The Change in Monthly Repayment Calculations

Understanding what it means for you and your mortgage

If you have been advised of a change to your monthly repayment calculation, you may have questions on what this change means for you, what the old calculation meant for your mortgage and what the new method will mean. Below we set out an example and describe the differences under the two calculations, to explain how this works.

This is Mary, she is a working mother. Mary has in the past struggled to meet her mortgage repayments but is finding it easier now. Due to her financial difficulties in the past, however, Mary has an arrears balance on her loan.

Below we illustrate the affect that the method of calculating her repayments on the full balance of her loan has had on Mary's loan repayments over the last 10 years.

Mary took out a loan for €250,000 10 years ago to purchase her current family home, her loan was for a term of 20 years. Mary's mortgage loan is on a tracker rate linked to the European Central Bank (ECB) rate.

Mary suffered some financial difficulty in 2010 – 2014, her hours were reduced at work and she faced a lot of medical bills as her daughter was ill. During that time Mary missed a number of repayments, which resulted in an arrears balance of approximately €15,000 by June 2014 (a balance of missed payments). Her difficulties continued to the end of 2014, at the end of that year Mary's arrears balance was over €20,000.

Although Mary has recovered financially to the extent that she can again meet the repayments on her mortgage, she is not in a position to address the arrears balance.

At the moment Mary's outstanding balance is a little over €160,000. She has a reported arrears balance in excess of €20,000 and the capital balance is approximately €140,000 (the remaining balance of the amount originally borrowed). There are 10 years left on her loan.

There has been one reduction to the ECB interest rate during the life of Mary's mortgage, resulting in a reduction to her mortgage rate and a recalculation of her monthly repayments.

Overleaf we illustrate the difference in Mary's monthly repayments under the calculations of her repayments based on the current practice and the new practice.

This is an illustration of the practice and its impact on Mary's account, it does not describe any resolution that might be offered to Mary.

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Calculation 1 Old Method of Recalculation based on Full Balance Plus Interest Repayments:	Calculation 2 New Method of Recalculation based on Scheduled Capital and Interest Repayments
When Mary originally drew down her mortgage loan, her repayments were €1,324.76 per month. Her rate was 2.5%.	The repayments at commencement of the loan are the same under both repayment calculation methods.
In **March 2016,** there was a reduction in the interest rate. At that time Mary's arrears balance was €21,196 Under calculation 1, Mary's repayments were recalculated based on the full balance of her loan, this included the arrears, plus interest. The interest rate was reduced from 2.5% to 2%, however Mary's repayments increased to €1,450.06 The bank, although adding the arrears to her monthly repayments, retained a reported arrears balance.	Under calculation 2 when a rate change is applied on a loan the repayments are calculated based on the remaining capital balance (not including the arrears) plus interest. In **March 2016**, the capital balance (the remaining balance of the amount borrowed) on Mary's mortgage was €159,733 and her arrears balance was €21,196. If her repayments were calculated based on calculation 2 in **March 2016**, Mary's repayments would have reduced to €1,280.18
By **November 2017**, Mary has been meeting the mortgage repayments for four years. Despite the fact that she is paying the higher repayments, her arrears have not reduced. They remain at €21,196. By the end of **November 2017**, the full balance outstanding on Mary's loan is €161,043. As all repayments are applied to the loan under both calculations, the balance is the same.	As Mary's repayments have been calculated under Calculation 1, she has been making higher repayments than she would have done under calculation 2. If the additional amount paid had been used to reduce her arrears balance, by **November 2017** Mary's arrears balance would be reduced to €17,798. By the end of **November 2017**, however, the full balance outstanding on Mary's loan is €161,043, the same as under calculation 1.

The Effects of Higher Repayments.

- Mary was required to pay more per month to meet her repayments.
- As the additional amount was not used to reduce her arrears balance, rather it was allocated to the capital balance. In order to reduce her arrears balance, Mary would have had to make payments in excess of the higher monthly repayments under calculation 1 each month.
- Therefore this calculation method made it harder for Mary to address her arrears balance.
- The outstanding balance on the loan was not affected by the calculation of repayments based on the full balance outstanding, as all payments made on the loan were deducted from the outstanding balance under both calculations.