AN ARD CHÚIRT
(The High Court)
BAILE ATHA CLIATH 7
(Dublin 7)

24th October 2023

Re: Directive (EU) 2021/2167 on Credit Servicers and Credit Purchasers
<u>The New EU Mortgage Moratorium on Repossessions</u>

To all TDs and Senators,

A Chairde,

Your staff are frequently asked for advice and help in regard to mortgage arrears on their housing loans. Legal aid is not available to distressed borrowers in court and an obvious inequality of arms blights all *"repossession"* proceedings. How any litigant *"in person"* can be expected to be familiar with inaccessible provisions in EU Directives or Amendments thereto, which are even less accessible, or Irish Statutory Instruments, is beyond me.

You should be aware that, as of end December, the above Directive will have been transposed into Irish domestic law by a Ministerial Statutory Instrument to be signed by Minister Michael McGrath.

In part, that Directive (which deals primarily with Central Bank regulation of credit servicers and credit purchasers) also amends the 2014 Directive on Mortgage credit to require that mortgagors in distress be provided with helpful options *"before foreclosure proceedings are initiated"*. Effectively this imposes a new moratorium to enable "creditors to make efforts to exercise, where appropriate, reasonable forbearance." Article 28 of the 2014 Directive, as now amended by the 2021 Directive, now reads:

> *Member States shall require creditors to have adequate policies and procedures so that they make efforts to exercise, where appropriate, reasonable forbearance before foreclosure proceedings are initiated. Such forbearance measures shall take into account, among other elements, the Consumer's circumstances and may consist of, among other possibilities:*
>
> *(a) A total or partial refinancing of a credit agreement;*
> *(b) A modification of the existing terms and conditions of credit agreements, which may include, among others:*
> *i. extending the term of the agreement;*
> *ii. changing the type of credit agreement;*
> *iii. deferring payment of all or part of the instalment repayment for a period;*
> *iv. changing the interest rate;*
> *v. offering a payment holiday;*
> *vi. partial repayments;*
> *vii. currency conversions;*
> *viii. partial forgiveness and debt consolidation*

The Land and Conveyancing (Amendment) Act 2019 (the "Boxer Moran" Act) introduced the yardstick of "proportionality" into the court's "repossession" jurisprudence. It also required the court to weigh a Defendant's counterproposals. Building on the Act, and at the request of "Dublin Gazette," in December 2019, I put together some model alternatives to repossession, each with a user-friendly acronym, including the "Extended Redemption Option" (ERO); the "Portable Trade

Down" (PTD); the "MTR Put Option"; the "Bailout Carried Forward" (BCF); and the "Court Managed Receivership" (CMR). (I didn't charge any fee for this, obviously!). (see appendix)

Also active on the side of distressed borrowers, Deputy Michael McGrath, now Minister for Finance, introduced the Consumer Protection (Regulation of Credit Servicing Firms) Bill, which was passed in 2018, and which brought the Central Bank into the dynamic as a watchdog. And now, three years Later, we have the EU's Europe wide Directive, (2167 of 2021), underpinning and reinforcing that regulatory objective and extending regulation to so-called credit "purchasers", shadow bank entities which have bought the loan portfolios of the retail bank "loan originators". In turn, these entities, "orphaned" SPVs owned by "charities" (believe it or not), act as intermediaries and float the receivables to RMBS (residential mortgage-backed securities) investors in the capital bond market.

<u>From "encouraging..." to "requiring" creditors...</u>

Amendments to Directives are big news. Brussels means business on this one, clearly.
The debt forbearance measure in the original 2014 Directive required Member States to "adopt measures to *encourage* (my emphasis) creditors to exercise reasonable forbearance, etc...." but this has now been firmed up to read "Member States shall *require* (my emphasis, again) creditors to have adequate policies and procedures so that they make efforts to exercise, where appropriate, reasonable forbearance before foreclosure proceedings are initiated."

Perhaps I should also have added emphasis to the word "before" in the provision quoted above. Creditors now have to press the "pause" button on court action.

Clearly, the new moratorium is not open-ended, but neither is it time limited. The court will decline to entertain any "foreclosure" (collateral recovery/"repossession") claim unless it is satisfied that the "efforts" have been conducted with due regard firstly, for the EU's Charter of Fundamental Rights, and then also to some, if not all, of the loan modification measures (including partial forgiveness) listed in the Directive.

<u>Credit Servicers</u>

Some of you will recall that in the past housing loans were secured by the borrower handing the title to the house to the lender, retaining the right to redeem by repayment. But in 2009 we streamlined that business by substituting a legal charge on the house in place of the old mortgage though, confusingly, retaining the terminology. The borrower's title was then subject to the lender's charge but he remained the legal owner.

But then came a revolution in banking. Lenders started to fund the consumer loans by themselves borrowing *"securitising"* from the capital markets. In turn, these funds regularly remortgaged their portfolio of loans raising further capital by "leveraging" from the capital markets and collateralising these funds by the old fashioned mortgage involving a transfer of title of loans to the capital market funder.

We have had the term *"credit servicer"* in legislation for nearly ten years now, but the term *"credit purchaser"* now appears for the first time (to my knowledge). What many do not realise is that the retail mortgagee who advances the home loan (the *"loan originator"*) holds title to the loan for only as long as it takes him to sell on the credit to an unregulated *"credit purchaser"*. This is first stage, "securitisation". Sometimes the process of commodification proceeds further, and ownership of the risk and collateral can become fragmented amongst many investors.

For this reason, management and administration of the loan contract of the borrower is contracted out to a credit servicer. And more often than not, it is the loan originator who undertakes this role. (This can cause confusion for the borrower. Seemingly, also sometimes for the loan originator!)

It's surely clear that *only* the party which is entitled to possession of the house is entitled to seek a possession order. No one else. A recent portfolio sale of Ulster Bank loans was reported as a purchase by AB Carval *("through a vehicle called Elmscott Property Finance")* and that the new owner *"has enlisted loan servicing firm Pepper Finance to manage the loans as legal title holders"*. (Irish Times 6th September).

You cannot be the *"legal title holder"* of the mortgage charge unless you are the owner. The credit servicer doesn't have ownership; it just has a contract for services. As loan originator, he was owner of the mortgage once but, after a "true sale" securitisation, did the credit purchaser assign even the legal title back to the servicer? Even an equitable assignment? I can't find it.

A new species of unregistrable burden? An unregistered burden on a registered burden? How "conclusive", then, is the Register? (Lord Denning once complained about what he described as "*the welter of registration*". One can see why).

Nor is the servicer the *beneficial* owner "in due course". That interest clearly now belongs to the loan note holders joined in the "true sale" purchase of the portfolio.

This process of "securitisation" is certainly confusing, but only when it becomes necessary to *"foreclose"* the mortgage (a process known in financial circles as "collateral recovery"). The party entitled to possession is the party whose capital is at risk. In accountancy terms, on whose balance sheet does the charge appear as an asset? (NB. If it's on your balance sheet and you're not the registered owner, you've got a problem!

In order, presumably, to expedite prosecution, many of the credit servicers have falsely represented themselves as owners of the loans. The existence of funders who are the true owners is concealed from the courts. In the case of Housing Loans, Section 97 speaks of possession orders at the application of mortgagees. By implication, a possession order is *unavailable* to any other applicant, Credit Servicers are not mortgagees.

The Directive is also clear on the point. A new provision, Article 28, paragraph 1(a) is now to be read into the 2014 Mortgages Directive to the effect that *"In the event of an assignment to a third party of the creditor's rights under a credit agreement, the consumer shall be entitled to plead against the assignee any defence which was available as against the original creditor."* Obviously, the EU Commission so provided because the law expects the third party assignee, the *"credit purchaser,"* as owner, to be the Plaintiff in possession proceedings, and no one else.

My Take

After securitisation, the loan originator becomes the credit servicer. Not a problem. Just don't tell the PRA the charge has been sold on. And don't tell the Court it's been sold on.
Say: *"I'm registered as owner"* (the truth: that's what it says on the register of title), but don't say: *"I'm not the owner"* (the whole truth).

Then, instead of selling as mortgagee in possession ('cos you're not the mortgagee anymore, just the servicer), get a possession order from the Court in your own name and use that as your title document. You could then sell the order itself (sic) or evict and sell the property "with vacant possession." Remit the proceeds to the credit purchaser.

And, of course, the shortcut is equally convenient for *performing* loans because the credit servicer, persisting in his charade as mortgagee, can give good (bad) discharge by endorsing receipt on the deed. No need to bother the (offshore) credit purchaser, even though the relevant Statutory provisions have not been complied with.

The legal charge can be listed as a "burden" on the folio registering ownership of the land but, as confirmed by the retired Deputy Registrar, John Deeney, in his comprehensive book, at page 142: *"Registration of a charge as a burden on registered land is not evidence of its ownership, it is evidence only that the charge is an encumbrance on the estate of the registered owner."*

Claims to ownership of the charge, when made by credit servicers registered as owners, must be rejected as fraud. *"Mere entry will not, of course, give validity to an invalid claim."* In reality, their validity is never challenged or adjudicated, largely because the name it bears is that of the original lender even after it had morphed into a credit servicer without title to the charge, and the change has not been notified to the Register. It is a *"conveyancers' artifice"* and involves several prosecutable offences, not to mention, when the case comes to court, clear perjury in the failure to tell not just the truth but the whole truth regarding ownership.

This topic has also struck the Supreme Court as one which demands full debate but, of course, the Court can (perhaps frustratingly) only deal with the issues which arise in those cases which arrive in its list. Actually, members of the Court have effectively signalled that they are on the lookout for a suitable case. In a "Determination" declining to entertain an appeal, on other grounds, in Pepper v Jenkins 2020 IESC DET 118, the Supreme Court noted as follows:

"The Court does not exclude the possibility that, in a suitable case, the entitlement of the transferor of the beneficial interest in a security who retains the legal title to seek an order for possession might meet the constitutional threshold but the present application does not raise that issue."

This may be ominous news for credit servicers. It also suggests that s.31 of the Registration of Title Act is no longer fit for purpose. That Act dates back to a time when mortgages were not collateralised. "Owner"? There is no point in being the registered "owner", if only the beneficial owner can sue for possession. There is nothing to be gained from the (misplaced in my view) reading of the section to the effect that the registered "ownership" is presumed to be "conclusive". Conclusive of what? Forget about s.31. Prove your title the old way. The registered ownership doesn't cut it.

These are technicalities (apart from perjury, which is, to my mind, foundational) and one can understand why courts have long upheld the moral hazard viewpoint and are loathe to refuse a lender the orders he seeks against a defaulting borrower when a societal lynchpin might be destabilised, but two wrongs don't make a right.

"Unfair" terms: negative clearance

It is in consumer contracts (contracts of "*adhesion*" – take it as you find it) that terms unfair to the consumer are most likely to be found. They may even be considered to be unfair if the small print language is unintelligible.

The court will not look at contract terms which have been "individually" negotiated (or at core terms, the main subject matter, the price etc., which are "in plain intelligible language"). Only at terms ("of adhesion") which are the same for all customers. Any non-negotiable term may be determined to be unfair where, *"contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations under the contract to the detriment of the consumer."*

The scope of the review of these terms includes "all circumstances attending the conclusion of the contract." Terms which were not individually negotiated might still be nuanced. A.I. might not pick it up. All contractual terms are factually contextualised. Interpreting them, on the balance of probability, involves judgement of evidence, and preferably not relying (hilariously) on the oath as quality control of evidence of code compliance. Commenting on the Judicial Review test of "substantial evidence" supporting an agency's finding, (Universal Camera 340 U.S. 474 1931), Mr. Justice Frankfurter said that *"It is not permissible for courts to determine the substantiality of evidence without taking into account... whatever in the record fairly detracts from its weight."*

The circumstances include, of course, Consumers' reliance on what is said to them. *"If they can be induced to part with money by claims and promises, and the seller can then simply disclaim responsibility on the basis of "variation clauses," the scope for "bad faith" is clear."* (OFT Bulletin 5). But the OFT also noted that "there may be no unfairness in a term that enables a supplier to change prices only in line with an independent published index."

The current rate changes being demanded of mortgagors by the non-bank funds need to be examined in regard to fairness/unfairness of price changes during the term of the contract. I haven't yet seen any breakdown of these *"credit purchasers"* cost of funds in the capital market. They are not tracked to ECB bank rates. Yet, to be fair, the formula used to measure interest chargeable is supposed to be clear.

Changes to interest charges "not fairly related" to the credit purchaser's cost of funds (including so-called "price gouging" by non-bank mortgagees) may be found to be unfair and unenforceable (on a case-by-case basis). In 2020 the Supreme Court looked in passing (*"obiter"*) at interest charges imposed *after a default* and thought it "likely" that rates "not fairly related" to the costs of the lender would be found to be an unfair "penalty".

It is unusual to find an *obiter* to the effect that a particular outcome is "likely". On the authority of that judicial comment, I say that it is "likely" that the courts will need open book access to credit purchasers' business accounts when interest charges are hiked because of (alleged) underlying "cost of funds" inflation.

Own Motion Assessment

There is strong institutional resistance to the obligation imposed on the courts to scan consumer contracts and satisfy themselves that the terms are not unfair, even in cases when neither party requests the court to do so. Lawyers strive to draft written terms which are certain and binding and the notion that a subset of contracts – consumer contracts – might be uncertain (or might operate "*unfairly*") is counterintuitive to the judges.

This push back was, perhaps unwittingly, aided by a section of the Consumer Rights Act which reproduced a distorted version of the EU Law principle. Section 13b provided an escape clause. It provided that the obligation *"shall not apply* unless (my emphasis) *the courts consider that it has before it sufficient legal and factual material to enable it to determine whether the term is unfair."* An easy opt out for a judge? No sanction for the opportunistic Plaintiff who omits key documents in order to game the system?

My reading of EU case law suggests a much firmer obligation. In SPV Project 1503 (Case C – 693/19) the ECJ found that *"effective judicial protection* necessitates (emphasis added) *that the court hearing the proceedings is able to assess whether the contractual terms are unfair*." I read that as a direction to the national court to make the appropriate arrangements to ensure its ability to assess, failing which the claim should fail.

In my view, any case involving a consumer contract must be deemed to be a "*contested*" case *ipso facto*, and court rules require it to be placed in the Judges' list. It's also clear from that ECJ judgment that the suggestion that the County Registrar could do the negative clearance of terms instead of placing the case in the Circuit judge's list is not a runner. It's a task for "the court hearing the proceedings," not a quasi judicial court officer (who, *"while not expected to give detailed written rulings, should always give the gist of the reasons for a decision."*).

Another standard contract term, the "transfer of rights" clause, the contractual entitlement of a lender to sell on all or any part of the *security* (emphasis added) without notice to the borrower, *"the Appellants have not given any indication as to how the clause in this case could be found to have been unfair to them."* piqued the interest of the Supreme Court (*Pepper Finance v Cannon [2020] IESC 2*), who noted that Does this not suggest that the Supreme Court would welcome an opportunity, in another case, to delve into this issue also? (The Supreme Court specifically referred back to a 2011 judgement of Judge Peart in which he rejected an unfair contract terms challenge on this issue on the basis that such clauses *"are neither unusual, mysterious nor unlawful."* No mention of "fairness." Perhaps trial judges need to look more closely at contract terms.)

Access to Justice

Writing in *Prospect* magazine in 2018, David Neuberger, former President of the UK Supreme Court, said: *"Without the rule of law, society becomes unjust, violent and poor. It is of fundamental importance that Courts are open and accessible. Accessibility means that people with grievances and those being sued must get access to legal advice and to Courts. It is an affront to justice if people cannot understand or enforce their rights."*

If you need insight into the shortcomings of our system, you could hardly do better than dig out and read two written judgments of our High Court Judge Max Barrett. He plays a straight bat, but his unease is obvious. (*Start v Cussen* [2021] IEHC 531 ; *EBS v Ryan* [2020] IEHC 212).

Looking over our Judges' shoulders, the European Court of Human Rights frequently insists on access to courts allowing for *"effective participation,"* and this ECHR Article 6 prescription is further bolstered by the EU's own Charter of Fundamental Rights, applying due process guardrails (A.47) to all litigation referencing EU law. Note: once mortgage credit materialised in the form of an EU Directive, the Charter is engaged.

In the absence of significant legal aid for housing cases here, will any litigant manage to "participate" to the extent of raising specific issues regarding either (a) the new forbearance moratorium under the amended Article 28, or (b) the specifics, the intelligibility, and the bona fides of contract terms in consumer contracts of adhesion? Or both (a) and (b)?

When we find the Court of Appeal having to spell out to a trial judge that he was wrong to read hearsay evidence, objection notwithstanding, and then *"simply refraining from referencing the documents in the judgment delivered... without expressly ruling on admissibility or engaging with the consequences of the ruling."* (*Comerford v Carlow Co.Co.* [2021] IECA 253), what hope is there for reasoned rulings on all these new complex issues in consumer mortgage litigation (mostly, when the lay litigant doesn't even know he can object!).

Regulatory role of the Central Bank

In adversarial court proceedings with *"inequality of arms"* (see C-600/19 *Ibercaja Banco* in regard to the financial resources of debtors in default) the principle of effective *judicial* protection applies.

There is another way. In the Consumer Rights Act 2022, the Central Bank, as regulator, is equipped with the tools to raise these issues in court. A hands-on approach by the regulator could raise issues of substance in regard to contract terms in suits seeking declaratory reliefs against credit purchasers and/or credit servicers. It is also to be hoped that the Central Bank will be proactive in holding the servicers to account if they continue to assert legal ownership. The securitisation paperwork says otherwise.

The plain-to-see risk here is that, absent a proactive *"legitimus contradictor,"* the Central Bank will think that the court is across this, while the court will assume it's a regulator's job for the Bank, in due course. Sometime.

Central Bank published (in 2019) analysis of the use of derivatives by securitisation special-purpose-vehicles showed that over forty percent of assets of SPV's domiciled in Ireland are of SPV sponsored by banks, but *"both derivative user and non user vehicles are predominantly orphan entities (set up by charitable trust),"* and that *"consequently, there is no direct liability of the* sponsor." But the report concluded that *"the nexus of reliance on debt finance, strong interconnectedness with the banking system, reinforces the importance of close monitoring and macroprudential surveillance of SPV's."*

The bank's macroprudential concern is, as always, contagion spreading from SPV *"credit purchasers"* to the general retail banking system. The retail banks have exposure to counterparty risk where the credit purchasers' funding has been leveraged with retail bank lending.

But under the new Directive the Central Bank now has a more hands on role in protecting mortgage consumers. Systemic and/or institutional malpractice by credit servicers must be sanctioned even where prudential concerns are triggered. The bank is on both sides of the trade.
(Also, the bank may now also find itself regulating servicers which are domiciled here but ply their trade elsewhere using new passporting mechanisms.)

The Ombudsman

It may be helpful to clarify that the Oireachtas is the forum to which all Statutory Regulators must account, and the Ombudsman is the actor to report on maladministration. As a matter of law, the Courts are likely to follow English judgements which re-direct maladministration claims, declining particularly where the regulator has a liability shield in its statute.

After the publication of the UK Ombudsman's report into the collapse of Equitable Life (entitled *"A Decade of Regulatory Failure"*) blaming financial services regulator FCA, the Court declined to overturn the Government's refusal to follow through on the Ombudsman's recommendations, quoting this rationale: *"The role of the Ombudsman under the 1967 Act is not only to report to Parliament, but, where appropriate, vigorously to alert Parliament to an injustice which has occurred through maladministration."* (Ultimately the UK government made *ex gratia* payments to pensioners whose savings had been lost.).

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Edmund Honohan

Edmund Honohan
The Master of the High Court

P.S. If you get the chance, please try to dissuade your constituents from taking out "reverse mortgages," cashing in some of their equity for some short-term retirement bucket list. In my experience, they live to regret it down the line, often leave suspicion and bitterness between offspring and their in-laws, and sometimes costly litigation.

PTD - The Portable Trade Down

YOU can afford to pay the mortgage now, but not the arrears?
Carry the loan (and a mortgage to secure it) to a trade-down home.

Happy days: you do not need to fit in with Central Bank guidelines because the Vulture Fund is not a bank!
Go to over 100% LTV if necessary. Build in an equity release to cover other creditors (if any). A fresh start!

Bring into court the exact plan: "This is the house we could move to, and we can do this if the court agrees."
Your winning argument should be: This gets the Vulture Fund a better deal than in an Insolvency Arrangement.

Difficult to prove, but also difficult to disprove.
If the Vulture Fund tries, argue back: the current arrears will be paid, and the mortgage payments will resume.

The 'MTR' Put Option

BET you didn't know that you're a 'receivable'! Every NET cent the Vulture Fund hopes to generate from your situation is, for them, a 'receivable'.

The issue for the court is that in order to assess 'proportionality', it needs to know what figure the Vulture Fund has pencilled in.

If they expect say, 100, from the sale, with the then unsecured deficit written off. (and can prove it), then you may be able to meet that by offering to pay a rent which, as a stream of future payments discounted to its Present Value (PV), at a specified and reasonable rate of interest, is equivalent to 100.

You can do this by offering to pay annual rent to the Vulture Fund as your landlord, and you get to remain in your home as a long-term tenant.

That Landlord/Tenant deal has a capital value of 100, which the Vulture Fund can sell on.
And the put option? Pay a little extra to buy the right to buy your home back, whenever (within 21 years).

Rent unpaid? Lose the house, lose the option.

BCF - The Bailout Carried Forward

MOST of us remember the crazy junior bondholder decision (pay them 100%).

It is a fact that your mortgage loan has been securitised, collateralised, sold on, reinsured and assigned by subrogation and so forth, again and again, to the point where its core asset value, resting finally in some balance sheet, has shrunk to the grade of junk bond.

Discounted many times, losses absorbed and risks priced in, the ultimate owner is the 'junior bondholder' of this transaction.
Ask the court to presume (unless its proved otherwise) that the beneficial owner is offshore, not Irish.

Offer a full and final 50% to buy out the nominal debt.
That's TWICE the asset value in the owner's balance sheet, and HALF what you owe.
That's proportionality. (And an offshore owner doesn't have Constitutional rights here).

CMR - The Court Managed Receivership

NOMINATE a trusted but independent third party to be a Court Supervised Receiver of the home, pending further Order.

To conduct a sale by public auction (with "vacant possession" but with the option of renting to you), and in the meantime (until completion) to allow your continued occupation as a licensee. (Pay a market rent to the Receiver).
Court directions to place a reserve on it, namely the sum which you, or your VBF or PRF, are able to raise to buy it.

Do not attempt to rig the auction: stay well away (this isn't John B Keane's The Field).
If you don't get to buy, offer the new owner to rent the place from him even if only on a temporary convenience basis.
Knowing how keen you are to stay, he may realise you'll be a long-term and paying tenant, with or without HAP.

ERO - The Extended Redemption Option

THINK ten years. Afforded monthly payments are not credited to your mortgage loan account, but instead held in escrow, and at the end of that period the total paid is returned to you as your deposit when you go to get a mortgage from a bank to buy back ("redeem") the house at it's market value.

The deposit lump sum "rests in your account", and is then paid again to the Vulture Fund as part of a "full and final" redemption. (You can assign your right to redeem at this point).

Residual arrears (if any) on the mortgage account are written off. The ten year deposit period will be cut short if you default at any point, and your savings will be forfeit.