Shared appreciation mortgage accrues interest at 5% with payments deferred & not payable until 5 yrs after the loan is made.	Mortgage to rent scheme the properties will be sold (or bought back) in 8yrs; shared equity scheme properties will be sold or bought backup to 5yrs	Subsidy to allow landlords to repair & purchase property

Country	Spain	Netherlands	Netherlands	Canada	New South Wales
Scheme	Subsidized Owner-occupied Dwellings	National Mortgage Guarantee (Repossession Insurance)	Mortgage Payment Facility (WLF)	Mandatory Mortgage Insurance	Mortgage Relief scheme (MRS)
Year		1993		1954	1982
Administration	Social Assistance	non-profit foundation; local & central government backing	Assessment by Mortgage Providers	Government	State Housing Department; Government
Types	Purchase scheme	Default insurance	Forbearance	Default insurance	Interest free loan
Eligibility	Low- middle income household	Total Mortgage costs <€350,000; Household finances total purchasing price; HP on new build max=€324,074; HP existing house max=€312,500	This scheme allows households to add their payment arrears onto the principal outstanding on the mortgage; Mortgage Providers decided the amount the household can pay during the period of reduced income.	According to the federal bank act, every mortgage from a federally regulated institution with a down payment of less than 25% is required to carry mortgage insurance.	Client must suffer unexpected loss of income.
Conditions	Dwellings may not be sold in the initial yrs of residency; once the qualification period expires the property becomes part of the normal housing stock	max loan €265k; Interest rate reduction up to 0.6% ; One-off tax deductible fee =0.45% of mortgage amount	to a max. value of 9% of the total mortgage sum; once income is restored the mortgage lender will agree a new repayment schedule	Premium on insurance varies though an up front cost also applies on the scheme. However many banks take that payment over the first few years of the mortgage.	Mortgage <\$350k; home <\$500k Payments after income loss >36% gross income & before income loss >27% gross income. Max income \$90k
Assistance		Guarantee pays residual debts after foreclosure;	This scheme allows households to postpone some of their mortgage repayments on a temporary basis.	Assistance and guidance to the private sector in the building, design and planning of houses is provided. Provisional governments have aligned their housing standards and planning practices along those of the CMHC	Interest free loan paid to lender; sometimes loans become grants or are written off

Country	USA	USA	USA	USA
Scheme	Housing Affordability Modification Plan (HAMP)	Home Affordable Foreclosure Alternative (HAFA)	HFA Hardest Hit Households	Principal Forgiveness Scheme (Bank of America Corp.)
Year	2009	5 April 2010 to 31 Dec 2010	Feb-10	2010
Administration	Combined lending institution & government scheme	Combined lending institution & government scheme	Government	Bank of America Corp.
Types	Forbearance	Vacating property without foreclosure proceedings	Fund for distressed households	Principal Forgiveness Scheme
Eligibility	Borrower is delinquent on their mortgage or faces imminent risk of default; property is primary residence; mortgage originated prior to 2009; principal outstanding < \$729,750	Principle residence; first lien originated before 2009; Mortgage delinquent or default is reasonably foreseeable;	Initial scheme included States where HP declines >20%; Extended scheme funding goes to states with highest share of population living in counties in which unemployment >12%	LTV> 120%; with a max reduction of 30% of principal outstanding - this is because on average a bank will loss approx one-third of the property value in foreclosure proceedings.
Conditions	Refinance mortgages with LTVs < 105%; to a serviceable monthly repayment with a debt-to-income ratio of 31%; term on mortgage extended to 40 yrs	Unpaid principal balance no more than \$729,750; total monthly repayments > 31%; title deeds must be free & clear of mortgage liens & encumbrances.	Fund used for: Unemployment Programs; mortgage modification; mortgage modification with principal forbearance; Short sale or DIL; Principal reduction programs for borrows in severe neg equity; second lien reductions	The program targets three mortgage products that were popular during the housing boom: subprime loans; payment-option mortgages with negative-amortization features; and "2-1" adjustable that offered teaser interest rates for the first two years, then adjust each year.
Assistance	Reduction in Interest; Extended term of loan & provided principle forbearance; Add back arrears to the back of the loan; Guarantees lower repayments for 5yrs	\$75bln program provides additional options to avoid foreclosures. It offers incentives to borrowers, services & investors who utilize a short sale or DIL; (1)\$1,500 to borrower relocation; (2)\$1,000 for admin & costs; (3)RMBS investors subsidised to a max of 3% of unpaid principal.	1st HFA up to \$1.5 bln (Feb 2010) for Nevada, California, Florida, Arizona, Michigan; The subsequent HFA up to \$600m (April 2010) for North Carolina, Ohio, Oregon, Rhode Isl, South Carolina.	phased in principal forgiveness as the first step towards keeping underwater households from foreclosure.

Appendix 4: Membership of Group

List of Group Members	Organisation
Mr. Hugh Cooney (Chairman)	KPMG
Mr. Brendan Burgess	Independent Consultant
Dr. David Duffy	ESRI
Mr. Matthew Elderfield	Head of Financial Regulation, Central Bank
Mr. Pat Farrell	Irish Banking Federation (IBF)
Mr. Tom Foley	Independent Consultant
Mr. Paul Joyce	Free Legal Advice Centre (FLAC)
Ms. Patricia T. Rickard-Clarke	Law Reform Commission
Dr. John Thompson	Department of Finance
Mr. Brendan Fox (Group Secretary)	Department of Finance
Mr. Niall O'Sullivan	Department of Finance
Mr. Declan Keane	Department of Finance
Mr. Philip Nugent	Department of Environment, Heritage, and Local Government
Mr. Brendan Mac Namara	Department of Justice and Law Reform
Dr. Orlaigh Quinn	Department of Social Protection
Mr. John Shaw	Department of the Taoiseach
Mr. Stephen O'Connor	Special Advisor to Eamon Ryan TD, Minister for Communications, Energy and Natural Resources