Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

The Tracker Mortgage Examination

Final Report
July 2019

Contents

1. Executive Summary

The scale of lenders' tracker mortgage failings was industry-wide, causing distressing – and in some cases devastating – consequences for customers. It required a robust and comprehensive regulatory response that required lenders to identify affected customers and to redress and compensate them for the harm the lenders had caused.

The Tracker Mortgage Examination (the 'Examination') was that regulatory response. It is the largest, most complex and significant consumer protection review the Central Bank of Ireland (the 'Central Bank') has ever undertaken, probing all lenders who ever offered tracker mortgage products in Ireland.[1] Arising from the Examination and issues pursued with lenders pre-Examination, lenders have identified c. 40,100 customers affected by tracker mortgage failings and paid out c. €683 million in redress and compensation to end May 2019.

Lenders have paid €683 million in redress and compensation. Lenders have identified 40,100 affected customers

The circumstances in which customers lost their tracker mortgage entitlements are the subject of the Central Bank's separate enforcement investigations. We recently concluded an enforcement investigation where we reprimanded one of the main lenders and imposed a very significant monetary penalty – the largest imposed on any regulated firm by the Central Bank to date – in respect of serious failings affecting tracker mortgage customers.[2] We continue to pursue our investigations against all the other main lenders.

The Central Bank serves the public interest by safeguarding monetary and financial stability and by working to ensure that the financial system operates in the best interests of consumers and the wider economy. In line with our mandate, the Central Bank intervened with a number of lenders over the 2008-2015 period in relation to tracker mortgages, including requiring certain lenders to offer affected customers the right to return to a tracker

1 For the purposes of the Examination, a 'Tracker Interest Rate' refers to the interest rate applied to a mortgage product: 1) which tracks a rate which comes from a publicly available source which can be verified by both the customer and the regulated entity, including without limitation, a rate that tracks the European Central Bank ('ECB') main refinancing operations rate; and 2) which is calculated in a manner similar to a rate which falls within 1) above, and includes interest rates calculated on the basis of a fixed rate margin and/or pricing promise.

2 https://www.centralbank.ie/news/article/press-release-enforcement-action-permanent-tsb-30-may-2019.

rate and/or payment of redress and compensation.[3] At the same time, the Central Bank strengthened the regulatory protections for tracker mortgage customers.

The Central Bank launched the Examination in 2015 after it became clear through combined supervisory and enforcement work and from information supplied by consumer advocates, members of the public and public representatives that tracker related issues could potentially be industry-wide.

The Central Bank is today publishing its final report as we are satisfied, following extensive supervisory challenge and assurance work, that the affected groups of customers have now been identified, that redress and compensation is nearing completion and that the supervisory phase of the Examination can be concluded accordingly.

The supervisory phase of the Examination is now concluded

While the supervisory phase of the Examination is now concluded, the Central Bank will continue to monitor the outcomes of any complaints, appeals and court cases. If any new information of a systemic nature comes to light, we will of course investigate.

1.1. Overview

The Central Bank put in place a Framework (the 'Framework') for conducting the Examination and 15 lenders were in scope.[4]

It is important to stress that lenders are responsible in the first instance for how they treat their customers. Yet, notwithstanding the serious issues of customer detriment under consideration in the Examination, some lenders initially attempted to minimise the number of affected customers to whom they would have to pay redress and compensation.

Lenders are responsible in the first instance for how they treat their customers

The Central Bank, in line with its mandate, intervened at all appropriate stages of the Examination to counteract this. Through a series of intensive engagements and intrusive supervision, the Central Bank successfully challenged lenders to include an additional c. 20,000 customer accounts - representing c. 60 per cent of the total number of accounts identified through the Examination.

3 Since 2008, the Central Bank has pursued tracker mortgage issues with lenders. Approximately 7,100 affected customers were remediated outside of the Examination. The 7,100 number is included in the overall number of affected customers of c. 40,100. Redress and compensation of c. €47 million was provided by permanent tsb plc and Springboard Mortgages Ltd outside of the Examination.

4 For the full list of lenders see Section 2 of this report.

Similarly, the Central Bank judged the initial redress and compensation schemes proposed by some lenders to be materially deficient. We reviewed more than 30 iterations and had an estimated 220 engagements with lenders in relation to their proposed redress and compensation schemes, driving substantial improvements in both their schemes and their appeals processes for the benefit of their customers.

1.2. How Lenders' Failures Affected Customers

While numbers alone cannot give the full picture of the impact that lenders' failures have had on tracker mortgage customers, up to and including the loss of homes and properties in some cases, they nevertheless highlight the scale of the detriment caused:

- The total number of affected customer accounts identified through the Examination is c. 33,000 to end May 2019. When added to the c. 7,100 cases remediated following Central Bank intervention prior to the Examination, it brings the total number of accounts affected by tracker mortgage related issues to c. 40,100.

- Total redress and compensation paid to affected customers stood at c. €683 million at end May 2019. This comprises c. €636 million paid through the Examination and c. €47 million paid outside the Examination.

- Offers of redress and compensation have been made in respect of 98 per cent of affected accounts, with two per cent remaining to receive payment at end May 2019. The accounts remaining to be paid chiefly comprise recently identified affected customer accounts and ones whom lenders have been unable to contact to date. The Central Bank has set out its expectation that lenders hold redress and compensation payments for uncontactable customers in a special ring-fenced account and lenders may not profit from these proceeds.

Offers of redress and compensation have been made in respect of 98 per cent of affected accounts

- At end May 2019, customers lost 99 Private Dwelling Homes ('PDH') and 216 Buy-to-Let ('BTL') properties as a result of lenders' failings.

Dependent on the circumstances of each individual case, where loss of property occurred, further amounts may have been paid to reflect the additional detriment, including, for example, payments to reflect increases in property value, or the write-off of residual debt:

- Within the terms of their schemes lenders included minimum payments to customers who lost properties of €25,000 for BTL properties and €50,000 for PDHs.

- The average redress and compensation paid in respect of loss of ownership of PDHs due to lenders' tracker mortgage failures is c. €194,000 and the average for BTLs c. €162, 000. Further details on redress and compensation paid are contained in Section 3.2 of the report.

The Central Bank also required lenders to set up an independent appeals process to deal with affected customers who were dissatisfied with any aspect of the redress and compensation offer they received from their lender.

- To date, ten per cent of affected customers have made appeals. The lenders' independent appeals panels have awarded customers c. €7m at end May 2019, with the majority of upheld appeals arising from awards for additional detriment due to personal customer circumstances of which the lender may not have been aware at the time the original redress and compensation was awarded.

The case studies in Section 3 of this report set out for illustrative purposes the effect of lenders' failures on their customers, while Section 3.2 breaks down redress and compensation paid.

1.3. Enforcement

The supervisory phase of the Examination focused on identifying affected customers and ensuring they were appropriately redressed and compensated by the lenders. Whilst the supervisory phase is now complete, the Central Bank's work in relation to tracker mortgage related issues has not concluded. We continue our ongoing enforcement investigations to determine how and why customer detriment happened.

The Central Bank is continuing its enforcement investigations to determine how and why customer detriment happened

Financial misconduct on the part of regulated entities will have serious consequences. The gravity with which we view tracker related failings is demonstrated by the €21 million fine recently imposed on a main lender in the first enforcement outcome arising from the Examination.[5] This is the largest fine imposed on a regulated firm by the Central Bank to date. The enforcement investigations are firstly examining the exact circumstances surrounding how and why customers lost their trackers and how lenders

[5] The Central Bank earlier imposed a fine of €4.5m on Springboard Mortgages Limited, which is part of the PTSB Group, in 2016 in respect of breaches of its obligations to tracker mortgage customers.

dealt with complaints relating to tracker mortgage related issues. Secondly, they are examining instances where lenders may have failed to have the requisite safeguards in place to ensure that they implemented the 'Stop the Harm' principles properly.[6] Finally, they are considering the actions of individuals which may be relevant to establishing how and why customers lost their trackers.

The Central Bank cannot comment on the specifics of ongoing investigations. As the investigations were commenced at different times, they will conclude on different timelines.

1.4. Strengthening the Regulatory Framework

In the decade since the financial crisis, a series of international and domestic scandals has highlighted why a robust regulatory system – coupling assertive supervision with strong redress and enforcement powers – will remain paramount in order to safeguard stability and protect consumers.

In keeping with that objective, and working within national and international frameworks, the Central Bank continually evolves our system of supervision for the regulated financial services sector as a whole. Our work in the Examination will feed into that process.

The Examination has exposed a clear lack of a consumer-focused culture in lenders. While many lenders publicly state they put their customers first, the evidence from the Examination suggests otherwise.

The Examination exposed a clear lack of consumer-focused culture in lenders

While responsibility for preventing detriment to consumers rests firmly with regulated entities, the Central Bank has taken steps to strengthen the regulatory framework. These measures include an enhanced approach to financial conduct regulation, the introduction of a new Consumer Protection Risk Assessment model ('CPRA'), a review of the behaviour and culture of the five main Irish retail banks and a commitment to conducting more frequent targeted conduct supervision of those firms that pose the greatest potential harm to consumers.

In addition, and arising from the recommendations in the Central Bank's Report on the Behaviour and Culture of the Irish Retail Banks, the Central Bank has made proposals to the Minister for Finance for the introduction of an Individual Accountability Framework, to include a Senior Executive Accountability Regime. The Central Bank has also sought the introduction of

6 The 'Stop the Harm' principles were put in place to ensure that potentially affected customers did not lose possession of their properties while lenders were carrying out their reviews.

enforceable conduct standards for regulated firms and the individuals working within them and the removal of the requirement to prove participation in the context of the Administrative Sanctions Procedures.[7]

We believe that the proposed Individual Accountability Framework will ensure greater accountability by placing obligations on regulated entities and senior individuals within them to set out where responsibility and decision making lie for their business along with a statutory duty of responsibility on senior individuals to take reasonable steps to prevent breaches occurring. This would assist the Central Bank in assigning responsibility to individuals and limit their ability to avoid liability for regulatory wrongdoing.

Accordingly, the Central Bank is working with the Department of Finance to progress legislative proposals for consideration by Government as part of the proposed Central Bank (Amendment) Bill.

1.5. Ongoing Monitoring

The Framework focused on requiring lenders to identify groups of customers affected by tracker mortgage related issues. The Central Bank is aware there is a possibility that individual, customer-specific issues may emerge which may not have been captured to date.

In addition, the Central Bank designed the Framework in such a way that after they receive redress and compensation, affected customers continue to have options to appeal to their lenders' independent appeals process, to the Financial Services and Pensions Ombudsman ('FSPO') and the courts to raise their own individual personal circumstances.

The Central Bank will continue to monitor the outcomes of any complaints, appeals or court cases

While the supervisory phase of the Examination is now concluded, the Central Bank will continue to monitor the outcomes of any complaints, appeals and court cases. We have clearly communicated to lenders our expectation that if any individual outcomes arise that have the potential to impact customers more widely, they then must address this broader impact and inform the Central Bank accordingly.

Finally, in concluding the supervisory phase, it is important to reiterate the immense distress and damage that lenders' unacceptable failings have caused affected customers and their families.

7 The participation hurdle means that, at present, the Central Bank can hold individuals to account only where they are proven to have participated in a firm's breach of rules. Removing the hurdle would mean the Central Bank could hold individuals to account directly for their misconduct under the Administrative Sanctions Procedure.

At every step of the Examination, our focus has been on affected customers and ensuring lenders paid them appropriate redress and compensation. While the supervisory phase of the Examination has now concluded, its outcomes will be taken forward and reflected in our continuing supervision.

2. Introduction

The Central Bank serves the public interest by safeguarding monetary and financial stability and by working to ensure that the financial system operates in the best interests of consumers and the wider economy. The best interests of consumers are protected and confidence and trust in the financial system is enhanced through effective regulation of firms and markets. We recognise the detriment to consumers that can occur if firms do not conduct themselves appropriately.

During a period of increased competition in the Irish mortgage market between 2003 and 2008, tracker mortgages – which tracked the European Central Bank ('ECB') interest rate by a margin – grew in popularity as a product. When interest rates started to rise between 2006 and 2008, many customers on variable interest rates (including tracker interest rates) decided to fix their interest rate for a period in order to have certainty about their monthly mortgage repayments.

From 2008, due to the economic and banking crises, lenders' funding costs rose and were no longer aligned to ECB rates. As a result, all lenders in the market stopped offering tracker interest rates to new customers.

However, in doing this, lenders sometimes failed to take account of their obligations to existing customers, including customers who had a contractual right to a tracker rate of interest - or the legitimate expectation of a tracker rate based on documentation or other influencing factors - when their fixed rate mortgage expired. In particular, some customers who had chosen to fix their interest rates between 2006 and 2008, lost that tracker interest rate, or were not offered that tracker interest rate, during the remaining term of their agreements. This resulted in often significant overcharging of customers, over a prolonged period of time in some cases.

Lenders sometimes failed to take account of their obligations to existing customers

In line with its mandate to ensure the best interests of consumers are protected, the Central Bank intervened with a number of lenders over the 2008-2015 period in relation to tracker mortgages, including requiring certain lenders to offer affected customers the right to return to a tracker rate and/or payment of redress and compensation. At the same time, the Central Bank strengthened the statutory protections for tracker mortgage customers. After pursuing tracker mortgage related issues with some individual lenders, the Central Bank launched the Examination in 2015. It had become clear through earlier supervisory and enforcement work and information supplied by consumer advocates, members of the public and public representatives that some lenders were denying customers a tracker mortgage or putting them on the wrong rate and that tracker related issues were potentially industry-wide.[8] Accordingly, the Central Bank put in place the Framework for conducting the Examination and 15 lenders were initially contacted. This report updates on the outcomes for the 11 lenders whose customers were affected by tracker mortgage related issues and who, therefore, implemented redress and compensation schemes. Those lenders are:

- AIB Group;
- Bank of Ireland Group;
- Permanent tsb plc;
- Ulster Bank Ireland DAC;
- KBC Bank Ireland plc;
- ACC Loan Management Limited;
- Bank of Scotland plc;
- Danske Bank;
- IBRC;
- Springboard Mortgages Limited; and
- Stepstone Mortgage Funding Limited.

This report updates on the outcomes for the 11 lenders whose customers were affected by tracker mortgage related issues

Dilosk Limited, Leeds Building Society, Pepper Finance Corporation (Ireland) DAC and Start Mortgages Limited DAC are not covered in this report as they do not have affected customers and as a result redress and compensation schemes are not being implemented.

Given that IBRC was in liquidation, certain aspects of its redress and compensation scheme were not fully aligned with the Principles for Redress.

---

8 Since 2008, the Central Bank has pursued tracker mortgage related issues with lenders. Approximately, 7,100 affected customers were remediated outside of the Examination. Redress and compensation of c. €47 million was provided by permanent tsb plc and Springboard Mortgages Ltd outside of the Examination.

As part of the Examination, a small number of affected customers were admitted by the special liquidator as unsecured creditors and have been remediated, where contactable, and repaid the amounts of interest overcharged as part of the liquidation process.

The Framework required lenders to conduct their Examination in four phases:

Phase 1: Development and Submission of Detailed Plan;

Phase 2: Information Gathering/Review/Report Submission;

Phase 3: Calculation of Redress and Compensation (where relevant); and

Phase 4: Implementation of Redress Programme (where relevant).

The Central Bank designed the Framework so that the phases of the Examination could run concurrently within a lender and at different times across lenders. The boards of the lenders were ultimately responsible for ensuring the lenders carried out a robust and comprehensive review, in accordance with the Framework. The Central Bank's review of the lenders' phases also ran concurrently.

The Examination involved an initial review of more than two million mortgage accounts by lenders to identify the number of in-scope accounts. Accounts in scope include all mortgage accounts from the date the lender commenced offering tracker interest rate mortgages until 31 December 2015, in respect of both Private Dwelling Houses and Buy-to-Let properties:

- that originated on tracker interest rates;
- that had tracker interest rates applied at any stage during the term of the underlying mortgage agreements; and/or
- where the underlying mortgage agreements provided for contractual rights to or options for tracker interest rates at any stage during the term of the agreements.

The Examination involved an initial review of more than two million mortgage accounts by lenders

The Central Bank has published regular updates since the Examination began in 2015 in order to inform affected customers and the wider public of the Examination's progress.[9] This final report concludes on the review and remediation phase of the Examination and sets out the assurance process that the Central Bank has carried out in order to reach this conclusion.

[9] https://www.centralbank.ie/consumer-hub/tracker-mortgage-examination

It provides data on the outcomes that the lenders' appeals processes have delivered for customers to 31 May 2019 and sets out that the Central Bank will monitor payments, complaints, appeals and any residual issues to completion as part of our normal conduct supervision.

The report further outlines the various options put in place for affected consumers in the event that they were not satisfied with the redress and compensation payments from their lender.

While the Central Bank's supervisory work is now complete, customer appeals and other channels available to consumers under the Framework will continue to deliver outcomes. In addition, work continues on a number of enforcement investigations which build on the work carried out in the supervisory phase, as detailed in Section 5.

3. Supervisory Outcomes

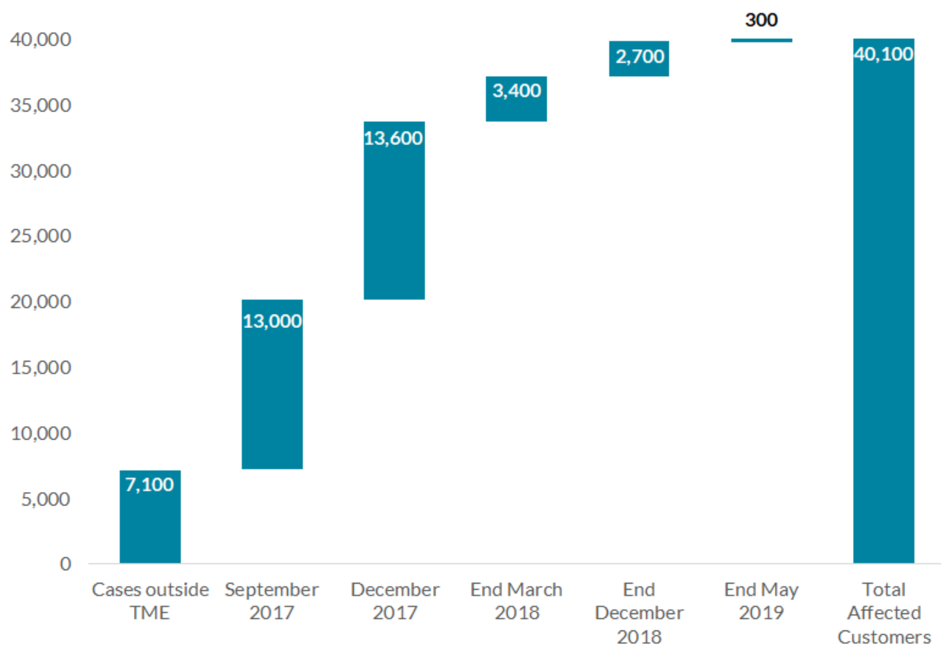
From the outset, the Central Bank focused on a system wide response to lenders' failures and to ensuring that lenders identified and remediated the detriment they had caused to affected customers as promptly as possible.

3.1. Customers included for Redress and Compensation in the Examination

The total number of affected customer accounts identified through the Examination to end May 2019 is c. 33,000. When added to the c. 7,100 cases remediated prior to the Examination, it brings the total number of customer accounts affected by tracker mortgage related failings to c. 40,100. The five main lenders – AIB Group, Bank of Ireland Group, KBC Bank Ireland plc, Permanent tsb plc and Ulster Bank Ireland DAC – account for c. 98 per cent of affected customers identified as part of the Examination, while the remaining lenders account for the balance.

40,100 customer accounts were affected by tracker mortgage failings

Chart 1: Customers Identified as Affected by Tracker Mortgage Related Failings since Commencement



The above chart captures the increase in the number of affected customers identified for redress and compensation. As can be seen from the chart, the critical period was post September 2017, when lenders had submitted their reviews in accordance with Phase 2 of the Examination and the Central Bank interrogated and challenged these reviews.

Through this series of intensive engagements and intrusive supervision, the Central Bank challenged lenders to include an additional c. 20,000 affected customer accounts as reflected in Chart 2 below. This represented c. 60 per cent of the total number of accounts identified through the Examination. As can be seen from Chart 1, smaller numbers of affected customer accounts were identified in the latter stages of the Examination, as assurance work, including data verification work, concluded.

Chart 2. Breakdown of Accounts Affected by Tracker Related Issues Identified as part of the Examination

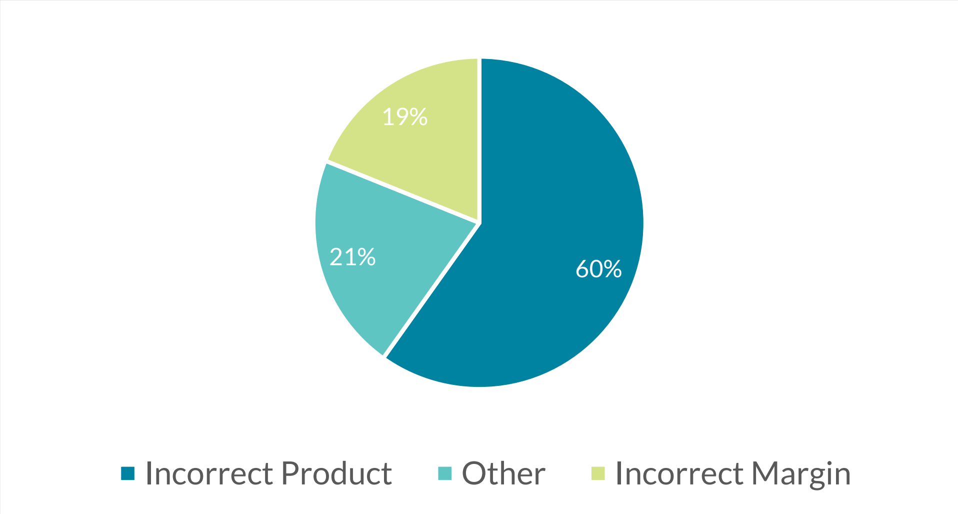
3.1.1. Breakdown of Affected Customers

While the range, complexity and variance of cases within the Examination is significant, Chart 3 (below) shows the circumstances of affected customers, which can be broken down into three main categories, as follows:

- customers who, despite a contractual entitlement to a tracker rate of interest, or the legitimate expectation of a tracker rate based on documentation or other influencing factors, lost that tracker interest rate, or were not offered that tracker interest rate, during the term of their agreements ('incorrect product');
- customers who were on an incorrect tracker interest rate margin ('incorrect margin'); and

- customers affected by short term operational type failures and customers not offered a particular rate in accordance with the account terms and conditions ('other').

Chart 3: Breakdown of Affected Customers by Category



60 per cent of affected accounts arose from contractual or transparency failings

In order to further explain these categories, described below are some examples:

Incorrect product (loss of tracker product/rate due to contractual and transparency issues)

- a customer's loan documentation provided an enduring right to a tracker rate at the end of any fixed interest rate period. However, at the end of a fixed rate period, the customer was not offered the option of a tracker interest rate.
- in relation to the rate to apply at the end of a fixed interest rate period the wording created a reasonable expectation for a customer that a loan would revert to a tracker interest rate on expiry of a fixed rate period.

Incorrect margin

- a loan offer specified the margin to apply to the mortgage but at drawdown a higher margin was applied, with no evidence that the customer was informed of the higher margin.
- a loan offer specified a discounted tracker margin, but the discounted margin was not applied.

Other

- a mortgage had a longer fixed interest rate term applied than specified in the fixed rate agreement and, therefore, did not roll to the tracker interest rate on the correct date.
- a mortgage had a different rate applied on the lender's system, with no evidence that the rate change was requested by the customer, or that the customer was informed, before being corrected after a short period.
- customers not offered a tracker rate in accordance with the account terms and conditions.

Below are illustrative examples of how customers could be impacted by tracker mortgage failings.

3.1.2. Case Studies

Case Study 1 – Contractual issue resulting in loss of tracker

In early 2006, Mary drew down a mortgage on a tracker rate of 3.45% (ECB rate of 2.5% + 0.95% margin) over a 20-year term. Later that year, Mary decided to move to a one-year fixed rate of 4.75%. When her fixed rate expired in 2007, although offered a tracker rate at this point, she decided to enter into another fixed rate of 4.89% for an additional two years. When that expired in 2009, she rolled to a Standard Variable ('SVR') rate of 4%.

The loan documentation that Mary originally signed set out that the tracker interest rate at drawdown would apply at the end of every fixed period entered into during the term of the mortgage. However at the end of the second fixed rate period, her lender failed to apply a tracker rate to Mary's mortgage.

Mary's account has now been put on the correct tracker rate of interest (ECB rate + 0.95% margin) and a balance adjustment has been made on her account which was calculated using the tracker rate.

Mary has also received a redress and compensation offer of €41,232 which includes a refund of the interest overpaid since 2009, a compensation payment and a payment towards obtaining independent financial advice.

Case Study 2 – Private Dwelling Home loss of ownership resulting from a failure to offer a tracker rate

Luke drew down on a tracker rate of 3.85% (ECB rate of 3% + 0.85% margin) in 2006. In 2008, he moved to a three-year fixed rate, which was due to expire in 2011. On expiry of the three-year fixed period, the mortgage rate rolled on to a standard variable rate of 3.25%.

Luke's loan documentation was unclear as to what rate would apply to his account on expiry of his fixed rate period. Based on the wording in the documentation, Luke may have had a reasonable expectation that he would revert to the tracker rate at the end of his three-year fixed period. If Luke's mortgage had reverted to a tracker rate on expiry of the fixed period in 2011, based on the margin he was on prior to moving to the fixed rate, the tracker rate would have been 2.1% (ECB rate 1.25% +0.85% margin).

Luke lost his job in 2011 and he entered into various alternative repayment arrangements such as interest only periods and reduced repayment options with his lender. In 2013, Luke's mortgage was deemed unsustainable by his lender and he sold his house in early 2014.

If the correct tracker rate had been applied to Luke's account, he would have qualified for a longer term alternative repayment arrangement and as a result, his mortgage would not have been deemed unsustainable and he would not have lost ownership of his home.

Recognising the severe detriment caused by the loss of ownership due to the lender's failure to offer Luke a tracker rate on expiry of his fixed period, Luke has received a redress and compensation offer of €216,200. In addition to redress and compensation for the loss of property and payment for independent advice, the overall payment includes a payment to reflect the increase in property value since he sold his home.

In addition, his lender has written off the residual debt remaining on his original mortgage. Luke has also been offered a new mortgage on a tracker rate of ECB + 0.85% margin, which is the tracker margin that his mortgage account would have been on had this failing not occurred.

Case study 3 – Margin issue resulting in wrong margin applying to the tracker mortgage

Jane drew down a mortgage on a tracker rate of interest of 4.25% (ECB rate of 3.25% + 1% margin) in 2006. The offer letter specified that a discounted tracker rate of interest of 3.75% (ECB rate plus 0.5% margin) would apply for the first two years. However, Jane's lender failed to apply the discounted rate of interest and, as a result, Jane was charged an additional 0.5% for two years.

Jane has received a redress and compensation offer of €2,021, which includes a refund of the interest overcharge, a compensation payment and a payment towards obtaining independent financial advice.

Case study 4 - Mortgage account not affected by a tracker related failure

In 2004, Paul drew down a mortgage on a standard variable rate of interest of 4.5%. In 2005, he moved to a two-year fixed rate of 4.7%. The fixed rate agreement that Paul signed stated that a standard variable rate of interest would apply on expiry of the fixed rate of interest. In 2007, on expiry of the two-year fixed rate period, Paul was offered a number of options by his lender, including a standard variable rate of interest, a tracker rate of interest and a fixed rate of interest. Paul chose a fixed rate of interest for another two years (until 2009) at 4.88%.

The loan documentation indicated that a standard variable rate of interest would apply on expiry of the fixed interest rate period. Paul's lender subsequently withdrew tracker interest rate products in 2008. On expiry of this two-year fixed rate period in 2009, Paul was offered the option of a standard variable rate of interest or a fixed rate of interest. Paul opted to move to a standard variable rate of interest of 3.98% at that time.

Paul's mortgage was never on a tracker interest rate. His original loan agreement did not provide a contractual right to a tracker interest rate, nor to the offer of a tracker rate of interest. The fixed rate agreements were clear that a standard variable rate would apply at expiry of the fixed interest rate periods, and the options offered by the lender at expiry of the two-year fixed rate period in 2007 did not confer a contractual right to a tracker interest rate.

When Paul became aware of the Examination, he contacted his lender regarding his entitlement to a tracker on the basis that he was offered the option of a tracker interest rate in 2007, which he did not take up. Paul's lender advised him that he was not in scope for the Examination as he never had a contractual right to a tracker and the documentation was clear in relation to the rate to apply at the end of the fixed interest rate period. The conclusion of the lender is in line with the Examination Framework.

3.2. Redress and Compensation

The Framework requires lenders to identify all affected customers and to address customer detriment in line with the Central Bank's Principles for Redress, which, along with supplemental guidance, clearly set out the Central Bank's expectation that lenders make redress and compensation offers that are fair and commensurate with the detriment suffered by their customers. The full range of Examination documents, including the Framework, can be seen here.[10]

Key elements of the Principles for Redress include:

- stopping further detriment to potentially affected customers;
- redress to return customers to the position they would have been in had the lenders' failures not occurred;
- compensation to reflect the detriment suffered;
- the establishment of an independent appeals process for affected customers;
- the provision of a payment to enable affected customers to obtain independent advice; and
- guidance with regard to the manner in which lenders should communicate with affected customers.

The Central Bank repeatedly challenged lenders to improve their redress and compensation schemes

Conscious of the damage that lenders' actions caused to customers, the Central Bank has, throughout the Examination, prioritised ensuring that lenders' offers of redress and compensation to affected customers were commensurate with the detriment they suffered. In this regard, as previously noted, we judged some lenders' initial redress and compensation proposals to be materially deficient. The Central Bank challenged those lenders repeatedly, reviewing more than 30 iterations of proposed redress and compensation schemes and holding an estimated 220 engagements with

10 https://www.centralbank.ie/consumer-hub/tracker-mortgage-examination

lenders to drive improvements in both their redress and compensation proposals and their appeals processes, to the benefit of affected customers.[11]

Examples of the improvements made include:

- increased minimum payments to affected customers;
- increased compensation levels;
- increases in rates used to calculate the Time Value of Money[12];
- increased independent advice payments;
- the inclusion of a payment to recognise an uplift in property value for customers who lost ownership of their property due to a failing by the lender; and
- recognition of detriment to affected customers, who switched lenders, to take account of losses they suffered after the switch, subject to certain criteria.

3.2.1. Redress and Compensation Paid

Recognising that financial compensation cannot fully right the wrong done to affected customers, the Central Bank insisted that lenders address the financial losses suffered by providing redress to affected customers to put them back in the position they would have been in if the failure had not occurred and to provide compensation for the detriment caused.

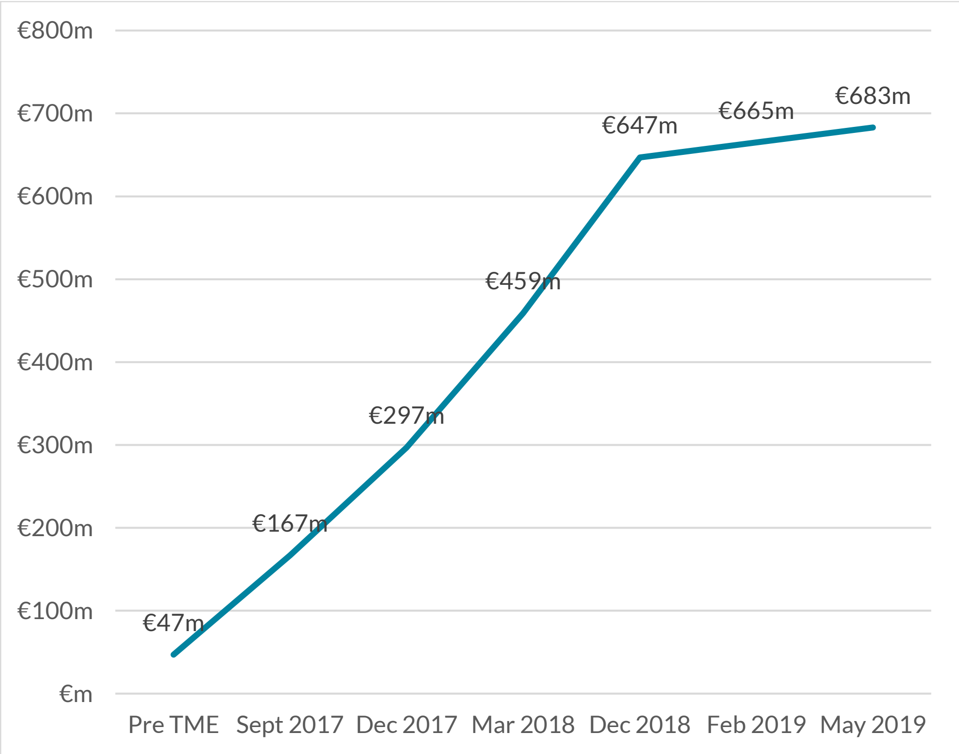
At end May 2019, total redress and compensation paid to affected customers arising from the Examination was c. €636 million – of which c. 21 per cent relates to compensation. When the c. €47 million paid outside the Examination is included, total redress and compensation paid to affected customers stood at €683 million at end May (see Chart 4 below).

---

11 Engagements include meetings, letters, emails and telephone calls.

12 The Time Value of Money payment compensates for the period in which the affected customer did not have access to, or the benefit of, the money that was overpaid by them.

Chart 4: Value of Redress and Compensation Payments

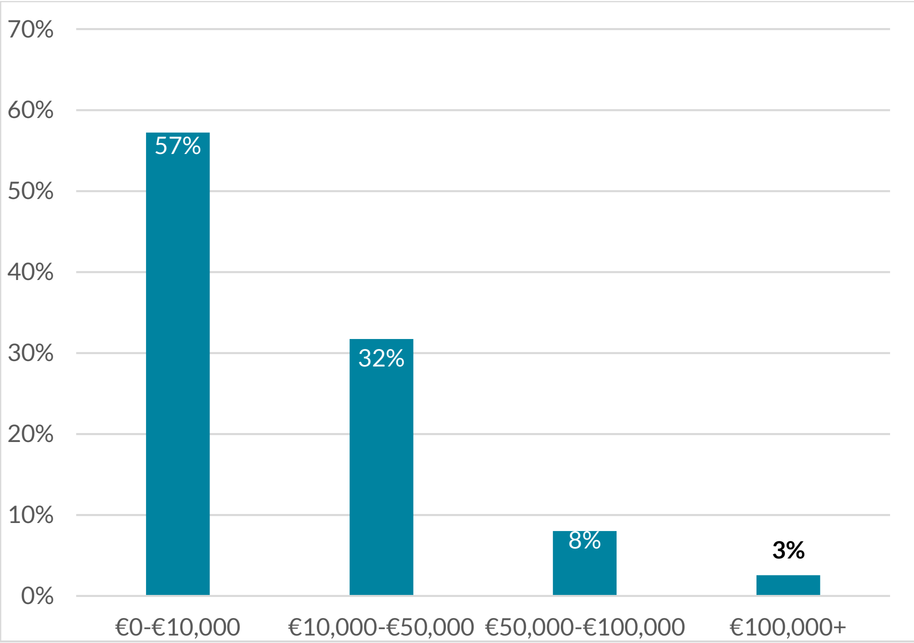


Payment of redress and compensation is now nearing completion across the lenders. At end May 2019, offers of redress and compensation have been made in respect of 98 per cent of affected accounts. The accounts remaining to be paid mainly comprise recently identified affected customers' accounts and ones whom lenders have been unable to contact to date and whom they are actively trying to trace. The Central Bank will continue to engage with relevant lenders to ensure that payments are made in line with the Framework.

3.2.2. Range of Payments Made to Affected Customers

The majority of customers (57 per cent) received payments up to €10,000, with three per cent receiving payments in excess of €100,000. The range of payments is illustrated in Chart 5 (below).

Chart 5: Percentage of Affected Customers in Each Payment Category



It is important to note that payments made to affected customers vary significantly and depend on a number of variables including the amount borrowed, the period of the overcharging, the margin by which the customer was overcharged and the level of detriment suffered (up to and including loss of ownership of the property as a result of a lender's failing).

3.2.3. Loss of Ownership

As at end May 2019, loss of ownership as a result of a tracker related failure has occurred in respect of 99 PDH and 216 BTL properties. The average redress and compensation paid to date in respect of loss of ownership of PDHs due to lenders' failures is c. €194, 000 and the average for BTLs is c. €162,000.

Chart 5 above includes c. 830 customer accounts which received a payment in excess of €100,000. Of this figure, 228 lost ownership of their property due to tracker failures, 75 of which were PDH properties.

These figures reflect the upper range of redress and compensation payments for loss of ownership. It should be noted that redress and compensation for such affected customers will vary depending on the personal circumstances of each customer. These circumstances include the term of the mortgage remaining at the time of the loss of ownership, the size of the mortgage, the date the loss of ownership occurred and the amount of any uplift in the property value. The lender was required to take all of these circumstances into account in calculating the level of redress and compensation to be paid.

3.3. Supervisory Programme for the Examination

The Central Bank developed a comprehensive Framework for conducting the Examination

The Central Bank required lenders to conduct a review to examine the extent to which they met their contractual obligations to tracker mortgage customers and to examine the transparency of their communications with customers in relation to tracker related issues. In order to ensure that the reviews across all lenders were conducted in a robust and thorough manner, a Framework was developed that applied to all lenders who fell within scope.[13] The Examination was conducted in phases with different phases running concurrently in each lender and across lenders.

The Framework requirements were designed to minimise the risk of lenders failing to identify any impacting issues or groups of customers. To achieve this, lenders were required to:

- segment and test all groups of customers within the in-scope population for tracker impacting issues;
- conduct a review to determine that they had met all regulatory requirements for tracker customers;
- conduct a top-down review of transparency considerations and any influencing factors that may have affected a customer's decision regarding their tracker; and
- conduct a review of all tracker related complaints focusing on the issues that were the subject of the complaints, as distinct from the outcomes of any decisions on tracker complaints that had already being adjudicated on by the lender or FSPO.

The Framework also required lenders to appoint external independent overseers to undertake independent assurance work for all aspects of the Examination. In addition, given the scale and complexity of the Examination, a rigorous, comprehensive and robust supervisory programme has necessarily underpinned each stage, with the aim of ensuring that lenders complied with the Framework (including the Principles for Redress) in carrying out reviews, and that all groups of affected customers were

13 The Framework required the Examination to be conducted in four phases:

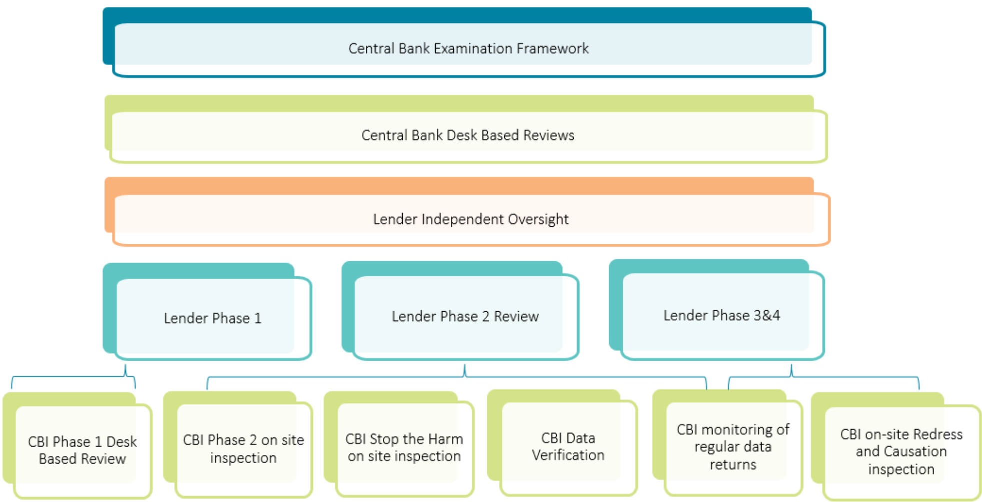
- Phase 1- Planning;
- Phase 2- Information Gathering/Review/Report Submission;
- Phase 3 - Calculation of Redress and Compensation; and
- Phase 4 - Implementation of Redress Programme.

The Examination covers all lenders who may have sold tracker mortgages in the past, including those no longer selling mortgages. It also covers mortgages that have been redeemed or switched to another lender.

identified. The Central Bank was assisted by two third parties in carrying out this work.

Chart 6, below, demonstrates the rigorous and multi-faceted approach taken to the Examination comprising a number of layers and different forms of Central Bank assurance, including desk based reviews, on-site inspections, data verification work, regular monitoring of lenders' data returns and regular engagement with lenders. In excess of 3,000 days were spent completing Central Bank on-site work throughout the course of the Examination. This was in addition to a significant level of ongoing engagement with lenders prior to, during and after the completion of the assurance work. All of this assurance work was underpinned by robust internal Central Bank governance. It should be noted that in respect of the smaller lenders, for certain elements of the assurance work and data verification work, a bespoke approach was adopted, reflecting the nature of their loan books and their individual circumstances.

Chart 6- Central Bank of Ireland's Approach to the Examination



3.4. Programme of Assurance

3.4.1. Phase 1 Desk Based Review

The initial phase of the Examination required lenders to develop and submit a detailed plan and put governance structures and systems in place in order to conduct a comprehensive review. The Central Bank then reviewed the plans submitted from lenders and, where necessary, challenged them to ensure compliance with the Framework.

3.4.2. Phase 2 Inspections

Following desk based review and engagement with lenders, the Central Bank undertook on-site inspections of relevant lenders following their completion of the information gathering and review phase of the Examination. The scope of the inspections was to determine whether lenders' approach to their Phase 2 reviews and the conclusions they reached on groups of customers were in accordance with the Framework. The testing was focused on customer accounts considered in-scope for the Examination, but which lenders had concluded were not affected by a tracker related issue.

Where the Central Bank assurance work identified concerns with lenders' decisions or the robustness of their reviews, the Central Bank challenged lenders until such concerns were addressed. This substantial challenge and engagement resulted in the lenders including an additional c. 20, 000 customer accounts as affected.[14] Two lenders in particular required significant challenge to bring them in line with the expectations of the Framework.

3.4.3. Stop the Harm Inspections

The core objective of the Central Bank's work was to require lenders to fully address the impact their actions had on affected customers. To help achieve this aim, the Central Bank developed 'Stop the Harm' principles which required lenders to:

- stop any potential harm being caused to customers at the earliest possible time;
- cease charging impacted customers the incorrect interest rate and apply the appropriate tracker interest rate (or, where this could not be determined, apply an interim reduced rate); and
- submit to the Central Bank detailed information in relation to the controls they put in place to ensure no further loss of ownership events occurred or litigation was progressed in respect of potentially impacted customers.

The Central Bank conducted on-site inspections of the controls and measures put in place by relevant lenders and followed up as appropriate.

---

[14] Engagements include meetings, letters, emails and conference calls

3.4.4. Redress, Compensation and Causation Inspections

The Central Bank also conducted on-site and desk based assurance work on the Redress and Compensation process of lenders (Phases 3 & 4) to ensure that lenders were operating redress and compensation payment processes in line with their redress and compensation schemes.

A small number of lenders had to revise and issue additional remediation in some cases. The work also examined the process followed by lenders when determining whether an affected customer lost possession of their property as a result of a tracker issue, to ensure that those processes were reasonable and robust.

3.4.5. Data Verification

In addition to the assurance work undertaken to determine that the lenders' approach to the Examination was in line with the Framework, the Central Bank also conducted a data verification review across lenders.

The Central Bank conducted a data verification review to ensure that the data on which the lenders relied to conduct their reviews was robust

This was done to ensure that the data on which lenders relied to conduct their reviews was robust and that lenders had reduced the risk of incorrect identification of groups of customers impacted by their failures.

The work involved an initial review of lenders' governance, processes and procedures for extracting from their systems the data they required to carry out their reviews. In the case of the five main lenders, the Central Bank then used data from those lenders to recreate groups of impacted accounts and gain assurance that lenders had not wrongly classified customers as not impacted.

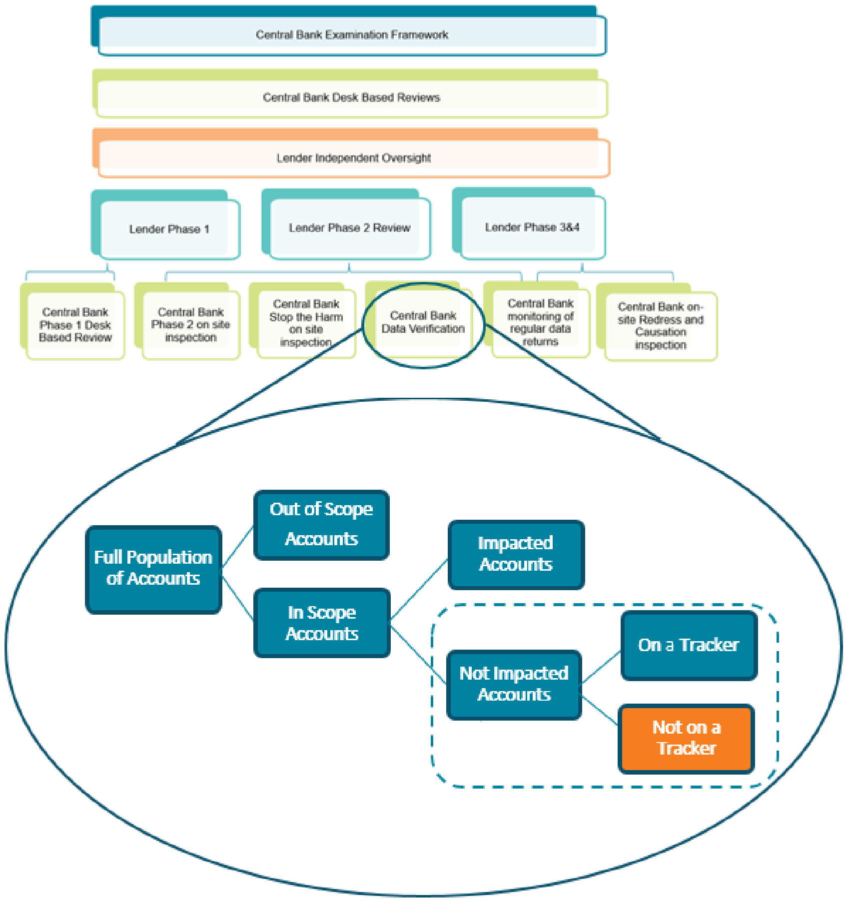
In addition, the Central Bank assessed the robustness of the exclusion testing, which the lenders were required to carry out to ensure that no groups of customers were incorrectly deemed out of scope.

Lenders were also requested to produce a data breakdown which filtered the full mortgage population into accounts that were in-scope and ones that were out-of-scope.

The in-scope accounts were further broken down into two groups - impacted and not impacted accounts. This allowed the Central Bank to further examine a population of customer accounts which were considered to be 'high risk' because they were in-scope for the purposes of the Examination, were not on a tracker rate, but had been deemed unaffected by lenders.

The Central Bank carried out further targeted file testing and requested lenders to provide satisfactory explanations and evidence for their decisions in relation to this group. The Central Bank reviewed and challenged as necessary in order to gain assurance that these accounts were not affected by a tracker mortgage related failure. The lender data verification process is set out in Chart 7 below.

Chart 7 – Lender Data Verification Process



3.5. Supervision Conclusion

The Framework focused on the identification, by lenders, of groups of customers affected by tracker related issues from a systemic perspective. While the Central Bank is satisfied that the supervisory phase of the Examination was suitably robust and comprehensive, we are aware there is a possibility that individual customer-specific issues may be identified, which have not been captured to date. Such cases may arise through complaints to lenders and to the FSPO, appeals and court cases which we reference in Section 4.

The Central Bank is aware that some groups of customers are not satisfied with their outcomes because they were not deemed impacted under the Examination or, where they have been deemed impacted, are unhappy with the particular interest rate margin offered. Through the robust supervisory process outlined above, the Central Bank has challenged lenders to the fullest extent possible to ensure that all impacted groups were identified. The Central Bank is satisfied that, from a supervisory and legal perspective, it has worked to the limit of its mandate to ensure that where grounds were sufficiently clear and impact was established, all relevant groups have been included.

At this point in the Examination, the Central Bank is not in dispute with any lender in respect of groups of customers which should be deemed impacted, and as such is satisfied it has the required assurance in order to conclude on the supervisory phase of the Examination. In line with its consumer protection mandate, the Central Bank will continue, through ongoing supervision, to monitor outstanding redress and compensation payments to customers, to ensure that these are carried out by agreed timeframes and in line with the Principles for Redress, and to ensure that complaints and appeals are dealt with in line with the Framework.

The Central Bank will also continue to monitor the outcomes of any complaints, appeals and court cases and has also communicated to lenders the expectation that they must fully consider whether any individual customer issues arising could have the potential to impact more widely.

4. Appeals

The Central Bank drives a system-wide industry response where we identify issues causing detriment or potential detriment to customers. Accordingly, the Framework was designed to deliver redress and compensation to affected customers.

Redress was designed to restore affected customers to the position they would have been in had the failure not occurred, while the compensation was to be appropriate and reasonable to take account of the specific circumstances of each customer to reflect the detriment caused.

As the Central Bank does not have a statutory role in dealing with individual customer complaints, the Framework required lenders to establish an independent appeals process. This process was necessary as lenders' offers of redress and compensation were made on the basis of broad-based customer groups and, as a result, may not have taken into account the personal circumstances specific to individual accounts. The appeals process was established to deal with customers who were dissatisfied with any aspect of the redress and compensation offer made to them by their lender, including circumstances where customers felt their own personal circumstances had not been appropriately addressed in the offer.

The appeals element of the Framework was to ensure that customers had further options, up to and including recourse to the courts, if they felt the redress and compensation offered by their lender was insufficient. In this way, the Central Bank was in a position to drive redress and compensation on behalf of consumers without prejudicing any further actions they may wish to take. The Central Bank, as part of the Framework, required that lenders would not rely upon or raise the Statute of Limitations as a defence in respect of any claim that an affected customer might bring against a lender to secure a remedy. This ensured that affected customers would not have been denied a remedy due to the passage of time in respect of tracker mortgage related issues.

Lenders could not rely upon or raise the Statute of Limitations as a defence for affected customers

4.1. Lenders' Appeals

Under the independent appeals process, affected customers could accept their offer for redress and compensation while still making an appeal. This ensured that a customer's need to receive payment upfront was not a determining factor in deciding whether to appeal an offer. The Central Bank also insisted that Appeals Panels could not make a less favourable finding than any offer made to affected customers pursuant to the lenders' redress and compensation schemes. Lenders are required to reimburse affected customers for their reasonable costs incurred in bringing appeals, in the event that the appeals are successful in part or in whole.

Appeals form an important part of the overall Examination process as they ensure an independent and transparent consideration of issues raised by affected customers about any aspect of the redress and compensation they have been offered. In particular, affected customers who have suffered severe detriment, and feel that their personal circumstances have not been sufficiently taken into account, may wish to bring that information forward for consideration by the Appeals Panels within a set period of time from receipt of their redress and compensation offers.

Panels must include appropriately qualified professionals and are required to be comprised at a minimum of an independent majority (including an independent chairperson). In respect of appeals from customers who have been affected in a more serious manner, panels are required to be wholly independent of the lender. All panels must include a consumer voice representative.

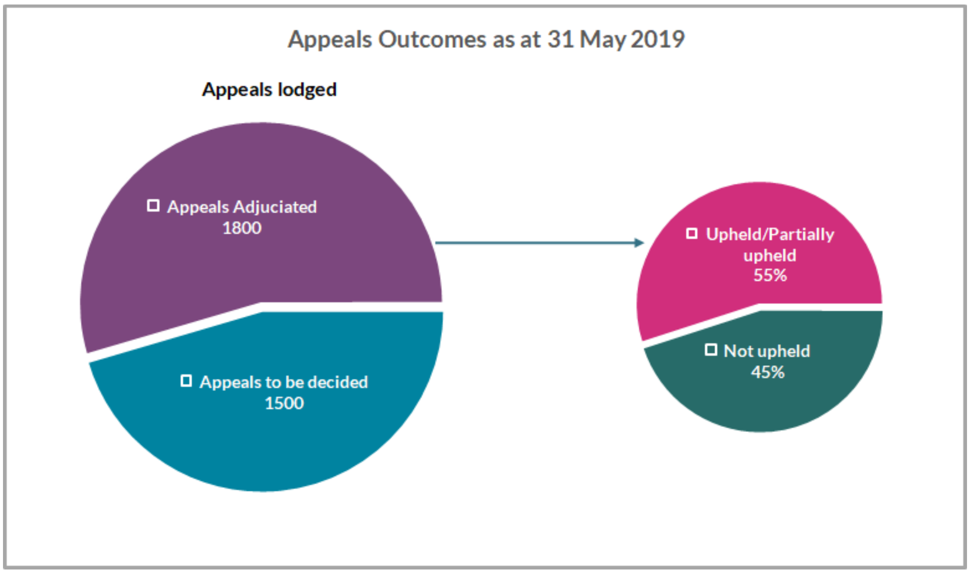
The Appeals Panels are operational in all relevant lenders. The independence of the appeal process is critical and allows the appeals to be heard on an unbiased basis. The Central Bank engaged with and challenged lenders on the terms of reference and procedural rules of their Appeals Panels when they were being drafted.

The independence of the Appeals Panels - of both the lender and the Central Bank - was deemed critical for their credibility. As such, the Central Bank cannot intervene in Appeals Panels' decision making but is monitoring the progress and outcomes from the appeals. The Central Bank also expects lenders to monitor the outcomes of the Appeals Panels and, where necessary, apply outcomes on any system wide issues across their wider customer population where similar customer circumstances arise.

4.2. Appeal Outcomes

At 31 May, c. 3,300 customers had appealed to their lenders the original compensation offer they received.[15] This represents c. 10 per cent of customers who have received payment. In respect of appeals lodged at end May, c. 1,800 appeal outcomes have been decided upon by Appeals Panels. Of the c. 1,800 appeals decided, 55 per cent have been upheld/partially upheld and 45 per cent have not been upheld. The majority of appeals upheld arise from awards for additional detriment of which the lender may not have been aware at the time of the original redress and compensation awarded. At 31 May 2019, Appeals Panels have awarded c. €7 million additional compensation to affected customers.

Chart 8 – Appeal Outcomes



When they were paid their initial redress and compensation, affected customers were advised of the deadline for making an appeal. About 20 per cent of affected customers who have received payments of redress and compensation are still within the time period for making appeals if they so wish. It is again critical to stress that under the Framework, customers could accept the initial redress and compensation offered and still make an appeal.

As required under the Framework, lenders have made customers aware in their initial offers of redress and compensation of their option to appeal, the relevant timelines and the option to bring a complaint to the FSPO and the courts.

[15] This relates only to customers included in the Examination.

4.3. Financial Services and Pensions Ombudsman and the Courts

Where affected customers have complained to their lender including where they remain dissatisfied with the outcome of their complaint, and do not accept the findings of the Appeals Panels, they also retain the option to bring a complaint to the FSPO. Customers deemed by their lender not to be affected by tracker related failures also have the right to make a complaint on their individual case within specific time limits set out in the FSPO's governing legislation.

The FSPO presents customers with a means of resolving their complaint in an independent, fair and transparent manner, which takes account of their unique personal circumstances, through an informal dispute resolution process or formal investigation (if not resolved through dispute resolution). The FSPO has the power to direct both compensation and rectification as appropriate. Final decisions of the FSPO are legally binding on both the customer and on the lender, subject only to an appeal to the High Court.

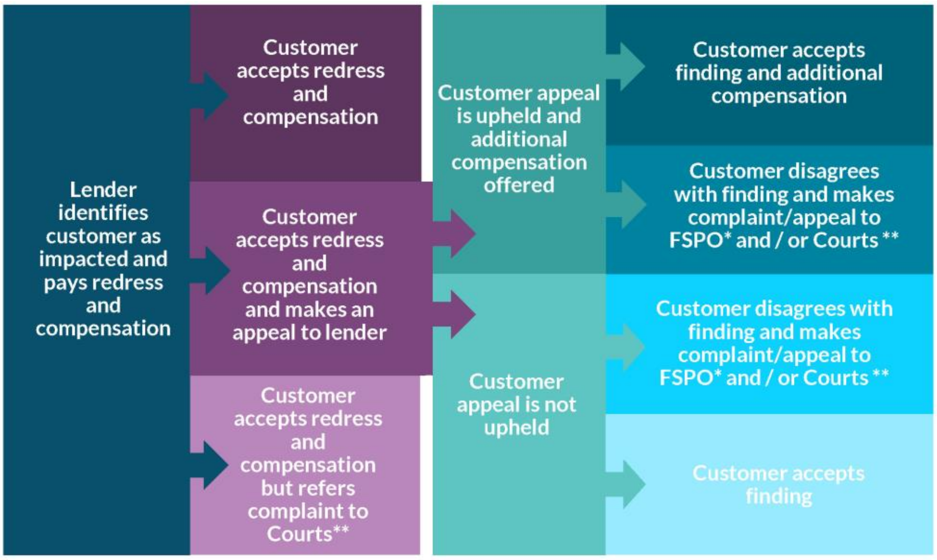
Given that the FSPO considered that the most effective and efficient way to provide redress and compensation to borrowers was for the lenders to co-operate fully with the Central Bank's Examination, it decided, in consumers' best interests, to put their complaints on hold pending the outcome of the Examination.[16]

However, as the supervisory phase of the Examination is now concluded, the FSPO is progressing, where possible, some previously paused complaints. Customers also have the right to directly initiate court proceedings outside of the appeals process and the FSPO, within a specified period of time. Chart 9 below sets out the processes available to customers.

---

[15] Presentation to the Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach by Financial Services and Pensions Ombudsman, 7 December 2017

Chart 9: Tracker Mortgage Examination: Process for Impacted Customers



Note: Processes for impacted customers are subject to certain time limits. Accordingly customers are required to take steps in the processes within those time limits.

***FSPO:** An independent officer whose remit is to investigate, mediate and adjudicate unresolved complaints of customers about financial services and pension providers. If a customer remains dissatisfied with the legally binding decision of the FSPO, the customer can appeal to the High Court (within 35 days of the FSPO decision).

****Court:** Any customer can take a claim through the courts system in respect of contractual and non-contractual issues related to their mortgage account.

5. Enforcement Update

The Central Bank seeks to enhance confidence and trust in the financial system through high quality regulation, purposeful engagement, effective gatekeeping, assertive supervision and robust enforcement.

We use our suite of enforcement tools to hold firms and individuals to account, to achieve the highest regulatory standards of compliance and to prompt firms to promote a customer focused culture from the top down. The outcomes of the supervisory phase of the Examination have been fed into our ongoing enforcement investigations. These investigations, which are comprehensive and forensic in nature, involving extensive document collection and review exercises and interviewing of former and current employees of the lenders, are considering the actions of firms and also the actions of individuals. The investigations are seeking to establish the exact circumstances of how and why customers lost their trackers and how lenders dealt with complaints relating to tracker mortgage issues.

The investigations are seeking to establish the exact circumstances in which customers lost their trackers

In addition, arising out of the supervisory assurance work undertaken as part of the Examination, the Central Bank is investigating instances where lenders may have failed to have the requisite safeguards in place to ensure that they implemented the 'Stop the Harm' principles properly and as a result may have failed to prevent further detriment to customers occurring after the Examination commenced. Whilst the Central Bank cannot comment on the specifics of ongoing investigations, it can confirm that as the investigations were commenced at different times, they will conclude on different timelines. The Central Bank last month reprimanded and fined one lender for tracker mortgage failures.[17]

Finally, arising from the information procured through our supervisory and enforcement work, the Central Bank will consider deployment of its toolkit, as appropriate, where fitness and probity concerns arise. For example, where tracker related behaviours investigated give rise to concerns in respect of the competency, honesty or integrity of individuals who are subsequently proposed for appointment to senior positions, the Central Bank will ensure that it exercises its gatekeeper function to appropriately challenge these individuals as part of its pre-approval process.

17 https://www.centralbank.ie/news/article/press-release-enforcement-action-permanent-tsb-30-may-2019.

6. Strengthening the Regulatory Framework for Supervising Financial Conduct

In the decade since the financial crisis, there have been a wide range of financial misconduct scandals around the world, while the Tracker Mortgage scandal has demonstrated the scale of the damage that was caused to Irish consumers.

The economic consequences of these conduct and compliance failures have been enormous.[18] The Chair of the Financial Stability Board noted in 2017 that global banks' misconduct costs had reached over $320 billion – capital that could otherwise have supported up to $5 trillion of lending to households and businesses.[19] In Ireland, lenders have taken combined provisions of €1.1 billion to cover both the costs of redressing and compensating their customers for tracker issues and the related administrative costs.

These failures have damaged the already fragile public trust in financial institutions - many of which had been bailed out at enormous public cost during the financial crash. This lack of trust was particularly evident in Ireland - of 28 markets surveyed as part of the Edelman Trust Barometer 2018, Ireland was the least trusting of its financial services sector.[20]

These failures have damaged the already fragile public trust in financial institutions

Similarly, the G30 noted that banks and banking rely on trust and that while trust takes years to establish, 'it can be lost in a moment through failures caused by problematic ethics, values and behaviours.' The G30 recommended that 'the banking community as a whole needs to repair the damage done by failures in culture, values, and behaviours, and should tackle the challenge with renewed vigour and purpose to achieve tangible improvements in outcomes and reputation.'[21]

The Central Bank regularly reviews the legislative, regulatory and policy framework within which it operates to assess the extent to which changes may be necessary. In the immediate aftermath of the financial crisis, for

[18] Examples of high-profile conduct scandals since the financial crisis are highlighted in the G30's November 2018 report: Banking Conduct and Culture, A Permanent Mindset Change
[19] https://www.bis.org/review/r170322d.pdf
[20] Edelman Trust Barometer 2018.
[21] See Banking Conduct and Culture. A Call for Sustained and Comprehensive Reform

example, the regulatory and supervisory frameworks were considerably strengthened.[22]

However, the persistence of international and domestic misconduct has highlighted why a robust regulatory system – coupling assertive supervision with strong redress and enforcement powers – will remain paramount in order to safeguard stability and to protect consumers. In keeping with that objective, and working within national and international frameworks, the Central Bank continually evolves our system for supervision for the regulated financial services sector as a whole. Our work in the Examination will feed in to that process.

The Central Bank is enhancing is approach to supervising conduct and culture

In line with the increased international and national focus on financial conduct, the Central Bank has in recent years taken a number of actions to enhance its approach to conduct supervision which we summarise below.

6.1. Development and Roll-Out of an Enhanced Supervisory Tool to assess Consumer Risk

Recognising the fundamental importance of risk management in achieving the necessary shift in culture, in March 2017 the Central Bank published the Consumer Protection Risk Assessment Model.[23] The CPRA assists supervisors in assessing how firms identify and manage risks to consumers. It enables supervisors to assess the extent to which firms understand the risks faced by their consumers, not only from the products and services they offer, but also from the behaviour of the firms themselves and that of the wider market. The CPRA has strengthened our supervision of conduct risk and complements our sectoral thematic supervision with an intensified firm-specific focus.

6.2. Enhanced Approach to Financial Conduct Regulation

The Central Bank's mission is to serve the public interest by safeguarding monetary and financial stability and by working to ensure that the financial system operates in the best interests of consumers and the wider economy. It seeks to deliver on its mission through its combined central banking and regulatory mandates.

22 See Appendix 1 of the Behaviour and Culture Report for an account of the evolution of regulation and supervision since the crisis.

23 https://www.centralbank.ie/news-media/press-releases/central-bank-introduces-new-consumer-protection-risk-assessment-model

In 2017, the Central Bank announced a significant re-structuring with the creation of the new Financial Conduct and Prudential Regulation Pillars. In the ensuing two years, the Central Bank enhanced its financial conduct strategy further to protect consumers and investors.

As outlined in our strategic plan 2019-2021, one of the Central Bank's main areas of strategic focus over the next three years is strengthening consumer protection, including the implementation of this enhanced approach to financial conduct regulation. This includes a greater focus on the culture and behaviour of firms and those who run them.[24]

Importantly, we recognise that prudential and conduct regulation are intertwined. Financially unsound firms pose grave threats to consumers and investors. In a similar vein, we recognise that macro-financial stability and conduct regulation are intertwined: the Irish public is well aware that systemic instability is deeply damaging for consumers and investors.

6.2.1. Review of the Behaviour and Culture of the Irish Retail Banks

During the course of the Examination, the Central Bank detected a number of cultural indicators that were standing in the way of effective consumer outcomes. For example, we found banks adopting an overly narrow approach rather than embracing a customer-focused perspective; assigning insufficient resources to the Examination; or offering initial compensation proposals that fell well short of our expectations.

At the request of the Minister for Finance we conducted a review of the Behaviour and Culture of the five Irish retail banks: Allied Irish Banks, Bank of Ireland, KBC, Permanent TSB and Ulster Bank. In July 2018, we published a report which detailed our findings.[25]

On the positive side, the reviews found that all five banks had recently taken steps to reinforce consideration of the consumer interest. However, the consumer-focused cultures at these banks remained under-developed and all five banks still had a considerable distance to travel.

Banks have a distance to travel to embed a consumer-focused culture

Following on from the Behaviour and Culture Reviews, we requested the five banks to develop action plans to mitigate the risks identified in our reviews. During 2018, we met with the boards of the five main lenders to set out our expectations in relation to conduct and culture issues.

[24] See Central Bank's Strategic Plan 2019-21

[25] The Behaviour and Culture of the Irish Retail Banks. See Section 3 which details the Central Bank's work to mitigate conduct risk, including risks stemming from ineffective culture, within firms

While culture is a matter for each individual bank in the first instance, supervisors monitor, assess and influence culture within firms in order to guard against conduct risk and drive better outcomes for consumers. In that respect, the Central Bank expects regulated financial services providers to have comprehensive risk management frameworks in place, including conduct and consumer risk frameworks, and to manage these risks effectively. We will therefore closely monitor and challenge the delivery by the banks of their behaviour and culture plans over a multi-year cycle. Over the immediate term, we will expect to see significant developments by each bank in terms of behavioural and structural changes and the design of controls that will support a sustainable cultural change. Over the medium- to longer-term, we will expect to see concrete evidence of the effectiveness of these behaviours, structures and controls.

6.2.2. Individual Accountability Framework

Internationally, it is recognised that culture must be continually managed and monitored at a senior level within firms. While there are already elements of such a monitoring regime in the Irish and European regulatory framework, including the Fitness & Probity Regime, the Central Bank is of the view that enhancing individual accountability is integral to the regulation of firms and individuals in financial services, and will help to foster more effective culture and clarity of responsibilities so that staff and senior managers within firms promote consumer interests and proactively address problems. We have recommended a new Individual Accountability Framework which would apply to banks and other regulated financial service providers.[26] The proposed Individual Accountability Framework consists of four key elements:

Enhancing individual accountability will help to foster more effective culture

- the introduction of a Senior Executive Accountability Regime ('SEAR') to ensure clearer responsibility and accountability by placing obligations on firms and senior individuals within them to set out clearly where responsibility and decision-making lie for their business;
- enforceable Conduct Standards which set out the basic standards of behaviour the Central Bank expects of regulated firms and the individuals working within them;
- enhancements to our enforcement processes to cater for the introduction of enhanced individual accountability, particularly at

[26] These recommendations were contained in our submission to the Law Reform Commission in January 2018 and again in our July 2018 report to the Minister for Finance.

senior levels, so the Central Bank may pursue individuals directly for their misconduct under the Administrative Sanctions Procedure; and

- enhancements to the current Fitness and Probity ('F&P') regime to strengthen the onus on firms to proactively assess the fitness and probity of key staff, and to enhance the Central Bank's oversight function of these staff.

The Central Bank considers these reforms to be necessary enhancements to its supervisory and enforcement toolkit in order to deliver an effective and credible individual accountability framework which supports achievement of the stated objectives. While the proposed reforms are ultimately a matter for the Oireachtas, the Central Bank is actively engaged with the Department of Finance in the development of legislative provisions in the context of the proposed Central Bank (Amendment) Bill.

6.2.3. More Intrusive Supervision

The Central Bank has also committed to conducting more frequent, targeted conduct supervision of those firms that pose the greatest potential harm to consumers, including robust challenge of boards and executive management. This will substantially strengthen our supervision of conduct risk and will complement our sectoral thematic supervision with an intensified firm-specific focus. We will accordingly scale up our conduct supervision resources to support this model.

The Central Bank will conduct more frequent, targeted conduct supervision of those firms that pose the greatest potential harm to consumers

Those firms that have a lower potential adverse impact will continue to be supervised through thematic and event-driven supervision, with the Central Bank taking targeted enforcement action against firms across all impact categories whose poor behaviour risks jeopardising consumer protection.

It is inevitable that future consumer protection issues will arise that could not reasonably have been foreseen or that may be the result of fraud, criminal conduct or human error. In those circumstances, it is crucial that regulated firms swiftly remediate any consumer detriment.

The Central Bank works to ensure that our system of supervision is kept under continuous review, and that where systemic issues arise, we take corrective action to ensure consumer detriment is redressed. The Tracker Mortgage Examination has demonstrated our determination to deliver on that commitment.

T: +353 (0)1 224 6000
www.centralbank.ie

Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem