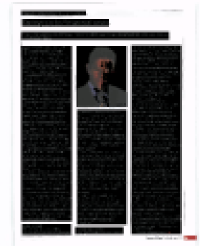
Publication: Business & Finance
Date: Friday, November 16, 2012
Page: 103
Extract: 1 of 2
Circulation: 20.000
Author: Sean Kelly
Headline: Facing up to financial woes



**Corporate restructuring** RSM Farrell Grant Sparks

# Facing up to financial woes

Sean Kelly examines the Personal Insolvency Bill to see if it can deal effectively with long-term and unsustainable debt.

Sean Kelly

The new Personal Insolvency Bill published in June, is a vitally important and complex piece of legislation which is designed to tackle the problem of personal over indebtedness, particularly in relation to unsustainable mortgage debt which represents 70% of the overall personal debt problem.

The legislation will affect the lives of large numbers of people who are in financial distress. It will have serious implications for our banks and the wider economy. It represents a radical, far reaching and innovative development for dealing with personal insolvency and bankruptcy in Ireland by way of reforming antiquated bankruptcy laws some of which have been in existence for over 100 years.

The most important and controversial aspect of the new relief concepts in the legislation is the Personal Insolvency Arrangement (PIA) which is tailored particularly for mortgage holders with substantial arrears on their loans and who are in negative equity. The PIA approach is designed to give borrowers with unsustainable levels of debt a means of tackling their financial difficulties, while also encouraging banks to be more flexible in their dealings with debtors and more willing to agree to non-judicial out of court settlements. A PIA allows for private individuals to enter into a scheme of arrangement with their creditors which allows for an element of debt forgiveness similar to the examinership model for limited companies.

Central Bank statistics confirm that there are in excess of 77,000 home owners or 10.2% of the residential mortgage market who are unable to pay their mortgages and are in arrears of 90 days or more. This amount to €22 billion of mortgage debt which is either in arrears of more than 90 days or is currently being restructured. The banks policy to date of making case by case arrangements with individual borrowers - including forbearance solutions and long-term extensions - is not working and is not capable of dealing effectively with the magnitude of the problem of long-term and unsustainable mortgage debt.

### Power of veto

When the draft insolvency Bill was published in January, one of the big talking points was the effective power of veto which the banks would have in relation to the PIA, in that if they voted against the arrangement, it would in practically all cases defeat the arrangement as it was proposed that the debtor needed 75% in value of his creditors to agree to the arrangement. In the published legislation, the 75% has now been reduced to 65% but in practice this will have little impact as in most cases the bank will be by far the largest creditor.

There are very few material changes to the published legislation from the draft Bill released in January but at the time, there were calls for the appointment of an independent mediator or arbitrator who would adjudicate on the fairness or otherwise of the proposed PIA or impose solutions both in relation to the proposed repayment schedule and how the shortfall would be dealt with. No such mechanism is provided for in the new Bill and this is a major weakness which needs to be addressed.

In addition, the legislation has not addressed the moral hazard issue by devising a mechanism to distinguish between those who cannot pay and those who will not pay before and write-downs can be considered. A formula should be determined in order to calculate an individual's ability to meet their obligations.

### Insolvency services

The Bill establishes a new state funded independent body to be known as The Insolvency Service which will oversee the entire process. The Bill also provides for the appointment of Personal Insolvency Practitioners (PIP) to investigate the debtor's financial affairs, formulate proposals, summon creditors meetings and oversee the individual arrangements. The PIP will be nominated by the debtor. It will be necessary to ensure that experienced and well qualified

Publication: Business & Finance
Date: Friday, November 16, 2012
Page: 103
Extract: 2 of 2
Circulation: 20.000
Author: Sean Kelly
Headline: Facing up to financial woes

professionals only are authorised to act as PIPs as they will be crucial to the success or otherwise of the process. A proper licensing and regulatory will need to be introduced in this regard.

The six year period for the implementation and duration of the PIA appears unduly protracted and offers little incentive for the borrower to commit to a lengthy period of potential economic hardship, particularly in circumstances where the 12-year term of bankruptcy has been reduced to three.

The legislation does not address the issue of the criteria which banks will use to access and evaluate the proposals contained within the PIA and how they will deal with the treatment of debt that will be required to be written off as part of the resolution of the individual's distressed debt. There will be a need for consistent, reasonable and fair criteria that banks will apply across the board in their evaluation of the proposals. The question of transparency of the process when the debtor's proposals are under review, will be fundamental to the success of this section of the legislation.

In practice, a realistic mechanism for the process to succeed would be for the debtor/borrower to procure an official professional valuation of their property, following which, the bank would agree to adjust the mortgage amount to the realistic value of the property (as per the official valuation) and write off the balance of the mortgage debt. It remains to be seen whether the banks would agree to any such proposal.

*Sean Kelly is a director of the Restructuring and Insolvency Department at RSM Farrell Grant Sparks. For further information, contact Sean at Sean.kelly@rsmfgs.ie or +(353) 1 418 2085, www.rsmfarrellgrantsparks.ie.* ■