Personal and Mortgage Debt:
Nine key principles to overcome the personal debt crisis

A statement by organisations & researchers working for those in debt

The organisations and researchers who have signed this statement have a strong track record of working and campaigning on anti-poverty issues including debt and credit, social housing, social welfare, homelessness and tenant's rights. We believe that the response of government to the current debt crisis has been inadequate and has failed to adequately consult with consumer representatives. This document sets out some broad principles and outlines an approach which we believe should form the basis of a much more fundamental policy response to this problem, a response that must be just, fair and equitable. The signatories to this statement continue to work in their own right in their own specialist areas of activity to achieve the objectives set out in this document.

On behalf of: ***Free Legal Advice Centres, Threshold, Focus Ireland, New Beginning, Society of Saint Vincent de Paul, Northside Community Law Centre, Ballymun Community Law Centre, Respond! Housing Association, Dr Stuart Stamp (NUI Maynooth), Ciara Murray (Public Information Consultant), Simon Brooke (Housing and Social Policy Consultant), Dr Michelle Norris (University College Dublin), Dr Padraic Kenna (NUI Galway).***

A summary of principles to address the debt crisis

1. **Over-indebtedness** – It is inability to pay rather than a lack of willingness to do so that is at the heart of the personal debt crisis. Over-indebtedness is a deep social and economic problem that requires a multi-dimensional strategic response from government.
2. **The need for data** - Comprehensive information is urgently needed to quantify the extent of the debt problem. Policy initiatives undertaken must be constantly evaluated in light of such data.
3. **Multiple debt** - Proposed solutions must take all debt liabilities into account to be effective and workable.
4. **Personal insolvency legislation -**There is an immediate need for the introduction of personal insolvency legislation. A Debt Resolution Agency should be established to oversee the legislative scheme to ensure transparency and consistency.
5. **Debt write-off -** Insolvent debtors should pay to the best of their ability for a limited time period and remaining debt should then be written off.
6. **Access to representation -** Debtors must be entitled to have an advocate represent their interests in negotiations to agree or processes to contest debt repayments.
7. **Minimum income -** Debtors must be entitled to a minimum income to meet their basic needs while repaying debts.
8. **Unsustainable mortgages** - The fact that some mortgages are unsustainable must be recognised and where repossession results, appropriate social housing and social welfare rights must be provided to such households.
9. **Retention of dwelling -** State supports should aim to keep people in their homes where possible, whether in an ongoing mortgage or as a tenant where appropriate.

The rationale behind these basic principles is set out below in more detail.

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1. THE PROBLEM AND ITS CAUSES

Over-indebtedness (which we define as a persistent inability to meet essential living expenses and debt repayments as they fall due) is at the heart of the current debt crisis in Ireland. What many perceive to be primarily a "mortgage arrears" problem is in fact a much broader and deeper social and economic problem and hence it requires a multi-dimensional and co-ordinated strategic response, in both social and economic terms.

On the basis of the empirical evidence available to us, we suggest that over-indebtedness is caused in most instances by socio-economic factors largely beyond the power of the individual to control; the external factors that lead to loss of income such as unemployment, failed enterprise, ill-health or relationship breakdown.

We would also suggest that over-indebtedness is strongly associated with poverty, inequality and financial exclusion. These factors both cause over-indebtedness and are consequences of it. Throughout the credit boom, for example, those on lower incomes continued to pay more for credit, particularly to sub-prime lenders. In turn, disproportionate amounts of now reduced incomes being swallowed up by debt repayments have left many households with insufficient income to meet their needs.

It is our view that institutional practices drove the growth in borrowing and were the primary cause in resulting over-indebtedness. These same lending practices were facilitated by regulatory, statutory and government inaction and indifference. The consequences of such inaction led to an inordinate focus on the economy to the detriment of society and both are now in need of drastic repair as a result. While each individual household is held to account for its actions, their responsibility to remedy the situation rests with the government.

2. THE PROBLEM AND ITS CONSEQUENCES

It is clear that increasing numbers of people now lack both resources and options, and there is no blinding light at the end of the tunnel in economic terms. Many who are over-indebted have lost their jobs or businesses; others are surviving on substantially reduced incomes. This is therefore not a case of deliberately choosing not to pay but of lacking capacity to do so. Many families thus live a daily nightmare of juggling scant resources in the face of regular but unregulated pressure from a variety of creditors or debt collectors acting on their behalf, a war of attrition that will have untold 'downstream' consequences for the health and welfare of society as a whole. To leave people in this plight with no comprehensive structure to resolve their indebtedness is not only an abdication of the State's social responsibility to its citizens, it is short-sighted from an economic perspective. A failure to take account of the costs of doing nothing is a failure of accountability in the dispersal of scarce state resources.

3. AN EVIDENCE DEFICIT

We also believe that a lack of data and 'hard' evidence is hindering reform. The recent publishing of data on mortgage arrears by the Central Bank is welcome, although more depth in the figures would be beneficial. However, there is a critical lack of corresponding statistics on consumer credit arrears as well as rent and utility debt. Hence, we do not know the full extent of over-indebtedness in Ireland and crucially, we do not know who is most affected and why, and what is coming down the tracks. The Central Bank should require "arrears data" from all lenders (and the government from all state and semi-state creditors) in order to present a picture of where we really stand.

Together with the lack of an independent evaluation of current policy initiatives – for example, a rolling assessment of the results and effectiveness of the Mortgage Arrears Resolution Process (MARP) set out in the Code of Conduct on Mortgage Arrears - the consequence is an evidence-deficit, which hampers informed and responsible policymaking.

4. AN "ALL DEBT" INTEGRATED POLICY RESPONSE

There are no quick fix solutions and a policy focusing on one part of the problem, such as mortgage arrears, or on one aspect of the solution, such as industry resolution processes, is inadequate. What is needed is a comprehensive policy framework that addresses the various components of over-indebtedness.

Muddling along in the hope that things will get better is no longer acceptable. The social costs **–** mental health problems, crime, increasing pressure on welfare budgets **-** are potentially enormous as families and communities disintegrate under the weight of financial pressure and the uncertainty of what the future will bring. From an economic perspective, the lack of a plan of action and a sense of the State assuming responsibility hampers consumer spending and fresh lending. Indeed, it is notable that the International Monetary Fund (IMF) has insisted as part of the terms of the bailout that personal insolvency legislation be introduced in this country by the end of the first quarter of 2012.

5. PERSONAL INSOLVENCY LEGISLATION

Mortgage arrears have up to now grabbed the lion's share of public and media attention. It should be also said that rent arrears in both local authority and private rented accommodation are also a significant problem but again a lack of concrete information on the scale of these difficulties is apparent.

However, the bottom line from our perspective is that to be workable, proposed solutions to the debt crisis must take all debts into account. There is, for example, little to be gained in negotiating a revised affordable mortgage payment that will enable a household to stay in the family home without simultaneously reaching agreement on the repayment of other personal debts. Pressure from creditors in the form of threats of legal action if insufficient payments are made, and the potential for the enforcement of judgments (including their conversion into judgment mortgages) where they are obtained, has been and continues to be an obstacle in the way of attempts to reach settlements that are sustainable. The Law Reform Commission sums it up succinctly by stating that '*the holistic approach to personal debt requires that both mortgage and non-mortgage personal debt must be considered in order to provide satisfactory solutions to the problem of personal indebtedness'*[1].

The need for personal insolvency legislation to resolve multiple debt situations and to bring us into line with European best practice is urgent. The public interest demands it. Debtors who cannot pay in full must pay to the best of their ability over a defined period of time and in return remaining debt (including legacy debt following repossession of the family home) must be written off to allow for a 'Fresh Start'. Those currently drowning in a sea of debt desperately need this lifeline and the institutions 'stress tests' have in all probability already provided for it.

Such arrangements should prioritise the maintenance of the household in the family home where at all possible, but it is accepted that this may not be possible in a number of cases. However, we believe that a targeted restructuring of existing mortgage payments and potential write down of arrears should be examined in limited cases where it may serve to ensure the viability of the mortgage. The necessity to factor mortgage debt into a new personal insolvency regime in order to effectively settle debts is a tall order but nonetheless it is our conclusion that it is a grim reality in our current situation. Failing to deal with this reality will not make the necessity disappear.

6. "SETTLEMENT" NOT "FORGIVENESS"

'Moral hazard', or the fear that potential personal insolvency schemes will be hijacked by the undeserving, has also appeared to be a substantial impediment to remedial action. The debate has not been helped by the shallow characterisation of such schemes as 'debt forgiveness'. We strongly object to this term as it implies that 'blame' lies predominantly with the borrower, when the cause of indebtedness is most often factors beyond people's control and the reckless lending of credit institutions. A much more appropriate term, we would contend, to express the ethos behind personal insolvency legislation is "debt settlement", a process where an insolvent debtor makes payments to the best of his/her ability over a defined period of time prior to obtaining a write off of residual debt.

The use of the term "debt forgiveness" also implies that borrowers will somehow receive instant and painless absolution. This fundamentally misunderstands the nature of personal insolvency schemes as they operate throughout Europe and across the world. The settlement of debts generally requires a substantial commitment and considerable sacrifices on the part of the debtor in return for eventual debt write-off. We believe that a comprehensive process with a rigorous examination of finances and penalties for false declarations would act as a sufficient and substantial deterrent in most cases where borrowers are tempted to seek write-offs when in reality they have the capacity to repay.

7. EFFECTIVE STRUCTURES TO FACILITATE REPAYMENT ARRANGEMENTS

The effective settlement of debts under a personal insolvency scheme cannot be achieved in our view without the establishment of an independent Debt Resolution Agency to achieve consistency and transparency. Such a body would operate in private and would encourage mediated settlements in a non-adversarial environment. However, it must also have statutory powers to make independent binding adjudications where necessary (subject to a right of appeal into the courts), having engaged in a full enquiry into the debtor's financial and other circumstances. This will require sound judgment and a high level of expertise and there will undoubtedly be costs associated with the setting up of this infrastructure. However, we believe that as a society we simply have no choice at this juncture. In any case, some of these costs will be offset by removing many debt collection cases from the civil courts.

[1] Law Reform Commission Final, Interim Report – Personal Debt and Debt Management, page 5

8. INDEPENDENT ADVOCACY

The availability of independent advocates to work with and represent the interests of the debtor is also an essential part of the landscape to settle personal indebtedness and will be critical to the prospects of personal insolvency legislation being a success. Households in debt need assistance to face their difficulties, to assemble sustainable proposals, to explain procedures, to question decisions where necessary and to maintain a focus on discharging agreed obligations. In this regard the work of the Money Advice and Budgeting Service has been instrumental for almost two decades. We believe that independent and accessible money advice and legal advice must be provided to debtors and that organisations providing such services must be properly resourced.

9. MINIMUM HOUSEHOLD INCOME

The current piecemeal 'case by case' as opposed to systematic approach to mortgage and personal debt negotiation has allowed some lending institutions to minutely question the daily expenditure of households and to use the threat of legal proceedings to extract excessive payments. In some cases, this has driven down the residual income retained by the household to unsustainable and damaging levels, with all the consequences that follow for the health and welfare of household members (particularly children) and the integrity of relationships.

In our view, households should not be forced below the poverty line in an attempt to repair damaged loan books. From a human rights perspective and to ensure that processes are workable and sustainable, there is a clear need to set agreed thresholds of minimum income (dependent on household composition) to meet essential living expenses which are immune from debt repayment. Any surplus should be available for distribution to creditors. This is the approach taken across Europe in debt settlement schemes.

10. THE HOUSING DEBT PROBLEM

- **The evidence**

At the end of 2010, one in ten residential mortgages was in trouble. By March 2011, it was one in nine. At the end of June 2011, almost one in every eight mortgages was struggling.[2] Reductions in take home pay due to tax changes and reduced working hours renders more and more households vulnerable. The average arrears per household in the six months plus category that comprises some 40,000 mortgages is €21,000. There is also tangible evidence within the mortgage arrears data that lenders are obtaining court orders in a number of cases but not executing them; the depressed state of the property market and the spectre of negative equity may well explain this.[3] Nonetheless, even with a comparatively low level of new repossession cases in the courts, the number of houses returning to lenders has steadily increased quarter upon quarter.[4] It is also notable that the numbers of voluntary surrenders or abandonments (625) during the two years for which we have figures from the Central Bank substantially outnumbers actual repossessions (263) by a factor of about two and a half to one. A number of borrowers have therefore seen the writing on the wall. In summary, there is evidence within the figures of a worsening arrears problem while lenders play a waiting game.

- **Unsustainable mortgages**

Mortgage arrears is not just a debt problem, it is now also part of a wider social housing problem. Some mortgages are simply unsustainable. This reality must be factored into any proposed set of solutions and both the social housing and social welfare implications of this must be taken into

[2] This amounts to 95,158 of the total number of 777,321, comprising 55,763 mortgages in arrears and 39,395 'restructured' mortgages. Although mortgages in the restructured category are described as 'fully performing', they are only performing according to the terms of the restructuring arrangement and it is worth noting that the Central Bank states that 'the data collected on restructures relate solely to those principal dwelling house mortgages restructured due to financial distress'.

[3] 909 Possession Orders have been granted in the past two years, with only 263 actual repossessions taking place

[4] Mortgage lenders now collectively hold a stock of 809 properties repossessed as a result of court orders or voluntary surrenders/abandonments, up from 243 at the end of June 2009

account, as well as the legacy debt that will arise where such properties are in negative equity. Recognising unsustainable mortgages and supporting people appropriately into more viable accommodation arrangements should also free up limited resources to be devoted to support potentially sustainable mortgages. For example, there is a clear rationale for the more effective use of the Mortgage Interest Supplement payment in this regard. There is also an urgent need to produce more social housing units.

- **Retention of dwelling**

The overriding objective of any mortgage arrears resolution strategy should nonetheless be to facilitate people wherever possible to remain in their homes. The Mortgage Arrears Resolution Process (MARP) begins this process by obliging lenders to consider a range of mechanisms, generally referred to as 'standard forbearance', to reschedule payments and provide breathing space for those in arrears or pre-arrears. The final report of the Cooney Group further proposed a Deferred Interest Scheme [5] but the voluntary nature of this scheme and the lack of up-to-date information on how it is working are notable. The same report specifically recommended against the adoption of any formal scheme whereby the borrower would continue to reside in the family home despite the mortgage being unsustainable.

However, given the large numbers already on waiting lists when compared to the availability of social housing, we believe that mechanisms that promote the retention of the dwelling must be examined much more closely and must form part of a range of solutions in appropriate cases where desired. These should include both mortgage-to-shared equity and mortgage-to-rent schemes. A mortgage-to-shared equity scheme would involve the State purchasing a dwelling at a substantial discount from the lender, taking an equity stake and then restructuring instalments to reflect current financial circumstances but with provision for borrower buy-back where financial circumstances improve. Mortgage-to-rent on the other hand would involve the purchase of the dwelling (again at a substantial discount) by a housing association or a local authority with the former borrower becoming a tenant at an affordable rent.

Finally, it should also be noted that the mortgage debt crisis has also impacted not just on borrowers/homeowners but also on (private) tenants, including those whose homes are in buy-to-let apartments, where the investor/borrower is facing repossession and the tenant is therefore faced with eviction. Equally, insufficient attention has been paid to local authority tenancies and housing loans in arrears. Proposals to ensure that these categories of household are protected from eviction, wherever possible, must also be developed.

11. CONCLUSION

We believe that over-indebtedness is a social as well as an economic problem that adversely impacts on virtually all sections of society but particularly those with the least resources. We suggest that a coherent, wide-ranging response is therefore required that would consist of a clear definition of the extent of the problem, together with putting in place the preventative, curative and rehabilitative elements to address it. The social and economic costs of the minimal policy intervention we are currently experiencing will, in all likelihood over time, outweigh the costs of responding comprehensively now. We therefore urgently call for a national strategy to be put in place to resolve over-indebtedness and to foster a responsible credit market that would prevent a similar crisis from occurring for future generations.

[5] Mortgage Arrears and Personal Debt Group – Final Report, 16th November 2010, Pages 22 -23.