

# **APPEARANCE BY THE INSOLVENCY SERVICE OF IRELAND BEFORE THE OIREACHTAS JOINT COMMITTEE ON FINANCE, PUBLIC EXPENDITURE AND REFORM**

## **Opening remarks by Mr. Lorcan O'Connor, Director, Insolvency Service of Ireland**

Thank you for inviting the Insolvency Service of Ireland (ISI) to appear before the Committee today to meet and brief members on developments within the ISI, with specific reference to debt management and resolution.

I am accompanied today by my senior management team whom I would like to introduce at the outset: Ms. Cathy Clarke who is head of our Regulation Division, Mr. Randall Plunkett who is head of our Case Management Division, dealing with the new alternatives to bankruptcy – the DRN, DSA and PIA; and Mr. Christopher Lehane who is head of our Bankruptcy Division and the Official Assignee in Bankruptcy.

We look forward to the opportunity to answer as many questions as we can from members of the Committee but, before doing so, I wish to give you a brief overview of work undertaken since our meeting in July last year and to highlight a number of other salient points. I will then ask the Official Assignee in Bankruptcy to address certain points around bankruptcy that the Committee specifically inquired upon.

### **WHAT THE ISI HAS ACHIEVED**

It is important to remember that the ISI was established only a year ago.

When I speak to my counterparts in the Insolvency Service of England and Wales or the Insolvency Service of Northern Ireland, or other equivalent organisations for that matter, they speak in years rather than months when referring to their experiences around initial establishment or the roll out of completely new business areas.

Those involved in the regulation of people practising in the financial services sector provide a similar commentary. In that relatively short time, from a standing start, we have achieved an enormous amount, both directly and indirectly.

In direct terms we have developed a whole new legal infrastructure and service dedicated to providing sustainable solutions for insolvent debtors and these solutions are now being put in place.

While the initial uptake of debt relief schemes by debtors is slow, I am confident that the number of cases on the system will grow significantly over the coming months. The statistics that were published by the ISI earlier this month point to a trend moving in the right direction. The slow start in terms of volumes is mirrored in the experience of other jurisdictions where new measures on debt relief were introduced. It does take a little time for people to become comfortable with them.

I expect thousands will have availed of our services within the next year.

In terms of the ISI's indirect impact it is worth remembering that this time last year insolvent debtors were not obtaining debt agreements with creditors – this situation is very different now. I believe the ISI has been a significant catalyst for this change. Until the ISI published its guidelines on a Reasonable Standard of Living and Reasonable Living Expenses, negotiations around allowable expenditure between debtors and creditors never moved past 'go'. What was once the most difficult aspect of addressing personal over-indebtedness is now not even on the agenda.

Since the autumn, we see evidence of a growing number of agreements between insolvent debtors and creditors being successfully concluded. This would not have happened but for the introduction of the new debt solutions and the reform of bankruptcy laws.

### **DEVELOPMENTS IN THE ISI SINCE JULY 2013**

Since we met in July of last year, a number of milestones have been reached by the ISI.

In **August** the ISI began authorising Approved Intermediaries and Personal Insolvency Practitioners.

We now have over 200 practitioners. These are made up of 134 PIPs - the people who deal with Debt Settlement Arrangements (DSAs) and Personal Insolvency Arrangements (PIAs) and 80 people within the MABS offices that have been authorised as Approved

Intermediaries – the people trained to help those wishing to apply for Debt Relief Notices (DRNs). I expect the number of practitioners will continue to increase.

In **September** the ISI issued its Strategic Plan 2013-2016. We also began accepting applications for the new debt solutions.

**October** saw the first Protective Certificates issued.

**November** saw the first Debt Settlement Arrangement approved by creditors.

**December** saw the reduction in the bankruptcy term from 12 to 3 years and the formal transfer of the Office of the Official Assignee into the ISI.

**January** of this year saw the first Debt Relief Notices issued.

**February** saw the first Personal Insolvency Arrangement approved by Court.

**March** of this year saw us take on our 500<sup>th</sup> case.

And earlier **this month** we published our first Quarterly statistics report.

The ISI will shortly launch an information campaign in consultation with the Citizens' Information Board, MABS and PIPs. This will include information sessions held around the country offering opportunities for one-to-one advice.

## **PROTOCOLS**

I now wish to turn to one particular initiative currently underway that I believe will further assist in increasing numbers availing of the new alternatives to bankruptcy.

In February this year the ISI hosted a conference for creditors and practitioners in Dublin Castle.

A major aim of the conference was to initiate the development of protocols for the DSAs and PIAs. Agreed protocols will make the insolvency application process both simpler and faster for creditors, practitioners and debtors.

The development of these two protocols do not require any amendments to existing legislation and is in line with best practice in other jurisdictions.

If I could use an analogy, conveyancing solicitors do not write individual contracts for the sale or purchase of houses. If they did so, each individual transaction would take far longer and would cost substantially more than it does at present. Instead, for a regular transaction, they will use the standard terms and conditions produced by the Law Society. Similarly, a protocol for insolvency applications will soon have standard terms and conditions that will assist in transparency and greater acceptance for all concerned.

At the conference the ISI announced an ambitious target to have the DSA protocol agreed this spring. Thanks to the high level of commitment shown by all of the participating stakeholders, we are on track to achieve that. Members of the steering group and working group, set up at the end of February, have already spent over 2,000 working hours on developing a DSA protocol and we have a further session scheduled for this afternoon. Our aim today is for the Steering Group to sign off on the DSA Protocol.

In the UK, the equivalent process took over two years to develop. We are seeing a clear desire from participating stakeholders to have the protocol up and running in the shortest possible timescale.

An equivalent protocol in the UK has resulted in acceptance rates for protocol-compliant IVAs (their equivalent of our DSAs) exceeding ninety five per cent. That's what I want to see happen here.

Once the DSA protocol is complete, it will be followed by a PIA protocol which will deal with the additional aspects of secured debt.

## **RECENT COMMENTS BY CERTAIN CREDITORS**

While I am proud of what the ISI has achieved in its short existence and while I am also firmly of the view that the Personal Insolvency Act and the ISI will assist many thousands of insolvent debtors badly in need of help over the coming months, I believe it would be remiss of me to ignore recent comments made before this Committee by certain creditors.

Before doing so, I would like to stress that the ISI is an independent statutory body with clear functions set out in Section 9 of the Act. It is not the role of the ISI to question a creditors approach to any given case. We are not 'pro debtor' or 'pro creditor'. Our primary purpose is to deliver the infrastructure to facilitate DRNs, DSAs and PIAs.

The concepts behind the DRN and DSA are tried and tested in other countries. The PIA, dealing with secured debt, is a new concept. However, the Act carefully balances the interests of both debtors and creditors when dealing with secured debt.

While I was disappointed by the comments made by one creditor in particular to this Committee, I cannot say I was altogether surprised. They were blunt about how they intend to approach PIAs in particular. But making a global policy statement about how they intend to deal with applications does not take full account of the new reality - the new debt solutions, including the PIA, are designed to deliver better outcomes for both debtors and for creditors. And if a creditor stands in the way of a solution, there are mechanisms available to debtors to deal with this.

Despite the statements made here, I believe that on a case-by-case basis, we will achieve solutions. If, however, I am proven wrong, we hit a brick wall and we do not make progress on individual cases, then we will report this back to you and we will recommend change. At this time, however, only a few months into the process, the sample size of cases is insufficient to make this assessment.

## **TO CONCLUDE**

Both the Minister for Justice and Equality, and the ISI have indicated that the effectiveness of the legislation will be kept under review and if issues arise that need to be addressed they will be. Monitoring creditor engagement will obviously be a key focus.

In the short term, the ISI remains focussed on developing the DSA and PIA protocols.

There are some people who have been quite publicly critical of the ISI on the issue of the numbers of individuals seeking an insolvency solution. To them I would observe that the ISI opened in record time; taking applications online six months from establishment. Our presence is contributing to breaking a stalemate between stakeholders, which in some cases has lasted for six years or more.

In addition to providing mechanisms to address individual cases of unsustainable debt, the enactment and operation of the new insolvency legislation has an even broader impact. It redefines the overall framework within which lenders and debtors assess their options for dealing with insolvent debtors. It can already be seen that as a result of the enactment and coming into operation of the Personal Insolvency Act, some financial institutions are taking more active and constructive steps. They are moving towards long-term sustainable debt resolution rather than short-term debt amelioration.

I believe this would not have happened without the personal insolvency legislation and the establishment of the ISI.

These new debt solutions are not just good for debtors but are also in the interests of creditors. They offer an efficient and fair means to tackle what is a very large problem for everyone. Ultimately it is in all of our interests to return an insolvent debtor to solvency, to ensure their well-being and to give them the second chance that they deserve.

I will now ask Mr Christopher Lehane, Official Assignee in Bankruptcy to briefly speak to you around the recent changes to the bankruptcy laws here and what this might mean for a debtor's home.

## **BANKRUPTCY ACT CHANGES**

As Committee members are aware the most significant changes made to the Bankruptcy Act 1988 (effective as of 3<sup>rd</sup> December 2013) were as follows:

- A reduction in the automatic discharge period from 12 years to 3 years
- A €20,000 debt requirement for creditor and debtor petitions
- A requirement for the Court to consider on both creditor and debtor petitions, whether it is appropriate to adjourn proceedings to allow the debtor to attempt to enter into a Debt Settlement Arrangement or Personal Insolvency Arrangement
- An increase in excepted assets not forming part of bankruptcy estate to €6000
- Pensions (other than mainly Approved Retirement Funds) no longer form part of the bankruptcy estate, subject to 5 year claim
- An increase in avoidance provision periods to 3 years where there are fraudulent preferences of creditor claims, sales at an undervalue and fraudulent transfers
- A limit of 5 years on income payment orders
- A Court, on application by the Official Assignee/ trustee, has the discretion to extend the bankruptcy period for maximum further period of 5 years.
- The Office of the Official Assignee transferred from the Courts Service to the ISI.

## **THE OFFICIAL ASSIGNEE (OA)**

When a person is declared bankrupt, all property of the bankrupt person vests in the OA. The OA has the same rights and powers of the bankrupt person in relation their property. The primary function of the OA is to gather in the assets, realise them and distribute proceeds to creditors.

## **BANKRUPTCY POLICY ISSUES**

I will deal with 2 key areas I believe are of particular interest to Committee:

1. Income Payment Orders
2. Family Homes in Bankruptcy

## 1. Income Payment Orders (IPOs)

An Income Payment Order can last for up to 5 years. A bankrupt person is assessed at least on a six monthly basis to establish whether he/she has surplus income after applying the ISI Guidelines to a Reasonable Standard of Living and Reasonable Living Expenses.

If the bankrupt person has surplus income, then an Income Payment Order will be sought. It is in the interest of the debtor to cooperate in these matters, so that an Income Payment Order can be put in place early in the bankruptcy to ensure it runs concurrently with the 3 year automatic discharge period.

If a debtor does not initially have surplus income but at some stage in the bankruptcy term does have surplus income, I as Official Assignee will seek an Income Payment Order but will generally limit the Order to the remainder of the 5 year period since adjudication. If however, the individual has refused to cooperate or failed to accurately disclose income, I will seek the full 5 year term.

## 2. Family Home in Bankruptcy

For obvious reasons people contemplating bankruptcy will be concerned around what might happen to their family home. We have published a very useful guide for debtors on bankruptcy which explains in detail how it will impact them, including in relation to the family home. We have also published a scenario pack giving practical examples of various family home situations in bankruptcy, all of which may be found on the ISI website [www.isi.gov.ie](http://www.isi.gov.ie)

### Key Provisions of Bankruptcy Act

There are three key provisions of the Bankruptcy Act relevant to family homes.

**Section 136** states, that whilst unsecured debts can only be claimed in bankruptcy, this *'shall not affect the power of a secured creditor to realise or otherwise deal with his security in the same manner, as he would have been entitled to realise or deal with it, if this section had not been enacted'*.

**Section 44** states that on adjudication, all property (including a half interest in a family home) vests in the Official Assignee.

**Section 61(5)** states that the Court shall have power to order postponement of the sale of the family home or shared home within the meaning of the *Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010* having regard to the interests of the creditors and of the spouse or civil partner within the meaning of the *Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010* and dependants of the bankrupt as well as to all the circumstances of the case.

### **Policy of Official Assignee**

1. Where there is positive equity in family home, all other assets will be realised before having recourse to it.
2. The Official Assignee's interest in the family home will be sold to the spouse, where possible.
3. The family home will not be sold earlier than 6 months after the adjudication order, unless to the spouse.
4. The bankrupt will be offered the opportunity of doing a composition with his creditors with proceeds of other assets sold, before the family home will be sold.
5. A sum of €5,000 will at minimum be sought for negative equity interest of the Official Assignee.

In **Appendix 1**, I deal with the 3 options of a secured lender when a debtor is declared bankrupt, the resultant actions of the Official Assignee and the consequences for the debtor.

In **Appendix 2**, I set out the findings of a recent survey we carried out on bankruptcies over the last 4 years (2011-2014) to establish the consequences for family home ownership in bankruptcy.

## APPENDIX 1

### Secured Creditor 3 Options in Bankruptcy – First Schedule to Bankruptcy Act 1988

While it is true to say that the same levels of protections around the family home within a PIA do not exist in bankruptcy, it is not automatic that a bankrupt will lose their home. The table below sets out the options available to a secured lender in bankruptcy.

| Financial Institution Choice  | Financial Institution and Official Assignee Actions   | Debtor Consequences   |
|---|---|---|
| <b>1. Rely on security</b><br>(and not claim in bankruptcy)                 | <b>1.1 Positive Equity, Financial Institution sells property</b><br>If the mortgage is <b>not</b> being paid on terms acceptable to the financial institution, it can sell family home and can claim interest on the mortgage up to date of sale. Surplus of sale proceeds given to OA (assuming no judgement mortgagees – who would have priority to OA) | <b>1.1 Positive Equity, Financial Institution sells property</b><br>Home lost. The surplus from the sale proceeds may generate funds that the bankrupt can use to do a composition with creditors, discharging the bankruptcy. If no composition is achieved, the OA will allow rent payments for accommodation as part of I.S.I. Reasonable Living Expenses (RLEs) allowance, before assessing for Income Payment Order. |
|   | <b>1.2 Positive Equity, OA sells property</b><br>Even if the mortgage <b>is</b> being paid, the OA nevertheless may sell family home, having obtained a Court order (under S 61(4) Bankruptcy Act) to realise equity in family home for creditors. In the first instance, he will always seek to sell to spouse.  | <b>1.2 Positive Equity, OA sells property</b><br>As above.  |
|   | <b>1.3 Negative Equity, Financial Institution does not sell property</b><br>Mortgage lender ignores technical default of bankruptcy, once mortgage being paid on terms acceptable to financial institution.   | <b>1.3 Negative Equity, Financial Institution does not sell property</b><br>Once mortgage being paid on terms acceptable to financial institution, it will <b>not</b> seek to sell family home.   |
|   | <b>1.4 Negative Equity, OA does not sell property</b><br>If no equity, the OA will not sell home and interest continues to vest in him, post discharge. In first instance, OA will always however seek to sell his half interest to spouse.   | <b>1.4 Negative Equity, OA does not sell property</b><br>Assuming agreed mortgage payments are reasonable for family size and OA allows as RLE – <b>he pays mortgage and retains home.</b><br>Spouse jointly & severally liable for full mortgage.  |
| <b>2. Abandon security</b> (and claim full debt in bankruptcy)              | Very rarely chosen – only where prior mortgages take full security<br>Unsecured claim for full debt made in bankruptcy.   | It depends on action of prior mortgagees whether bankrupt retains home<br>Spouse jointly & severally liable for full mortgage.  |
| <b>3. Realise or value security</b> (and claim for shortfall in bankruptcy) | <b>3.1 Financial Institution realises security and claims shortfall in bankruptcy as an unsecured claim</b><br><br>As financial institution is claiming in bankruptcy it is subject to S 75(2) Bankruptcy Act, which states that it can only claim mortgage interest up to date of adjudication.  | <b>3.1 Financial Institution realises security and claims shortfall in bankruptcy as an unsecured claim</b><br><br>Home lost. Shortfall after dividend payment (if any) is written off against bankrupt.<br>Spouse jointly and severally liable for full mortgage.<br>OA will allow rent payments for accommodation as part of RLEs.  |
|   | <b>3.2 Financial Institution values security and claims shortfall in bankruptcy as an unsecured claim</b><br><br>Rare as it limits security to amount assessed at time. Creditors tend to prefer 1.3 option, allowing mortgage be paid and security appreciates.  | <b>3.2 Financial Institution values security and claims shortfall in bankruptcy as an unsecured claim</b><br><br>Keep home, once mortgage being paid and allowed by OA<br>Spouse jointly & severally liable for full mortgage.  |

**APPENDIX 2**  
**SURVEY OF FAMILY HOMES IN BANKRUPTCY**

**Summary**

In April 2014, the Bankruptcy Division of the ISI carried out a survey of family homes in bankruptcy over the last 4 years. The results are split between the current year 2014 and years 2011–2013.

The key findings of the survey are that:

- The majority of bankrupts have remained in their family homes.
- Of 73 bankruptcies so far in 2014, 33 persons are renting (14 of whom were in homes that have been voluntarily surrendered), leaving 40 in their family homes now, though of these 4 have had possession orders made against them which have not yet been enforced.
- Of 121 bankruptcies between 2011– 2013 (deducting 5 that were annulled); 55 persons are currently renting (10 of whom were in homes that have been voluntarily surrendered and 11 of whose homes were possessed by order) leaving 66 now in their family homes. In relation to 16 of these remaining cases where persons are still in their family homes, there are family law proceedings in being or proceedings by the Official Assignee either issued, or soon to be issued.

|  | <b>2011 to 2013</b> | <b>2014</b> |
|--|---------------------|-------------|
| <b>Number bankrupted</b>                       | <b>126</b>          | <b>73</b>   |
| Family homes voluntarily surrendered           | 10                  | 14          |
| Family homes possessed by order                | 11                  | 0           |
| Possession Order granted (Still in possession) | 12                  | 4           |
| OA seeks order for sale (S 61(4))              | 3                   | 0           |
| Bankruptcy Annulled                            | 5                   | 0           |
| Mortgage being paid (not in default)           | 25                  | 16          |
| Mortgage not being paid (in default)           | 10                  | 16          |
| No mortgage                                    | 10                  | 0           |
| No Family home - renting                       | 34                  | 19          |
| <b>Total number of properties involved</b>     | <b>120</b>          | <b>69</b>   |

**Note: number of properties will be less than no. of bankrupts due to couples going bankrupt.**