

FINANCE  
FINANCIAL REGULATION

# Credit Servicing: Will the Irish regime need to change?

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At the start of 2019, the Irish credit servicing regime was expanded so that holding legal title, determining overall portfolio strategy, and maintaining control over key portfolio decisions in respect of residential mortgage loans, or in respect of SME mortgage loans originated by a regulated entity, now triggers an authorisation requirement. What impact will the proposed EU Credit Servicing Directive have on the Irish regime? This briefing looks at the background to the EU proposal, and what effect it might have in Ireland.

## BACKGROUND

In March 2018, the European Commission (the “**Commission**”) published its proposal for a directive on credit servicers, credit purchasers and the recovery of collateral (the “**Proposed Directive**”). The parts of the Proposed Directive dealing with a suggested accelerated extrajudicial collateral enforcement procedure (known as the “**AECE**”) were split out from the Proposed Directive when it became apparent that reaching consensus on the AECE would be a slow process. As there is considerable will at EU level to progress other aspects of the Proposed Directive that are designed to develop and support a well-functioning secondary market for non-performing loans (“**NPLs**”), the remainder of the Proposed Directive is moving ahead.

In light of this, we are not focusing on the AECE in this briefing, and will publish a separate update on that element of the Commission's proposal when it progresses further.

## SCOPE

In its current form, the Proposed Directive will apply:

- to servicers and purchasers of credit agreements that were originated by licenced EU banks (or EU subsidiaries of those banks);
- irrespective of the type of borrower - this means that it will apply

to credit agreements issued to individuals, incorporated bodies and unincorporated bodies; and

- to personal and business loans, secured and unsecured loans, and sales on the secondary market of both performing loans and NPLs.

The Proposed Directive will not apply to:

- loans serviced by licenced EU banks or their EU subsidiaries;
- the servicing of loans originated by non-bank lenders;
- the purchase of performing loans or NPLs by licenced EU banks or their EU subsidiaries; or
- loan sales that took place before the Proposed Directive comes into force.

## KEY AIM: WELL-FUNCTIONING SECONDARY MARKET FOR NPLS

As a consequence of the 2008 financial crisis and subsequent recession across the EU, many EU banks still have high volumes of NPLs on their balance-sheets.

The ratio between NPLs and the total loans extended by EU banks remains extremely high. High levels of NPLs require banks to hold higher amounts of regulatory capital and pay a risk premium in the liquidity markets.

The Commission's key aim, when introducing the Proposed Directive, was to tackle the NPL issue through encouraging the development of well-

functioning secondary markets for NPLs by establishing an EU-wide framework for credit servicers and credit purchasers.

In many ways, the Proposed Directive follows a similar approach to the European Central Bank's work on NPLs which borrowed from the Irish and Spanish rules on credit servicing and reducing NPLs.

It is important to note that the Commission views the functioning of secondary NPL markets as a cornerstone of its plans for a capital markets union. It recently published its new [Capital Markets Union Action Plan](#), and put forward proposals to remove regulatory obstacles to securitisations of NPLs. For further information, read our recent briefings: [Capital Markets Union: A “new, ambitious” Action Plan](#) and [Securitisation Regulation: Disclosure, Synthetic Securitisations and Non-Performing Exposures – What you need to know](#).

## KEY PROPOSALS

### • Authorising credit servicers

The Proposed Directive seeks to introduce a harmonised authorisation framework to allow credit servicers to scale up their activities in different EU Member States for the first time by using a passport. Credit servicers would be subject to uniform and harmonised conditions for authorisation, and to harmonised conduct of business rules, across the EU.

• **Loan sales**

The Proposed Directive sets out rules aimed at increasing transparency when loans (both performing and non-performing) are offered for sale in the secondary market.

Those rules would require the in-scope **sellers** to provide all necessary information to a credit purchaser prior to entering into a loan sale contract.

The rules would also require **sellers** of in-scope loans to notify the relevant competent authority (in Ireland, this is expected to be the Central Bank of Ireland) of the sale of in-scope credit agreements.

Credit **purchasers** will also be required to notify the relevant competent authority when they plan to take enforcement action in respect of a loan.

**Non-EU purchasers** of consumer loans will be required to appoint an authorised EU credit servicer, a licenced EU bank, or a subsidiary of a licenced EU bank, to service those loans.

**IMPACT ON IRELAND**

On transposition of the Proposed Directive, the current Irish credit servicing regime is likely to require amendment to align it with the requirements of the Proposed Directive. This could mean that, for post-transposition loan sales, the credit servicing regime will resemble the pre-2019 Irish credit servicing regime.

**Why is that the case?**

**The Commission's intentions are clear**

The Commission's intentions are clear from the Recitals to the Proposed Directive where it notes that:

- as investors on secondary markets are buying existing credit at their own risk and do not cause prudential concerns, there is **no justification for requiring those types of investors to apply for an authorisation** or to set special conditions for them to engage in such activities. Therefore, unlike the current Irish credit servicing regime, the Proposed Directive does not envisage the activity of holding legal title to a credit agreement as being an activity that requires authorisation;
- it is important that EU and national

consumer protection rules continue to apply once a loan has been sold and that the borrowers' rights continue to be those arising from the initial credit agreement – but the premise of the Proposed Directive is that this will be achieved by authorising the credit servicer and not the credit purchaser. While the Proposed Directive imposes some secondary reporting obligations in respect of loan sales (such as the requirement that the seller provide details of the purchaser to the designated competent authority), **the Recitals to the Proposed Directive make clear that there is no intention to require credit purchasers to be authorised.**

**Scope of what constitutes 'credit servicing'**

As currently drafted, the definition of a "credit servicer" in the Proposed Directive does not, in contrast to the existing Irish credit servicing regime, trigger an authorisation requirement in respect of any of the following activities:

- holding the legal title to a credit agreement or acquiring a credit agreement;
- determining the overall strategy for the management and administration of a portfolio of credit agreements; or
- maintaining control over key decisions relating to such portfolio.

These three activities have triggered an authorisation requirement in Ireland since January 2019.

Instead, the Proposed Directive defines a "credit servicer" as any natural or legal person, other than a credit institution or its subsidiaries, which carries out one or more of the following activities on behalf of a creditor (i.e. any person who has issued/acquired credit):

- monitoring the performance of the credit agreement;
- collecting and managing information about the status of the credit agreement, of the borrower and of any collateral used to secure the credit agreement;
- informing the borrower of any changes in interest rates, charges or of payments due under the credit agreement;
- enforcing the rights and obligations

under the credit agreement on behalf of the creditor, including administering repayments;

- renegotiating the terms and conditions of the credit agreement with borrowers (where they are not a credit intermediary); and
- handling borrowers' complaints.

As noted above, this definition does not include the three additional activities which have triggered an authorisation requirement in Ireland since January 2019 under the Consumer Protection (Regulation of Credit Servicing Firms) Act 2018.

As the current Irish credit servicing regime covers a much broader range of servicing activities than the Proposed Directive, and as the Recitals to the Proposed Directive make it clear that the Commission did not intend to require credit purchasers to be authorised, it is likely that the current Irish credit servicing regime will have to be amended to remove the three new authorisation triggers that were added in 2019.

**Credit servicers will be able to passport their activities**

Post implementation, Irish licenced credit servicers will be able to use a passport to provide credit servicing activities across the EU.

**TIMELINE**

The Commission's original proposal envisaged the Proposed Directive being transposed into national law by 31 December 2020, with most provisions coming into force from 1 January 2021.

However, the Proposed Directive is still under discussion and first reading by the EU Council.

As the Proposed Directive remains a core legislative deliverable for the EU, and as the proposed AECE has been separated out for further discussion, we anticipate that the Proposed Directive will perhaps be rescheduled for implementation in late 2021 or 2022.

It is possible that further changes may be made to the Proposed Directive as it moves through the EU legislative process, and we will publish further updates as the final shape of the Proposed Directive becomes clear.

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