IRISH INDEBTEDNESS

The issue of personal debt and the ability to repay is one of the most significant pressures now facing Irish families, especially young families and individuals.

The fact that we are a modern consumer society, with a dependency on credit, means that it is critical we now establish a principles based system allowing for debt resolution in a way that limits overall costs to society. In essence this means a modernisation of our Bankruptcy laws. The 'Moral Hazard' issue is valid but we cannot allow debt in itself become all consuming as it has the potential to do, because of our particular Irish set of personal debt circumstances.

We need to create the correct balances between the rights and obligations of creditors expectation of repayment and debtors ability to pay.

Debt forgiveness or structured write down has to be earned - there cannot be any suggestion of a free lunch or allowing for free riders. Abuse of any reformed system should be dealt with in a more stringent manner than that which exists previous to adoption or availing of the proposed system.

The governments most significant input in dealing with Irish indebtedness has to be reform of bankruptcy laws.

Work around debt in Ireland is reactive in nature, occurring generally when an individual is already over-indebted. This needs to change.

The issue can be broken down to two broad catagories:

Secured Debt (Mortgages)
Personal Unsecured Debt (Bank and Credit Union Loans, Credit Card, Utility)

Mortgages

792,893 mortgages are held by owner occupiers to a value of €118.3 Billion
It is estimated that 196,000 will be in negative equity by the end of 2010

Negative Equity in its own right should not be a financial problem once employment can be maintained and the family regard the house as their home, however you cannot discount the psychological impact it has on the individual and families in relation to their own financial confidence.

Mortgages in Default: Under the definition of more than 91 days in arrears there are currently 28,600 (3.6%)
Figures for households in arrears for any duration are estimated at 77,500
8,328 mortgage holders in arrears have entered the legal process

The available options at the moment seem to centre around renegotiation of the loan, the question about banks further profiting from this needs to be asked. There is also a need to look at penalties charged by banks in relation to interest on arrears, redemption fees paid to banks on changing mortgage rates and any potential stealth charges.

Equity sharing arrangements between State, Banks and Homeowners is a debate that is beginning. The possibility of transferring ownership of homes to a national

housing agency with subsequent rentback by the current owners is in operation in some countries (HFA Ireland, Voluntary Housing Agencies)

Mortgage Debt has because of the Irish persons traditional attachment to home ownership been the debt that the person will continue to make every effort to pay. There has to be a limit or a tipping point at which this becomes difficult and in travelling to this position there is probably carnage associated with additional unsecured personal debt.

The fact that Irish Banks are now beginning to independently raise interest rates (TSB, BoI) without recourse to the ECB rate will immediately put more pressure on Irish households.

The fact that we now have an obvious two tiered European economy tied to the fact that France and Germany are pathologically fearful (for historical reasons) of inflation and will ultimately increase the ECB rate to deal with it implies that Irish homeowners face the double hit of Irish Banks increasing their margins through interest rate rises to resume profitability and France/Germany increasing the ECB rate to deal with any potential inflationary problems.

A 1% rise in rate implies €50 rise per €100,000 borrowed

POTENTIAL SOLUTIONS

Mortgage Indemnity Insurance for all high LTV loans (those in excess of 70%). This system has been used in other economies and was used in Ireland up until the mid 1990's

Equity Sharing Agreements. Models such as the current local authority Shared Ownership Scheme.

PERSONAL DEBT

In 1995, Ireland had a household debt (including mortgages) to disposable income ratio of 48. By 2008, this had risen to a ratio of 176, an increase of almost 270%. This rise is much higher than for four other countries (Spain, UK, Canada and France) where similar comparative data sets exist.

See Appendix 1

In Ireland, there is a lack of formal insolvency schemes and the current bankruptcy system is unsuitable for a majority of current debtors. By contrast, there are personal insolvency options in England and Wales and the US. Ireland needs to address this shortcoming as quickly as possible.

The Central Bank estimates that non-mortgage related debt amounts to 18% of all debt in Ireland. Total household debt including mortgages stands at €147 Billion implying personal debt of approx €27 Billion.

Over the last two years, however, the levels of outstanding debt decreased in six of the nine types of debt to credit institutions. Only overdrafts, other loans and securities and credit cards increased from 2008-2010. This fact in itself is interesting in two ways in that all of these types of debt involve higher rates of interest and are debts that are left to pay until after the mortgage (fear of loss of home or eviction) and after the utilities (fear of disconnection).

See Appendix 2

There are interesting statistics from MABS in relation to the period 2008-2009

Analysis shows that from 2008-2009, levels of debt among MABS clients increased across most debt types. Personal loans with financial institutions, utilities, and credit cards form the largest proportion of debt, four types of debt experienced increases of over 70% from 2008-2009 These include the following:

Sub-prime (82.5%),Overdraft (75.4%),Hire purchase loan (72.1%),Catalogue (70.8%)

The necessity to prioritise debt, particularly secured debt over unsecured debt may result in the debts with the highest interest rates being paid last. This may mean that it will take longer overall to exit from debt.

POTENTIAL SOLUTIONS

The Individual Voluntary Arrangement

An Individual Voluntary Arrangement - IVA is a formal agreement between you and your creditors where you will come to an arrangement with people you owe money to, to make reduced payments towards the total amount of your debt in order to pay off a percentage of what you owe then generally after 5 years your debt is classed as settled. Due to its formal nature, an Individual Voluntary Arrangement - IVA has to be set up by a licensed professional called an Insolvency Practioner (IP)

Its Purpose?
It is a legally binding agreement between you and your creditors (people you owe money to). It helps those in financial difficulties to make a formal proposal to settle their debt.
What Are The Arrangements?
Monthly payments are based on an affordable disposable income. Once the final payment is made, any outstanding debt is legally written off. The arrangement can write off up to 65% of your debts (subject to your circumstances).

How does it work?
Debts are settled within a reasonable and fixed period of time (normally 5 years). Any interest and debt charges will be frozen and creditors will be prohibited from demanding additional payments.

Once a decision has been made that an Individual Voluntary Arrangement - IVA is right for you, you will be asked questions regarding your current financial situation. Based on the information you have given, a repayment amount will be agreed with you. Once proposals have been drawn up you will need to check and sign these and return them to your Insolvency Practitioner (IP).

An application may then be made to the court for an Interim Order. Once this is in place, no creditors will be able to take legal action against you. You may be asked to attend your creditors meeting but this rarely happens, normally you are asked to be contactable by phone on the day.

For an Individual Voluntary Arrangement - IVA to be approved, creditors will be called upon to vote either for or against the arrangement. If only one creditor votes "for" the Individual Voluntary Arrangement - IVA, the Individual Voluntary Arrangement - IVA will be approved. However, if only one creditor votes against the Individual Voluntary Arrangement - IVA and they represent less than 25% of your total debt, the meeting will be suspended for a later date and other creditors who did not vote will be called upon for their vote.

If the creditor who voted against the Individual Voluntary Arrangement - IVA represents more than 25% of the total debt you owe the Individual Voluntary Arrangement - IVA will fail. This is because an Individual Voluntary Arrangement - IVA will only ever be approved if 75% in monetary value is voted for. If any of the creditors don't vote on the meeting day they will still be bound by the IVA if it is accepted by your voting creditors .

The Individual Voluntary Arrangement - IVA will be legally binding. As long as you keep up the repayments, when the term of your agreement is finished, you will be free from these debts regardless of how much has been paid off.

During the period of your arrangement your financial situation will be reviewed regularly to see if there has been any change in your circumstances.

It is very important that consumers do not confuse an Individual Voluntary Arrangement - IVA with a Debt Management Plan, which are not legally binding.

Most Individual Voluntary Arrangement - IVA cases are based around one, affordable, monthly, payment, over a period of 60 months. This one affordable payment is based on your earnings minus your expenses.

An Individual Voluntary Arrangement - IVA proposal has to be prepared by a licensed Insolvency Practitioner (IP) who then presents it to creditors at a creditors meeting.

In the case of a consumer Individual Voluntary Arrangement - IVA it is unusual for any creditors or their representatives to attend the creditors meeting as most prefer to vote by fax or by post.

The rules of an Individual Voluntary Arrangement - IVA state that providing 75% (in value terms) of those that have voted, vote to accept the proposals (with or without modifications) then the Individual Voluntary Arrangement - IVA is agreed and becomes legally binding on all other parties whether they voted or not.

When an Individual Voluntary Arrangement - IVA is accepted the IP's role becomes that of supervisor, monitoring the Individual Voluntary Arrangement - IVA's progress and ensuring that the terms and conditions that were agreed to at the creditors meeting are properly adhered to.

It is the debtor's responsibility to pay the agreed payments to the IP who will then ensure that these payments are distributed to all creditors on a pro-rata basis in accordance with terms and until the successful completion of the Individual Voluntary Arrangement - IVA. It is in the debtors own interest to maintain their payments as failure to pay will almost certainly result in the failure of the Individual Voluntary Arrangement - IVA.

Upon the successful completion of the Individual Voluntary Arrangement - IVA the debtor will be considered debt free even though they may not have actually paid off all of their debts in full. Any outstanding balances are written off (known as a composition of debts) and the debtor is then free to make a fresh financial start.

It is worth noting that if you do enter into an Individual Voluntary Arrangement - IVA with your creditors and you have an endowment policy linked to your mortgage then you may be expected to cash it in and pay the proceeds into the arrangement. Likewise, if your property has a reasonable amount of equity then it is likely that a some of it will have to be released at sometime during the arrangement (usually the end), so it can be paid to creditors. Drastic as this may sound it can be a deciding factor in whether an Individual Voluntary Arrangement - IVA is approved by creditors and a realistic way in which a debtor can retain their property.

Appendix 1

Household debt to disposable income ratios - percentage change 1995-2006

Country	1995	2008	% increase
Ireland	48	176	267
UK	106	173	63
France	66	72	9
Spain	59	130	120
Canada	103	130	26

Source: Goodbody (cited by Amárach)

Appendix 2

Aggregate amounts outstanding to credit institutions by Irish residents 1999-2010 (€ millions)							
2000	**2002**	**2004**	**2006**		**2008**	**2010**	**% change (2000 to 2010)**
Overdrafts	7,798	7,632	6,966	7,389	8,104	8,770	12%
Repurchase agreements	172	752	921	457	1,615	763	344%
Loans up to and including one year	23,651	21,933	19,834	32,381	58,679	55,789	136%
Term/ revolving loans	38,009	60,440	67,510	95,382	137,345	130,434	243%
Instalment credit/hire-purchase /leases	3,337	4,720	3,595	3,659	3,651	2,461	-26%
Residential mortgages	31,816	40,647	61,460	92,765	118,984	109,770	245%
Other mortgages	5,535	7,520	9,875	11,974	17,862	14,996	170%
Other loans and securities issued to other residents	3,901	3,027	3,723	3,861	10,440	40,748	945%
Outstanding debt on credit cards	1,079	1,461	1,898	2,407	2,820	3,034	181%
Source: Central Bank Quarterly Bulletins							

The Mortgage Arrears & Personal Debt Review Group Task Force as established by the Minister last Spring does appear to be imbalanced. It does not include representation for consumer advocates with credible professional expertise in consumer indebtedness and consumer protection. People such as MABS, Credit Unions and Voluntary bodies such as the Vincent de Paul would offer a valuable perspective. These exclusions are telling. It is difficult to see how consumer interests can be fully, appropriately and expertly included for in the forthcoming report from the group as currently constituted. The recent comments by Mr. Elderfield the Financial Regulator, a member of this Task Force would seem to indicate the final report will be nothing more than window dressing and a sop to Irish people.

Mortgage debt is different from Personal debt in that it has a deep connection with peoples sense of security and safety in their family home, however following the figures released last week by the Financial Regulator in relation to the accelerating upward trend in Mortgage Arrears there is now evidence that people are shifting their debt priorities to unsecured personal debt in the form of Credit Cards and Overdrafts in order to ensure the basic essentials are catered for.

There are only two countries in Europe without Personal Debt Management legislation, namely Ireland & Greece. The Bankruptcy Act 1988 needs immediate reform and updating. The process of Examinership and Debt writedown is only for the wealthy, being a Court based system with High Court costs approximately tens of thousands of euro a day.

We in Ireland need to immediately introduce a system of non judicial debt settlement for Irish people and SME's such as the IVA (Individual Voluntary Arrangement) system in operation in the UK, pitched to operate at a level from €50000.

The period for a bankruptcy discharge application needs to be reduced from the current period of 12 years in order to cut off the possibility of Bankruptcy tourism gaining a foothold.