General Assessment of Consumer Protection (Regulation of Credit Servicing Firms) (Amendment) Bill 2018 (Private Members Bill)

The Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach has requested a general assessment of Private Members Bill Consumer Protection (Regulation of Credit Servicing Firms (Amendment) Bill 2018 (the "Bill"), to include the Department's views on the policy rationale for the Bill, and the various technical, legal and drafting aspects of the Bill. The purpose of this general assessment is to inform the Committee in its decision-making regarding scrutiny of the Bill.

This Bill was introduced on 21st February 2018 by Deputy Michael McGrath. It is the Department's understanding that Deputy McGrath does not believe that pre-legislative scrutiny is necessary in relation to the PMB.

Under Standing Order 149(3), it is a matter for the Committee to consult with the European Central Bank.

1. Policy Rationale and Implications

The Government agreed to support the Bill and work with Fianna Fáil and Deputy McGrath to develop appropriate amendments to the Bill so that it can be implemented as a matter of priority. The Department has ongoing engagement with Fianna Fáil to discuss the Bill. Government approved the drafting of amendments by the Office of the Parliamentary Council and work on this has commenced. The Department is also engaging with the Central Bank of Ireland on the issues arising from the Bill.

Broadly, the Bill proposes that owners of credit, regardless of their current location, be required to be regulated by the Central Bank of Ireland. However, notwithstanding the well-intentioned overall objective of the Bill, the Bill as drafted gives rise to a number of operational and administrative difficulties for the Central Bank.

Central Bank authorisation requirements insist that a regulated firm be capable of supervision in Ireland by the Central Bank and require that effective control of the firm is based in Ireland. Therefore a foreign based firm may be required to establish a decision making presence in Ireland which takes control of the Irish business. We have yet to bottom out the legal challenges that this may present, including for owners based in another EU country and whether these may be different from owners based outside the EU.

If a loan owner decided not to seek authorisation, it is unclear what the effect of this would be. It is an offence under the Central Bank Act 1997 to carry on a regulated business without authorisation and significant fines may be imposed. Furthermore, it may be that a court would prevent repossessions by such a firm but this is not certain.

Leaving aside the question of future loan book sales, the position of existing owners also requires careful consideration. In framing legislation, it is incumbent on the Oireachtas to make sure that it can be given practical effect and that the consequences of non-compliance are clear to all stakeholders.

The Bill also presents challenges for the Central Bank as it will require the Bank to supervise entities which up to now did not have a physical presence in Ireland and were not required to have such a presence.

In terms of conflicts with the Central Bank's existing statutory functions, the proposal could impact on the Central Bank's objectives with regards to the regulation of the financial sector, which includes stability of the financial system and the proper and effective regulation of financial institutions and markets, while ensuring that consumers of financial services are protected. The Bill could be seen as interfering with the independence of the Central Bank in the sections that impose requirements on it such as section 8 and 12.

Legal drafting is a complex technical task and requires absolute clarity of the detailed intention behind legislation in order to fully capture what is intended and to avoid unintended consequences.

2. Technical, legal and drafting aspects

The Committee has asked for the Department's views on the various technical, legal and drafting aspects of the Bill. As mentioned above, the substance of the Bill will require an in-depth review by all relevant stakeholders to understand the implications of the changes being suggested. A number of amendments will be necessary to make the Bill practical to implement. We are working to ensure that the Bill will achieve its intentions without creating unintended consequences.

The Bill seeks to require that all owners of credit in Ireland would be regulated by the Central Bank. It is fair to say that there are significant issues that need to be addressed and it must be noted that some of the proposed measures would have broad ranging implications.

<u>The value of loan sales may drop due to the cost of becoming regulated and a possible reduction in competition, if the number of operators in the market falls.</u>

Regulation will involve costs including renting or buying a business place of operation in Ireland, employing staff in the country, and familiarisation with local laws and methods of operating to ensure compliance with the new regulations. Requiring regulation may also become a barrier to entry to the Irish loan sales market. If a private equity firm decides the costs involved in being regulated, and potentially having to set up a base in Ireland, are too high, they may decide not to bid on any upcoming loan portfolios, which the banks advertise for sale. This may lead to less potential investors bidding on a loan book. With a lower number of investors, the bids being made may also be lower. This has the impact of a lower value being achieved by the banks in their sale, meaning in conjunction with that, that they have less funds available for other borrowers who may approach them for business, such as new mortgage sales.

The cost to the borrower / tax payer may increase

As the value of loan book sales received by the banks may drop and the cost of being regulated in Ireland increases for private equity funds, the borrower and tax payer may suffer financially from this. Borrowers may have to pay higher interest rates to banks if banks have less funds to lend. The tax payer may suffer also due to the reduction in the value of the banks in which the State has shares.

The Bill could have unintended consequences for securitisation

The Bill, as drafted, appears to intend to exclude securitisation in section 9. However, the current definition of "credit agreement owner" would include many securitisation vehicles. Securitisation will need to be described in a manner which prevents loan owners from structuring themselves so that they fall outside of the scope of the act. Securitisation must be treated with due care and attention. Fianna Fáil have acknowledged that they do not want to capture securitisation in its current form within the Bill.

There may be issues with European law and the provision of services throughout the Union from implementing this Bill in its current format

As part of the European Council NPL Action Plan, the European Commission has launched a proposal for a European Directive on the authorisation of credit servicers which will have to be carefully reviewed.

The current situation in Ireland is that credit servicing firms are regulated, these are the firms that deal directly with the customers.

The Commission proposal sets common standards to ensure proper conduct by and supervision of loan purchasers and credit servicers across the Union, while allowing more competition by harmonising market access rules across Member States. The Directive provides that credit servicers authorised in a Member State can provide their services across the EU provided they are in compliance with the Directive.

The proposal has limited rules for credit purchasers including that they have to employ an EU regulated credit servicer, have an EU based representative (if non-EU) and notify regulators of enforcement action. The proposal, if implemented, would not allow any Member States to impose additional rules on credit purchasers beyond those provided for in the proposed Directive. This would be problematic in that the proposals in the Bill would impose additional rules on credit purchasers that may have to be rolled back in the future if the Directive, as proposed, is adopted.

2.1 Possible impact on existing and potential investments

- The Bill as drafted could inhibit investment in this market of the financial sector, particularly given the broad and non-specific definitions used.

Existing investments

- Companies currently operating in the Irish market may be negatively impacted by this Bill. Having understood that they did not require authorisation to operate in the Irish market, they may now find that they do need authorisation and may need to change their business model. The Bill may lead to uncertainty as to what information needs to be provided to borrowers and the imposition of additional administration may lead to additional costs for these companies.

Potential investments

- Potential investors in this market may be discouraged from investing due to the additional administration charges which may develop and the potential that they may need to set up headquarters in Ireland.
- The financial institutions who need to sell loan portfolios may find that the value they achieve for loan book sales is lessened as a result of this Bill, due to the potential that fewer investors will be in the market place in Ireland as a result of the Bill. If this happens, there could be a negative impact for the taxpayer and the borrower.

2.2 Potential implications for Ireland's economy

- As outlined above, the Bill may have adverse implications for potential future investments by private equity firms in the financial services area.
- Irish banks may suffer from lower returns on loan sales in the market place as a result of this Bill.
- In addition, there would be an economic impact both in terms of the revenue lost to the tax payer via the banks lower value of sales, and through the possibility of a higher cost to the borrower, who may find themselves carrying further financial burdens as a result of this.
- Securitisation vehicles, used by the banks and others with regards to loan sales, may be at risk of being regulated, which would be an unintended and unwelcomed consequence of this Bill. On the other hand, caution must be taken that securitisation is not made into a loophole for private equity firms to use in avoiding regulation.

3. Existing legislation in relation to Consumer Protection in banking

3.1 Existing commitments

The Consumer Protection Code 2012, the Code of Conduct on Mortgage Arrears, the European Union (Consumer Mortgage Credit Agreements) Regulations 2016 and the

Consumer Credit Act 1995 are in place to protect consumers. Collectively these ensure that regulated financial service providers treat consumers properly and fairly.

Under the Central Bank's Consumer Protection Code, a regulated financial institution must act honestly, fairly and professionally in the best interests of its customers and the integrity of the market. Furthermore, the Code requires a regulated financial institution to make full disclosure of all relevant material information including all charges, in a way that seeks to inform the customer.

The Code of Conduct on Mortgage Arrears (CCMA) forms part of the Central Bank's Consumer Protection Framework. It is a statutory Code and has evolved to reflect the changing times and situations which have arisen in the area of consumer protection.

For example, an Addendum to the CCMA was published to take account of the Consumer Protection (Regulation of Credit Servicing Firms) Act 2015 which stated that with effect from 8 July 2015, credit servicing firms, as defined in the 2015 Act, must apply for authorisation to the Central Bank and that the CCMA 2013 would apply to these firms.

The CCMA is aimed specifically at the process to be followed by relevant firms, to ensure borrowers in arrears or pre-arrears in respect of a mortgage loan secured on a primary residence are treated in a timely, transparent and fair manner. A key element of the Central Bank's role is ensuring that the consumer protection regulatory framework is fit for purpose so that consumers' best interests are protected. The Central Bank have been asked to carry out a review of the CCMA to ensure it remains as effective as possible and for the review to be completed as soon as possible.

3.2 Alignment with Government policy

The Bill was introduced on 21st February and passed Second Stage in the Dáil on 06th March.

The Government agreed to support the Bill and work with Fianna Fáil to develop appropriate amendments to the Bill so that it can be implemented. The Department has met with Fianna Fáil to discuss the Bill and is currently engaging with the various stakeholders and the Attorney General's Office in relation to the drafting issues which this Bill poses.

On 05th June the Bill was assigned to an experienced drafter in the Office of the Parliamentary Council in the Attorney General's Office and correspondence with her has commenced.

The Department will be meeting with the Central Bank shortly to discuss the optimal approach for the regulation of loan owners.

The Department also anticipates meeting with Fianna Fáil shortly to progress the proposed amendments.

At EU level the Department has committed to seek to align the European proposal with the Bill.

Conclusion

In summary, therefore, the Bill could have much wider, unintended consequences, as currently drafted. It will require substantial redrafting at Committee Stage, as well as more in-depth analysis of its potential wider implications, particularly amidst the complexity of regulating private equity funds whilst ensuring securitisation can continue without being a loophole for any new legislation. This will take time and involve a number of relevant stakeholders.

In managing policy priorities, we must legislate cautiously so as not to raise any unintended consequences. It may be that the Bill, with its technical drafting challenges, could inhibit loan sales as and when necessary.

In considering this Bill, and the next steps to be taken, we have also taken into account the Consumer Protection (Regulation of Credit Servicing Firms) Act 2015, and the Code of Conduct on Mortgage Arrears which provides support and protections to consumers.

As it stands, both Central Bank codes such as the Code of Conduct on Mortgage Arrears and the Consumer Protection Code continue to apply when loans are sold. These Codes apply to all regulated entities in Ireland and credit servicing firms are regulated by the Central Bank of Ireland.

As things stand, an unregulated owner must use a regulated credit servicing firm to administer its loan book in Ireland and therefore all Codes apply. If an owner does not appoint a regulated credit servicing firm, then the owner itself must be regulated.

Furthermore, an owner cannot instruct a regulated credit servicing firm to do anything which would be a breach of financial services legislation, including the Codes. Even if the owner did issue such an instruction, it would be illegal for the credit servicing firm to implement it.

We must be careful that any actions we take to further protect borrowers whose loans are sold do not have unintended and very negative consequence for the banks, their relationship with the regulator and all our citizens who depend on a functioning banking system in their day to day lives.

It is our understanding that Deputy McGrath does not believe that pre-legislative scrutiny is necessary in relation to this Private Members Bill.

Department of Finance

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