Personal Insolvency in a time of Covid-19

by Tom Murray

It has been suggested by the recently retiring Official Assignee in Bankruptcy, that the current Covid-19 pandemic may lead to a "flood of unmanageable debt".

Indeed, certain sectors, for example the hospitality, bar and restaurant trade, have experienced a sudden shock where their income disappeared almost without warning. Individuals had been asked to take or consider pay cuts, reduced hours and possibly a sabbatical to assist businesses in troubled sectors.

Furthermore, over the course of the past 6 months, this and other sectors have no clarity or certainty regarding how much longer the limitations on their trade will endure. Thousands of citizens have no clarity on their income and debt servicing prospects as we head into 2021 with Covid-19 still a real and continual variable in our lives.

We have been in this situation as a country before, when as a direct consequence of the financial crash in 2008 thousands of individuals and families were left insolvent. Back then it was as a result of a crippled property market combined with unsustainable mortgages on family homes and buy to let properties as well as personal debt arising from failed business ventures.

This time it is different. On the one hand there is not the same level of exposure to property debt and there is a higher level of personal savings in the country which will "buffer' to some extent individual circumstances.

In addition, we have a Government which is proactively attempting to support those in difficulty through wage and income subsidies and various business supports.

There are also "holidays' from tax and debt servicing which are providing temporary relief however, in many cases, this may simply be kicking the can down the road where hard decisions will be required.

However, the biggest difference between "then" and "now" is that we have a much more sophisticated personal debt solution regime in Ireland.

Back in 2007 the only option for a person with unsustainable personal debt was bankruptcy and back then a bankrupt remained in that position for 12 years unless a deal was negotiated with creditors.

However, the Bankruptcy Act 1988, which established the bankruptcy period as 12 years with no automatic discharge, has since been replaced by the Personal Insolvency Act 2012 (as amended).

These important pieces of legislation introduced a much more "debtor" friendly bankruptcy procedure whilst underlying its status as being the last resort for individuals by introducing two formal insolvency arrangements to enable an individual deal with unsustainable debts before resorting to bankruptcy.

Option 1: Debt Settlement Arrangement

A Debt Settlement Arrangement ("DSA") is an insolvency solution for people who have unsecured debts. If secured properties were sold and crystallised the debt, you could avail of a DSA.

Unsecured debts are debts where the unsecured creditor does not hold security over any assets. Secured debts cannot be covered in a DSA. A DSA must be agreed by the debtor and approved at a creditor's meeting by 65% of creditors (in value). In addition, it must be processed by the Insolvency Service of Ireland ("ISI") and approved by the Court.

Under a DSA, a debtor's unsecured debts subject to the DSA, will be settled over a period of up to 5 years (extendable to 6 years in certain circumstances). If successfully complied with, the debtor will be discharged from debts specified in the DSA at the end of the period.

Option 2: Personal Insolvency Arrangement

A Personal Insolvency Arrangement ("PIA") can include secured and unsecured debts, but certain debts cannot be included in a PIA and certain other debts require the consent of the creditor prior to being included. A limit of €3m currently applies to the amount of secured

debt that can be included in a PIA, unless all secured creditors consent to the inclusion of a higher amount.

The PIA differs from a DSA as it includes secured debt. Secured debt is a debt backed or secured by an asset (e.g. a housing loan where a house is mortgaged to secure the loan debt).

A PIA must be agreed by the debtor and approved at a creditors' meeting by a qualified majority of creditors. In addition, it must be processed by the ISI and approved by the Court.

Following the issue of a Protective Certificate, a PIA will be formulated by the Personal Insolvency Practitioner ("PIP"), agreed by the debtor, approved by a qualified majority of creditors voting at a creditors' meeting, processed by the ISI, approved by the Court and details of it registered in a public register maintained by the ISI. The three following creditor thresholds have to be met for the PIA proposal to be approved at the creditors' meeting:

- Total debt creditors, representing 65% or more of the total amount of debts due, participating and voting at the meeting, vote in favour of the proposal.
- Secured debt creditors, representing more than 50% of the value of secured debts, participating and voting at the meeting, vote in favour of the proposal. For this purpose, the value of a secured debt is the lesser of the value of the security or the amount of the debt.
- Unsecured debt creditors, representing more than 50% of the amount of unsecured debts, participating and voting at the meeting, vote in favour of the proposal.

Under a PIA, a debtor's unsecured debts will be settled over a period of up to 6 years (extendable to 7 years in certain circumstances) and the debtor will be released from those unsecured debts at the end of that period.

Bankruptcy

Bankruptcy is a formal court procedure which either you or one or more of your creditors owed at least €20,000 can start. Your assets and income are dealt with by a Government official called the Official Assignee.

Your assets (with certain exceptions) are sold to help pay your creditors. However, you can usually keep your personal belongings, the contents of your home and your tools of trade (which may include your car) up to a value of €6,000. the value of your car must not exceed €4,000.

On the date that you are adjudicated bankrupt you are allowed to retain €1,000 for reasonable living expenses in the form of cash in your possession or a current account with a bank. On the date of adjudication, all accounts held in credit by financial institutions, will be frozen. In addition, you will be instructed to remit the excess amount over €1,000 held at the date of adjudication to the Official Assignee shortly after adjudication.

Bankruptcy lasts for just one year if your income does not exceed reasonable living expenses as set out by the ISI. If you have surplus income after meeting your essential household and personal expenses, you will have to make payments out of your income for up to 3 years (albeit you are no longer a bankrupt after the first year is up).

If your income does not exceed the reasonable living expenses, then you should be discharged in one year. Once you have been discharged from your bankruptcy, you are released from your debts (with certain exceptions). The period of bankruptcy may be extended to 8 years, if you are dishonest or non-cooperative in your dealings with the Official Assignee.

Going forward into 2021

At time of writing we are in the middle of the first week of the nationwide Level 5 lockdown.

Cognisant of the difficulties that individuals are facing, and look like facing throughout 2021, Government have taken steps to further refine, reform and improve the personal insolvency regime in Ireland.

Currently someone applying for a personal insolvency arrangement can seek a court review under S115 Personal Insolvency (Amendment) Act 2015 if their principal private residence mortgage lender refuses what they believe to be a reasonable insolvency proposal. However, in order to seek this review their mortgage arrears must date from before January 1st 2015, a hangover of bad debt from the financial crisis.

However, Government has announced it is introducing an amendment to the Bankruptcy Act which will open up the possibility of an appeal/court review to those whose mortgages have gone into arrears more recently including those effected by the current pandemic. Further amendments will be made to the Act in 2021 to incorporate changes arising from the statutory review of the Act.

In any event, any individual who is anxious about their financial situation should sit down with their accountant who can refer them to a Personal Insolvency Practitioner who will help them find the best route through what is looking like another challenging year ahead.

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