Insolvency Service of Ireland Stakeholder e-Brief

August 2017

ISI
Tackling problem debt, together

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1 Introduction

This is the third edition of the Insolvency Service of Ireland's (ISI) e-Brief. This document along with other resources can be found in the Stakeholder Information section on our website.

2 Courts

2.1 Recent Court Rulings – High Court

McDonnell Case – Section 105 Valuation Process (where parties cannot agree secured property valuation)

A recent High Court judgment found that a PIP had not strictly followed the statutory procedural requirements under section 105.

Section 105 provides a four-step valuation process for secured debt.

- Step 1: Creditor to provide a valuation as per provisions of section 102.
- Step 2: Where a section 102 valuation not acceptable to PIP parties shall try to agree a valuation.
- Step 3: Where a valuation cannot be agreed, the parties shall appoint an independent valuer to determine the market value of the property.
- Step 4: Where the parties cannot agree on the independent person to be appointed under step 3, the ISI shall appoint an independent expert whose valuation shall be binding on the parties.

In this case, the outcome hinged on the secured creditor providing a list of its panel of valuers to the PIP – having already confirmed it would not release to the PIP a copy of its own valuation report - and the PIP rejecting anyone off that panel to provide an

independent valuation. On foot of that, the ISI was requested by the PIP to appoint an independent valuer.

The PIP did not explicitly confirm with the creditor that the section 105(3) request to the ISI was being made, and it was this specific provision that the Court found had not been followed in the correct manner.

Judge Baker held that the language in section 105 was mandatory and that the parties must engage in all four stages in the valuation process. Further, Judge Baker felt that the PIP moved too quickly to engage the ISI, and that he ought to have counter-proposed the creditor's suggestion by identifying an independent expert or experts, and awaited a response before moving to the next stage – involving the ISI.

Further, Judge Baker stated that she was not in a position to excuse non-compliance with the mandatory requirements, noting that the objecting creditor would suffer prejudice were she to do so, and were the Court to accept a valuation, which is lower than the one proposed by the creditor.

On the matter of the secured creditor not providing a copy of its written valuation to the PIP, the Court noted that the section requires the parties to endeavour to achieve a valuation openly, in good faith and by using their best endeavours. Judge Baker was of the view that a valuation proffered should be capable of being sustainable, supported by credible evidence, and not a hypothetical figure proposed for negotiation purposes, or a starting point, particularly in the context of not creating a need to apply for a PC extension.

In this regard, Judge Baker noted the ISI Stakeholder E-brief of May 2017, in which the parties in the valuation process were strongly urged to "engage meaningfully and as quickly as possible" in order to avoid the need for PC extensions, and while noting it had no legal force, it was, she stated, informative and explains the preferred approach of the ISI. A refusal to show a written report, Judge Baker noted, is "at best unhelpful

and unlikely to instil confidence in a proffered figure. A seriously made request for a valuation report should in general therefore not be refused without cause", and felt that such refusal in this case was indicative of a lack of good faith or of meaningful engagement in the valuation process required under the Act.

In relation to the ISI's role in engaging an independent expert, Judge Baker was of the view that

(i) the ISI does not have an obligation to satisfy itself that the parties had failed to agree a valuation or an expert to provide one, or

(ii) to ask for evidence on which it could be satisfied that its statutory role had been properly engaged.

As a result, the Court rejected the argument that because the ISI nominated an independent expert in performance of its statutory role, the process was deemed to have reached a stage where the statutory power had become exercisable.

Concluding, Judge Baker stated that there had been insufficient engagement by the PIP with the third stage, and was satisfied that he moved with undue haste to the fourth stage. She confirmed that the Circuit Court was correct in its approach, and that the valuation was not binding on the parties and not a relevant one for the purposes of the process, as it had not been achieved in accordance with the requirements of the Act. **Link**

2.2 Recent Court Rulings – Circuit Court

Class of Creditor Cases

In two cases heard during July, in the Dublin and Eastern Circuit Circuits, decisions were made in relation to the classification of a credit union as a separate class of

creditor under the Act for the purposes of Section 115A. The Courts had not previously recognised this class.

In the **Eastern Circuit (Kierans case),** Judge O'Malley Costello ruled a credit union (CU) to be a separate class of creditor. This was in circumstances where the CU was owed debt to the value of 3% of the debtor's overall debt value while representing 32% of total unsecured debt. Equivalent figures for the debtor's spouse were 2.9% and 40% respectively.

The judge noted that in this case, the other unsecured creditors (Cabot and AIB) were both owed unsecured credit card or personal debt. The question for the court was whether the credit union, classified by the PIP as a Mutual Lender class, was to be accepted by the Court as a separate class for the purpose of section 115A of the Personal Insolvency Acts.

Section 115A(17)(a) provides that the Court may consider one creditor or more than one creditor to be a class of creditor where the Court considers the creditors to have, in relation to the debtor, interests or claims of a similar nature. It further provides at sub-section (b) that in deciding whether to consider a creditor or creditors to be a class of creditor, the Court shall have regard to the overall number and composition of the creditors participating at the creditors meeting, and to the proportion of the debts due to the creditors participating and voting.

The question for the Court was whether, in relation to the debtor, the credit union and AIB and Cabot (who attended the creditors' meeting and voted) all held interests or claims of a similar nature. The Court noted that:

- all three debts were unsecured, though arguably the CU had some security in that the total sum owed by the debtors was reduced by the amount of their CU shares.
- although not conclusive, it was noteworthy that in the PFS, the CU was listed as a separate category from other financial institutions.

- while the interest of the various unsecured creditors would be similar in as much as the method by which their unsecured debt was collected was similar, the relationship that exists between a member of a CU (such as the debtor) and the CU is not similar to that which exists between the debtor and the other unsecured creditors.
- the CU was governed by the Credit Union Act 1997 and owes to its members particular duties. It is a mutual organisation owned by the members, of which the debtor is one. It is a non-profit organisation and must operate in the interests of its members with whom it shares a common bond.
- with regard to the second requirement of S115A, i.e. the number of debtors and the proportion of debt due to the credit union, if one leaves aside the amount due to the Bank in respect of its unsecured debt on the PPR, it would not be disproportionate in the overall to allow the CU to be considered as a separate class of creditor.
- it agreed with the assertion by the bank that the burden of proof is on the debtor to satisfy the requirements of the Personal Insolvency Acts. In this regard, the Judge opined that a greater concentration on the facts of the case rather than legal argument in the affidavits would save time and cost and long hearings as the Court tries to elicit the factual situation of the debtor.

In the second recent judgment of note, the **Dublin Circuit Court (Parkin case)**[1] similarly had to determine the class of creditor as a preliminary case issue.

The Court noted that:

- it had been argued that there were only two classes of creditors - secured and unsecured - supported by High Court authority, which had been cited,

[1] Both the Kierans and Parkin cases are subject to an appeal to the High Court.

and that the secured creditor had an escalated status to the unsecured creditor. Section 115A (17) introduced a new concept of different classes of creditors, which in the Court's view went beyond a simple matter of secured and unsecured.

- it was the intention of the legislature, envisaging a grouping of creditors with interests or claims of a similar nature, which went beyond simply secured and unsecured classes.
- in deciding under paragraph (a) whether to consider a creditor to be a class of creditors, the Court had regard to all of case circumstances including the statement of grounds filed by the applicant, the affidavits and submissions made in Court.

The Court specifically referred to the need to have regard to the overall number and composition of the creditors who voted, there being two creditors in this matter: PTSB, which happens to have secured and unsecured liability, and the CU with unsecured liability.

In these particular circumstances, the Court determined that section 115A (17) of the Act allowed for more than a classification of creditors into secured and unsecured. The Court opined that more than one class of unsecured creditor is provided for where the creditors concerned have similar interest or claims. The court determined that given the composition of the liabilities due and owing to the secured creditor, the secured creditor and the CU did not share a common interest. The test to be applied is in respect of claims of a similar nature and a common interest and that the common interest is really the prevailing factor in terms of establishing a class. In this case, given the particular circumstances and the makeup of the PTSB debt, the Court was of the view that the CU is a separate class of creditor given that there are only two creditors.

Dublin Circuit Court (Parkin case) – Other issues

Of further interest in this case is that having dealt with the preliminary class issue, the Court proceeded to approve the Arrangement. In doing this, the Court rejected the three objections of the main creditor (PTSB) which were:

1. Unfair prejudice
2. The secured creditor's counter proposal to the debtor's proposal represented a fair outcome, that it was not properly considered by the PIP and her rejection of it represented an error of law and
3. The existence of a co-borrower

Unfair Prejudice

The Court determined that there was no unfair prejudice to the creditor and that in the circumstances of the case it was not unreasonable of the PIP to have written down the value of the Principal Private Residence (PPR) to its current market value. The parties had agreed to the value of the PPR pursuant to section 105 of the Act. The Bankruptcy comparison had not been challenged and the PPR was not disproportionate to the debtor's needs.

The secured creditor's counterproposal:

The secured creditor contended that its counterproposal would provide a better return to the debtor's unsecured creditors. The Court referred to the Callaghan case, indicating that it set out the obligations of a PIP where the secured creditor submits a counterproposal. The Court referred to the fact that a PIP may not, without reason ignore a counterproposal. The creditor's counterproposal provided for warehousing of a significant portion of the secured debt. Based on Judge Baker's judgment in the Callaghan case stating, "*There is ……nothing in ss 99 or 100 of the Act which precludes the splitting of the mortgage debt and the warehousing of part of the debt….. the fact that warehousing of the type and for the time proposed is not found in the list of options outlined in s102 (6) (d) does not mean that the proposal is not permitted by law*." The Court indicated that warehousing should be given due consideration in the context of the particular circumstances of the case. The Court referred to the fact that

the PIP and the debtor considered the bank's counter proposal and did not see it as affordable, sustainable or in compliance with the Acts. The Court held that the PIP did comply with her statutory obligations as she gave the counterproposal consideration but did not see it as either affordable or sustainable for the debtor.
The creditor argued that the proposed warehousing was generous and of benefit to the debtor. The Court indicated that the test to be applied when considering the counter-offer was one of reasonableness, citing paras 59 and 60 of the Callaghan judgment.

In the subject case, the debtor was 45. Under the terms of the counterproposal, the debtor would be 71 at the end of the extended mortgage period. She would be faced with a liability of some €98k, with the possibility of a write down of 30% of that amount. The debtor would also have a small pension.

The Court indicated that it could not speculate as to what the debtor's income would be at age 71, nor could it speculate if the debtor would have capital assets to enable her to clear off the residual balance of the loan and income to enable her to live in her home during retirement. The court opined that in determining the reasonableness of the counterproposal the Court must have regard to the current income and assets, which are ascertainable and available to the debtor.

The existence of a co-borrower:
In the JD case delivered by Judge Baker it was held that the absence of a co-borrower was not an impediment to an arrangement coming into force for the applicant. The creditor argued a distinction between the JD case and this case, in that the debtor did not seek any attachment of earnings order from her spouse. The Court took the view that the absence of an attachment of earnings order was not a sufficient ground to distinguish the two cases.

The Court approved the arrangement as proposed by the PIP.

South Eastern Circuit Court (Gilbride case) - Disclosure of debts

A recent hearing in the South Eastern Circuit dealt with a creditor objection to a protective certificate. It was alleged by a creditor that monies invested by the creditor in the debtor's business were misappropriated, and that this misappropriation took place against the backdrop of a breach of fiduciary duties by the debtor. The Court ordered that the Protective Certificate issued by the Court in respect of the debtor was not to apply to the objecting creditor. Costs were awarded to the legal representatives of the creditor. Judge Enright in her judgment determined that there were monies lent and misappropriated and that if the full extent of the situation had been made known to the Personal Insolvency Practitioner at the outset, it is likely that the debt would not have appeared in the debtor's Protective Certificate application.

In this regard, practitioners are reminded that they should ensure they seek confirmation from debtors, preferably in writing, that they have disclosed all their debts, and all pertinent information relating to their financial position. Practitioners should also pay close regard to sections 50, 54, 91(1) (e) and section 118 of the Act, which deal with full disclosure of a debtor's affairs in their application.

2.3 Court Sittings over the Vacation Period

Please see the table below showing the dates on which Circuit Court sittings are scheduled to take place over the traditional Court long vacation period (taken from Courts Service Online and other advices provided). The vacation period may pose challenges to the process in the context particularly of the possible need to apply for extensions to PC, or to make an application to allow a repossession application to be set aside.

In addition, Judge Baker has indicated that she will be sitting in the High Court for personal insolvency during the vacation period on Monday 4 September 2017.

Circuit Court (Insolvency) Vacation Sittings							
Dublin Circuit Court	**Cork Circuit Court**	**Kilkenny Circuit Court**	**Castlebar Circuit Court**	**Trim Circuit Court**	**Tullamore Circuit Court**	**Monaghan Circuit Court**	**Ennis Circuit Court**
					02-Aug-17		
					03-Aug-17		
09-Aug-17				09-Aug-17			
				10-Aug-17			
		14-Aug-17	14-Aug-17				
						17-Aug-17	
		21-Aug-17					
					24-Aug-17		
		28-Aug-17					
		04-Sep-17					
06-Sep-17							
		11-Sep-17					
							12-Sep-17
		13-Sep-17		13-Sep-17			
				14-Sep-17	14-Sep-17		
		18-Sep-17	18-Sep-17				
						21-Sep-17	
		25-Sep-17					
			02-Oct-17				
			09-Oct-17				

3 Meetings/Events

3.1 ISI Section 141 Submission

The ISI welcomed the opportunity to submit its views to the Department of Justice and Equality, along with other interested parties, on the operation of Part 3 of the Act in June 2017. Submissions were specifically invited on the thresholds and processes under Part 3 for Personal Insolvency Arrangements (including for insolvent persons who are unincorporated small or medium entrepreneurs) and on whether these should be changed. The Government had committed to review this issue, under the Programme for Partnership Government.
Further details are available here.

The ISI's submission demonstrates that the new solutions introduced by the Act work. The debtors who have availed of the solutions have returned to solvency and are able to make a fresh start. In the vast majority of cases, they get to stay in their home. For the creditors involved, they have had their bad loans dealt with in a fair and equitable manner. We equally demonstrate that many of the concepts behind the alternatives to bankruptcy introduced in the Act are well established and work well in other countries. The challenge now is to ensure that all of those people who would benefit from the solutions provided by the Act do so. The ISI estimates that long-term activity levels should be significantly higher than at present.

Currently the ISI is processing circa 1,300 solutions a year covering Debt Relief Notices (DRNs), Debt Settlement Arrangements (DSAs) and Personal Insolvency Arrangements (PIAs). International comparisons indicate this should be circa 6,000 per year. Experience in other jurisdictions indicates that it does take time to build awareness of new debt solutions and that it also takes time for activity levels to build.

The ISI has identified three key factors that influence activity levels:

1. Efficiency of Process

2. Debtor Engagement

3. Creditor Engagement

The ISI addresses all of these factors in its submission which is available here.

3.2 Mortgage Arrears Resolution (Family Home) Bill 2017

The private member's bill, Mortgage Arrears Resolution (Family Home) Bill 2017, passed through second stage in the Dail on 12/07/17 and will proceed to committee stage, presumably in the autumn. The stated purpose of the Bill is "to provide for the establishment of a Mortgage Resolution Office; to provide for a non-judicial Mortgage Resolution Order concerning mortgages over family homes; to provide for an independent appeals process against decisions of the Mortgage Resolution Office; and to provide for related matter."

In responding to the private member's bill, the Minister for Justice and Equality, Charlie Flanagan TD, has told the Dáil that he has serious reservations about the Mortgage Arrears Resolution (Family Home) Bill 2017, because it is unlikely to survive a challenge on constitutional grounds. The Dáil transcript can be found here.

4 Business metrics

4.1 ISI Quarter 2 2017 Statistics.

The ISI has published statistics covering the second quarter of 2017.

The high level of new applications has been maintained largely due to Abhaile, the Government's free mortgage arrears support scheme, which includes free Personal Insolvency Practitioner consultations for insolvent debtors. The number of Protective Certificates issued and the number of Arrangements approved continue to rise. While the number declared bankrupt so far this year is down compared to last year, the ISI estimates that the outcome by the end of the year will be broadly similar to last year.

4.2 Abhaile

To date, over 8,500 Abhaile Scheme vouchers have been issued, of which over 60% relate to vouchers to enable debtors avail of the services of a PIP. The balance of the issued vouchers relate predominantly to vouchers to avail of legal advice. Over 1,750 vouchers issued for the purpose of providing legal advice to applicants pursuing section 115A reviews.

5 General

5.1 Creditor Contact while a PC or an Arrangement is in place

The ISI continues to be informed about continuing creditor contact while debtor protection remains in please, in contravention of the provisions of the Personal Insolvency Act. This contact is in many cases exercised by creditors that have not voted at the creditors' meeting.

All creditors are reminded that such contact is prohibited under the legislation, and the ISI will continue to monitor persistent and continued breaches in this regard.

5.2 Section 105 Valuations

A number of requests for assistance have been made to the ISI in relation to its role in appointing an independent expert valuer under the provisions of section 105(4) of the Act.

Submissions have been received by the ISI from PIPs and creditors in relation to issues regarding repairs that may be required to the secured property, which if they were to be carried out would affect the market value of the property in question. In this regard, the ISI would refer you to the section 105 provisions, specifically the definition of 'market value', which states –

"(6) In this section "market value" –

(a) as respects property the subject of security for a secured debt, means the price which that property might reasonably be expected to fetch on the open market;

(b) as respects security for a secured debt, means the amount that might reasonably be expected to be available to discharge that secured debt, in whole or in part, following realisation of the security by the secured creditor concerned and, where permitted by the terms of the

security or otherwise, after deducting all relevant costs and expenses in connection with the realisation of the security."

The ISI believes that the "market value" assessed by the valuer in relation to the section 105 process should reflect the CURRENT market value, and not one which takes into account the actual costs involved in bringing the property to a certain condition prior to a sale.

In any valuation carried out by an independent expert, it would be expected that the valuer would be aware of (but not necessarily be able to quantify in detail) requirements in relation to the level of repair that might need to be undertaken. The cost of actual repairs, or any value added they might bring to the secured property, if carried out, are irrelevant to the determination of "market value" for the purposes of section 105.

5.3 Reasonable Living Expenses Guidelines 2017

In accordance with Section 23 of the Personal Insolvency Act, the ISI has issued guidelines as to what constitutes a reasonable standard of living and reasonable living expenses (RLEs) effective from 31st of July 2017. Since the previous update in 2016, the ISI carried out some research in conjunction with the Vincentian Partnership for Social Justice (VPSJ), to learn about the experience of debtors who are living within the RLEs on a day-to-day basis. It also consulted with creditors and other stakeholders to gain insight into how the RLEs were being operated in practice.

The ISI has reviewed the constituent parts of the RLEs and while some categories have changed, the overall effect of inflation has led to a very slight decrease in living expenses. Based on the above, it was decided that it was most appropriate to maintain the RLE figures at their current level.

The next ISI e-Brief is scheduled to issue in November 2017.

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