

PIA

Scenario 7

Contingent liabilities



TO HELP EXPLAIN SOME OF THE CONCEPTS CONTAINED IN THE PERSONAL INSOLVENCY LEGISLATION, THE INSOLVENCY SERVICE OF IRELAND HAS CREATED SOME POSSIBLE SCENARIOS TO ILLUSTRATE HOW EACH OF THE THREE SCHEMES MAY OPERATE IN RESPECT OF A DEBTOR, PERSONAL INSOLVENCY PRACTITIONER OR APPROVED INTERMEDIARY, CREDITORS, AND THE COURT.

THESE SCENARIOS MAY BE AMENDED OR DEVELOPED IN THE FUTURE WHEN ACTUAL CASES ARE PROCESSED TO A SUCCESSFUL CONCLUSION IN ORDER TO MORE ACCURATELY REFLECT SUCCESSFUL OUTCOMES APPROVED BY THE COURT.

IT IS IMPORTANT TO EMPHASISE THAT THESE POSSIBLE SCENARIOS ARE FOR ILLUSTRATIVE PURPOSES ONLY AS TO HOW A PARTICULAR ARRANGEMENT MIGHT WORK IN PRACTICE, AND ASSUME A PRAGMATIC AND REALISTIC RESPONSE BY CREDITORS.

THE ISI DOES NOT PROVIDE FINANCIAL ADVICE.

APPROVED INTERMEDIARIES IN THE CASE OF DRNS, AND PERSONAL INSOLVENCY PRACTITIONERS, IN THE CASE OF DSAS AND PIAS, ARE AVAILABLE TO ASSIST DEBTORS.

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SCENARIO 7

PIA - APPLICANT ELIGIBLE, CONTINGENT LIABILITIES.

This sample scenario is designed to illustrate the basic features of a PIA which include contingent liabilities.

1. GERARD'S STORY

Gerard is a structural engineer. He has seen his income drop dramatically in the last five years. He earns a net income of €3,000 per month.

He bought his Principal Private Residence (PPR) ten years ago. The outstanding mortgage is €180,000, which is the current value of the house.

Gerard owns a car valued at €5,000 which is required for his work.

Gerard bought two apartments in the same development six years ago. Each apartment is valued at €120,000 and each has an outstanding mortgage of €220,000 with monthly loan repayments of €987. The apartments are not currently being rented, despite efforts in recent months to secure tenants.

Gerard had set up an engineering company ABC Engineering Ltd seven years ago which is now in liquidation. When the company was trading Gerard provided a personal guarantee to the largest of his trade suppliers. ABC Engineering Ltd does not have enough assets to cover its liabilities. The largest trade supplier is still owed €150,000 and Gerard believes he will be personally liable for this outstanding €150,000.

Gerard also provided a personal guarantee on a mortgage his son obtained for a home six years ago. The outstanding mortgage on the son's home is €180,000. His son is in a secure job, making the full monthly repayments on the mortgage himself and the mortgage is performing fully.

Gerard also has unsecured debt of €40,000 which consists of a personal loan of €25,000 and credit card debt totalling €15,000. Gerard's current monthly commitments are as follows:

- PPR Mortgage repayments - €1,016
- Apartment 1 Mortgage repayment – €987
- Apartment 2 Mortgage repayment - €987
- Unsecured debts repayments - €1,175

Gerard's day-to-day outgoings amount to €1,045 per month. He has cooperated with his bank in relation to his PPR mortgage under the Central Bank Code of Conduct on Mortgage Arrears for a period of ten months but has been unsuccessful in agreeing an alternative payment arrangement. Gerard is unable to pay his debts in full as they fall due and acknowledges he is insolvent.

Gerard meets with a Personal Insolvency Practitioner (PIP) and provides full details of his financial circumstances so the PIP can understand his financial position.

2. GERARD'S INSOLVENT POSITION

| Assets | Value | Loan |
|-----------------------------|------------------|------------------|
| Principal Private Residence | € 180,000 | € 180,000 |
| Apartment 1 | € 120,000 | € 220,000 |
| Apartment 2 | € 120,000 | € 220,000 |
| Car | € 5,000 | € 0 |
| Total | € 425,000 | € 620,000 |

| Debts | | |
|------------------------|--|------------------|
| Secured debts | | |
| PPR Mortgage | | € 180,000 |
| Apartment 1 Mortgage | | € 220,000 |
| Apartment 2 Mortgage | | € 220,000 |
| Unsecured debts | | |
| Personal loan | | € 25,000 |
| Credit Card | | € 15,000 |
| Contingent Liabilities | | |
| Son's Mortgage PG | | € 1 |
| Trade Suppliers PG | | € 150,000 |
| Total | | € 810,001 |

| Monthly Income | |
|---------------------|----------------|
| Gerard's Net Income | € 3,000 |
| Total | € 3,000 |

| Monthly expenses | |
|--|------------------|
| Total Set costs ¹ | € 1,045 |
| Rent/Mortgage ² | € 1,016 |
| Childcare Costs ² | 0 |
| Reasonable Living Expenses | € 2,061 |
| Apartment 1 Mortgage | € 987 |
| Apartment 2 Mortgage | € 987 |
| Total Expenses before unsecured debt repayments | € 4,035 |
| Deficit prior to meeting unsecured debt obligations | (€ 1,035) |

3. ELIGIBILITY

Gerard qualifies for a PIA because:

- ✓ Gerard is insolvent – he is unable to pay his debts as they fall due.
- ✓ Gerard has secured debts.
- ✓ Gerard has not incurred 25% or more of his debts in the 6 month period ending on the application date for the Protective Certificate.
- ✓ Gerard has participated in the Mortgage Arrears Resolution Process (process approved by Central Bank) with his PPR mortgage provider for a minimum period of six months in relation to his PPR but has been unable to agree an alternative repayment arrangement.
- ✓ Gerard's total secured debts do not exceed €3 million.

¹ The Personal Insolvency Practitioner references the tables in the ISI "Guidelines on a reasonable standard of living and reasonable living expenses", available on the website (www.isi.gov.ie). Gerard's circumstances meet those covered by Table 2. "One Adult Household (vehicle)" on page 38 of the Guide (€1,045.48). For illustrative purposes and ease for the reader, the total set costs figure is rounded to €1,045.

² The Personal Insolvency Practitioner will assess the reasonableness of mortgage, rent and/or childcare payments in accordance with pages 11 and 12 "Guidelines on a reasonable standard of living and reasonable living expenses".

4. NEXT STEPS

- a) The PIP is satisfied that Gerard meets all the eligibility criteria for a PIA and submits an application to the Insolvency Service of Ireland (ISI) for a Protective Certificate (PC) on his behalf, including a Prescribed Financial Statement (PFS).
- b) The ISI and the Court are satisfied with Gerard's application and the Court issues a PC. Gerard's name, address, year of birth and date of issue of the PC will be added to the Public Register of PCs on the ISI website. The PC offers Gerard and his assets protection from legal proceedings by his creditors while he is applying for a PIA.
- c) The PIP has 70 days to develop a PIA proposal, get it voted acceptable by the creditors and submitted to the Court for assessment.
- d) Gerard agrees to the PIA proposal developed by the PIP (Details of potential PIA solution are set out below in point 5).
- e) The PIP provides the necessary documentation to each creditor prior to the creditors' meeting including analysis which demonstrates how the financial outcome for creditors under the terms of the PIA is likely to be better than the estimated financial outcome for such creditors were Gerard adjudicated bankrupt.
- f) Creditors representing 65% or more of Gerard's total debt participating at the creditors' meeting agree to the proposal (i.e. first threshold needed for creditors' approval). This includes creditors representing 50% or more of Gerard's secured debt (i.e. second threshold needed for creditors' approval), and creditors representing 50% or more of Gerard's unsecured debt (i.e. third threshold needed for creditors' approval).
- g) The PIP records the creditors' meeting results and sends them to the ISI, Gerard and each of his creditors. No creditor appeals at any point of the process.
- h) The ISI and the Court carry out final reviews of Gerard's case and the Court approves the PIA.
- i) Gerard's details are placed on a Public Register of Personal Insolvency Arrangements. (This includes his name, address, year of birth, and the date of coming into effect of his PIA).

5. POTENTIAL PIA SOLUTION FOR GERARD PROPOSED BY PIP

Gerard's current mortgage repayment on his PPR is €1,016 per month. The total mortgage repayments for both apartments are €1,974 a month. His total set costs are €1,045 per month and his unsecured debt repayments are €1,175 per month. With him having a net income of €3,000 per month this situation is not sustainable and the PIP considers how it can be addressed.

PPR MORTGAGE

The PIP assesses whether extending the mortgage term would make the PPR mortgage more sustainable. Due to Gerard's age it is only possible to extend the mortgage by five years, which would reduce the monthly mortgage repayments from €1,016 to €928.

TWO APARTMENTS

The PIP reviews evidence supplied by Gerard of his unsuccessful attempts to secure tenants for both apartments, and proposes to sell the apartments for €120,000 each and repay each of the mortgages in part with the proceeds. The shortfall of €100,000 on each apartment is treated similarly to unsecured debt in accordance with section 102(5) of the Personal Insolvency Act 2012.

CONTINGENT LIABILITIES

Although Gerard has provided a personal guarantee on a mortgage obtained by his son the PIP reviews the evidence supplied by Gerard that his son is making the full monthly repayments. The PIP believes an event of default occurring which would make Gerard liable for his son's mortgage is remote and so allocates a nominal value of just €1 to this debt.

The PIP inserts terms into the PIA to ensure that in the event that the guarantee crystallises during the lifetime of the PIA, such an eventuality is dealt with in both an efficient and transparent manner. The terms provide that upon crystallisation of the claim, the creditor holding this guarantee will begin sharing in the distribution of the unsecured dividends in proportion to Gerard's other unsecured creditors' debts. The terms of the PIA also set out that if the event occurs in year four onwards of the PIA, the duration of the PIA will be extended by a further period of 12 months. A full variation² will be required in the event that the guarantee crystallises at an amount in excess of €180k.

The PIP reviews the evidence supplied by Gerard in relation to the personal guarantee provided to the Trade Suppliers. ABC Engineering is in liquidation and its assets are not sufficient to pay its liabilities. Given that the trade supplier has indicated that he will call in the personal guarantee the

¹ Where a Personal Insolvency Arrangement provides for the sale or other disposal of the property which is the subject of the security for a secured debt, and the realised value of that property is less than the amount due in respect of the secured debt, the balance due to the secured creditor shall abate in equal proportion to the unsecured debts covered by the Personal Insolvency Arrangement and shall be discharged with them on completion of the obligations specified in the Personal Insolvency Arrangement.

² A variation to the PIA in accordance with Section 119 of the Personal Insolvency Act 2012.

PIP, in consultation with the debtor, considers the personal guarantee should be valued at the full amount of €150,000 for the purposes of the PIA.

Gerard's unsecured debts after PIA restructuring

| | |
|-------------------------------------|-----------------|
| Personal Loan | €25,000 |
| Credit Card | €15,000 |
| Apartment 1 (Principal Reduction) | €100,000 |
| Apartment 2 (Principal Reduction) | €100,000 |
| Trade Supplier (Personal Guarantee) | €150,000 |
| Son's Mortgage (Personal Guarantee) | €1 |
| Owed to Unsecured Creditors | €390,001 |

Gerard's monthly income and expenses after PIA restructuring

| | |
|---|---------------|
| Monthly Net Income | €3,000 |
| Less: | |
| Principal Private Residence Mortgage | €928 |
| Childcare Costs | €0 |
| Total set costs | €1,045 |
| Available to Unsecured Creditors | €1,027 |

Gerard's monthly disposable income, after deducting total set costs and mortgage repayments, is €1,027 per month. This amount is now available to make payments to his unsecured creditors. This equates to €73,944 over six years.

6. REPAYMENTS TABLE

| Year | | | 1 | 2 | 3 | 4 | 5 | 6 | Totals | Return for Creditors |
|--|------------------|-------------|----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|----------------------|
| Net monthly income | | | € 3,000 | € 3,000 | € 3,000 | € 3,000 | € 3,000 | € 3,000 | | |
| Set costs | | | € 1,045 | € 1,045 | € 1,045 | € 1,045 | € 1,045 | € 1,045 | | |
| Rent/mortgage | | | € 928 | € 928 | € 928 | € 928 | € 928 | € 928 | | |
| Childcare | | | € 0 | € 0 | € 0 | € 0 | € 0 | € 0 | | |
| RLE | | | € 1,973 | € 1,973 | € 1,973 | € 1,973 | € 1,973 | € 1,973 | | |
| Monthly contribution | | | € 1,027 | € 1,027 | € 1,027 | € 1,027 | € 1,027 | € 1,027 | | |
| Annual contribution | | | € 12,324 | € 12,324 | € 12,324 | € 12,324 | € 12,324 | € 12,324 | € 73,944 | |
| Less PIP's fees | | | (€ 3,000) | (€ 1,500) | (€ 1,500) | (€ 1,500) | (€ 1,500) | (€ 1,500) | (€ 10,500) | |
| Net contribution | | | € 9,324 | € 10,824 | € 10,824 | € 10,824 | € 10,824 | € 10,824 | € 63,444 | |
| Repayment breakdown between creditors¹ | | | | | | | | | | |
| Personal Loan | € 25,000 | 6% | € 598 | € 694 | € 694 | € 694 | € 694 | € 694 | € 4,067 | 16% |
| Credit Card | € 15,000 | 4% | € 359 | € 416 | € 416 | € 416 | € 416 | € 416 | € 2,440 | 16% |
| Apartment 1 Write-down | € 100,000 | 26% | € 2,391 | € 2,775 | € 2,775 | € 2,775 | € 2,775 | € 2,775 | € 16,268 | 16% |
| Apartment 2 Write-down | € 100,000 | 26% | € 2,391 | € 2,775 | € 2,775 | € 2,775 | € 2,775 | € 2,775 | € 16,268 | 16% |
| Son's Mortgage PG | € 1 | 0% | € 0 | € 0 | € 0 | € 0 | € 0 | € 0 | € 0 | 16% |
| Trade Suppliers PG | € 150,000 | 38% | € 3,586 | € 4,163 | € 4,163 | € 4,163 | € 4,163 | € 4,163 | € 24,402 | 16% |
| | € 390,001 | 100% | € 9,324 | € 10,824 | € 10,822 | € 10,822 | € 10,822 | € 10,822 | € 63,444 | |

For the purposes of this scenario, it is estimated that the PIP fees are €10,500. Therefore Gerard's unsecured creditors will receive €63,433 on a proportionate basis over the lifetime of the PIA.

As part of developing the PIA proposal, the PIP will seek to agree fees with the creditors. Fees will vary in accordance with the complexity of a case and what is acceptable to the creditors. In proposing the fee amount, the PIP may suggest a staggered drawdown of the fee to reflect the upfront work associated with making an application and a proposal, as well as his/her other statutory duties during the lifetime of the PIA.

¹ For illustrative purposes and ease for the reader, figures shown in the repayments table have been rounded.

7. GERARD'S POSITION AFTER MEETING HIS DUTIES AND OBLIGATIONS UNDER THE PIA

- a) Principal Private Residence mortgage is now sustainable because:
 - Term is extended to lower repayments.
 - Unsecured debts are discharged.
- b) Gerard will have repaid €63,444 of his unsecured debts at the end of the term of the PIA and the remaining €326,556 is discharged. This represents a 16% return for the unsecured creditors based on amounts outstanding at the date of the issue of the Protective Certificate.
- c) Gerard is no longer liable for either of the personal guarantees he had entered into.
- d) Gerard is solvent.

8. Appendices

Appendix A: Gerard Meeting Voting Rights

| Threshold 1 – 65% vote required | Total Debt Vote | Voting Rights |
|---------------------------------|---------------------|---------------|
| PPR | €180,000 | 22% |
| Apartment 1 | €220,000 | 27% |
| Apartment 2 | €220,000 | 27% |
| Personal Loan | €25,000 | 3% |
| Credit Card | €15,000 | 2% |
| Trade Suppliers PG | €150,000 | 19% |
| Son's Mortgage (PG) | €1 | 0% |
| Total | €810,000 | 100% |
| Threshold 2 – 50% vote required | Secured Debt Vote | Voting Rights |
| PPR | €180,000 | 42% |
| Apartment 1 | €120,000 | 29% |
| Apartment 2 | €120,000 | 29% |
| Total | €420,000 | 100% |
| Threshold 3 – 50% vote required | Unsecured Debt Vote | Voting Rights |
| Personal Loan | €25,000 | 6% |
| Credit Card | €15,000 | 4% |
| Apartment 1 | €100,000 | 26% |
| Apartment 2 | €100,000 | 26% |
| Trade Supplier (PG) | €150,000 | 38% |
| Son's Mortgage (PG) | €1 | 0% |
| Total | €390,001 | 100% |