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An Comhchoiste um Dhlí agus Ceart, Cosaint agus Comhionannas

Tuarascáil maidir leis an Téarma Féimheachta in Éirinn

Iúil 2015

Houses of the Oireachtas

Joint Committee on Justice, Defence and Equality

Report on the Term of Bankruptcy in Ireland

July 2015

31/JDAE/030

Contents

Chairman’s Preface	2
Introduction	3
Law on Bankruptcy	4
Observations	6
Conclusions and Recommendation	9
Appendix 1 – Published submissions	

Chairman's Preface

The issue of bankruptcy is a matter that retains renewed and very relevant context in the aftermath of the banking crisis and consequent financial collapse.

The Committee opened a consultation process on one very specific matter, should the term for bankruptcy in Ireland be reduced from 3 years to 1 year.

The call for submissions resulted in over 100 submissions being received from a wide range of stakeholders and interested parties.

Many of the submissions from private individuals contained some personal and detailed accounts of experiencing bankruptcy. While the Committee has taken note of the contents of all submissions it has decided only to publish submissions from organisations.

The law relating to personal insolvency has undergone significant and radical reform recently and the bankruptcy term was reduced from 12 years to 3 years.

In addition, newer debt settlement concepts have been introduced, including the Debt Relief Notice (DRN), Debt Settlement Arrangement (DSA) and Personal Insolvency Arrangement (PIA). It must be remembered that not all creditors are large organisations but can also take the form of small town businesses, suppliers and contractors. Therefore, a balance must be struck between debtors and creditors taking account of the justice of each and every case. Bankruptcy should not be used a "quick fix" solution for someone in financial difficulties to the detriment of their creditors when other solutions might be more equitable.

However, based on this process, the Committee believes that this issue should be kept under constant review and believes that the mechanism of bankruptcy should aid recovery in the fairest possible way, but not punish the debtor.

Finally, I would like to express my gratitude to all those who took the time to make a submission, the contents of which have been noted by the Committee.



A handwritten signature in black ink, which appears to read "D Stanton". The signature is written in a cursive style and is positioned above a horizontal line.

David Stanton T.D.
Chairman
July 2015

Introduction

At its meeting of 27th May 2015, the Committee had an engagement with the Insolvency Service of Ireland to receive an update on the recently introduced aspects to debt insolvency arrangements.

Arising from this, the Committee decided to examine the issue of the bankruptcy term but particularly to focus on the very specific issue of whether the term for bankruptcy in Ireland should be reduced from 3 years to 1 year.

The Committee published a call for submissions from interested parties and received a total of 122 submissions.

Many submissions contained some very detailed and personal accounts, demonstrating the wide-reaching effect debt has had on Irish society in recent years.

At its meeting of 8th July 2015, the Committee considered the submissions received and this report sets out the main points made in the submissions on which the Committee has made some observations.

This Report has been sent to the Minister for Justice and Equality and the Committee looks forward to engagement on this matter.

Law on Bankruptcy

Section 85 of the Bankruptcy Act 1988, as amended by the Personal Insolvency Act 2012, provides for automatic discharge after three years. However, if the Official Assignee or a creditor objects to discharge due to the applicant's failure to co-operate or non-disclosure, it may be suspended for up to eight years.

The bankrupt may also be ordered to make payments for up to eight years after the individual was adjudicated bankrupt under section 85D of the Act.

It is also worth noting that there is a prospect of EU harmonisation of bankruptcy arrangements. The European Commission, in its Recommendation of 12th March 2014 on a new approach to business failure and insolvency, suggested entrepreneurs should be discharged after 3 years.

Other jurisdictions take varying approaches to bankruptcy:

- In Northern Ireland, England and Wales, a one year term applies. However, an Official Receiver may impose a Bankruptcy Restriction Order for between 2 and 15 years. The bankrupt is automatically discharged after the one year term if there is no restriction. A shorter discharge is also possible if a notice is filed with the High Court.
- In Australia, a three year term applies. However, if the trustee objects this may be extended to between 5 and 8 years. If there is no objection, the bankrupt is automatically discharged upon completion of the term. There is no provision for a shorter bankruptcy but it may be annulled in certain circumstances.
- In the USA, the bankruptcy term varies and if creditors object, the discharge period may be extended. If there is no objection, the bankrupt is automatically discharged upon completion of the term. If creditors do not submit motions to the Court within a specified timeframe, then the Court may grant a shorter discharge.

The forms of bankruptcy in the United States may be as follows:

- Chapter 7 (Liquidation): approximately four months after the date the debtor files the petition with the clerk of the bankruptcy court.
 - Chapter 11 (Reorganisation): discharge upon completion of debt repayment plan, which may take a number of years;
 - Chapter 12 (Adjustment of debts of a family farmer or fisherman): approximately four years after the date of filing; and
 - Chapter 13 (Adjustment of debts of an individual with regular income): approximately four years after the date of filing.
- In Canada, the bankruptcy term ranges from 9 months to 3 years. However, the Court may suspend a discharge and the debtor may also apply early for a

discharge. If there is no such change, the bankrupt is automatically discharged upon completion of the term.

There is also an additional consideration on what proportion of the debtor's income goes towards his or her debts while in bankruptcy, with a number of jurisdictions taking different approaches.

- In Ireland the Personal Insolvency Service of Ireland has an obligation under section 23 of the Personal Insolvency Act 2012 to produce Guidelines on a Reasonable Standard of Living and Reasonable Living Expenses. The amount varies depending on the circumstances of the individual, their spouse or co-habitant and the age of any dependent children.
- In England and Wales the Insolvency Service produces a Household Expenditure Survey and uses this information to calculate income payment agreements. There is no set standard as housing costs are individually assessed.
- In Canada, there is provision for individuals whose income exceeds a certain amount while in bankruptcy to have to pay 50 per cent of their excess income to their bankruptcy trustee. The threshold may be adjusted if the debtor is co-habiting or has dependent children. However, the amount to be paid is adjusted for the share of the household income the bankrupt earns.
- Australia has a similar arrangement to Canada, i.e. 50 per cent of a bankrupt's excess income (while in bankruptcy) goes towards their debts. However, the excess income threshold depends on the individual circumstances of the bankrupt and no details are available on the thresholds.
- In the USA when filing for bankruptcy the debtor must produce "a detailed list of the debtor's monthly living expenses, i.e., food, clothing, shelter, utilities, taxes, transportation, medicine, etc." In a Chapter 13 bankruptcy if their income is higher than the median income in their State they must pay all their income above a set amount to their Trustee. This amount is based on standard expenses set by the Internal Revenue Service. These expenses can be State, City and/or county specific.

Observations

The Committee noted overwhelming support in submissions towards reducing the bankruptcy term from 3 years to 1 year.

There were many arguments in favour of a reduction:

- It is necessary to aid the economic recovery of the State and to enable many of those caught up in bankruptcy to become positive contributors to the economy as quickly as possible. The Committee observed this as a common trend from a number of submissions.
- A one year term would make the financial institutions engage more with debtors in reaching meaningful solutions and encourage further engagement with the DSA and PIA processes.
- It would pass on the benefits of economic recovery to all citizens by allowing people with crippling levels of debt associated with credit obtained during the economic boom to move on from that debt. This would allow the debtor to return to economic normality much faster. A particular context for this is the issue of negative equity.
- A reduction would bring Ireland in line with the United Kingdom and other common law jurisdictions.

The Committee was also told in submissions that the family home should be offered an element of protection. One submission expressed the view that banks may be willing to offer forbearance on mortgage debt for one year while the bankrupt goes through the process. Whether this takes the form of detaching this asset from the debtor's other debts, or transferring the asset elsewhere and allowing the mortgagor enter an alternative arrangement via the Official Assignee is a matter that the Committee feels warrants a serious and detailed level of consideration.

A smaller number of submissions were opposed to the proposal for a reduction in the term. However, in the Committee's view these did raise a number of issues:

- From the perspective of Credit Unions the debt represents other members' savings and the debtor undertaking a level of endurance before it can be written-off is argued as equitable.
- The view was expressed that the reduced time period of 1 year makes it too easy for the bankrupt to defer asset/income acquisition until after that date expiry. In addition, newer debt solutions, such as the PIA and DSA would become less attractive.
- Rather than reducing the term in all cases, the argument was made that the Official Assignee should be given the right to apply to the High Court to

discharge the bankrupt earlier. This would occur where the bankrupt has cooperated with the process and there is nothing further to be gained by enforcing the full three years.

A number of alternative suggestions were made to the Committee, including the following:

- Reducing bankruptcy to one year for combined debts of less than €500,000 with a longer term applied to large business debts with more complex forms of accounting. In one submission, it was argued that “this would ensure that those whose only crime was to purchase a home, and have since had to turn to bankruptcy, would be treated more fairly”;
- Similarly, a reduced bankruptcy term may be extended to 3 years if there is no cooperation from the debtor;
- Establishing an appeals mechanism for decisions of the Official Assignee as an alternative to reduced bankruptcy;
- Enabling the system in place to identify legitimate business bankruptcies from other bankruptcies
- The introduction of additional measures such as an early warning system and a second chance programme to operate alongside bankruptcy legislation;
- That availing of the one year bankruptcy term is dependent on having applied for the PIA and DSA processes or not having engaged in fraudulent and reckless trading;
- There was also the suggestion of making mortgage to rent schemes compulsory for banks as a mechanism for addressing the high level of home repossessions.
- An early discharge would enable the debtor to secure new credit / funds to purchase the remaining equity in the family home from the Official Assignee.

As well as the arguments for and against bankruptcy, the Committee made a number of further observations from submissions that it believes also warrant further consideration.

- The Committee observed an overwhelming support for reducing the term of bankruptcy from three years to one year. In addition, the Committee also noted support for reducing the associated income payments order, e.g. from 5 years to 3 years.
- The Committee also observed the issue of economic activity on the part of insolvent persons. One submission raised the issue of bankrupt persons not working for three years as a strategy to avoid having an income.

- The Committee observed a suggestion to adopt non-recourse lending for private mortgage similar to what is applied in the USA, which would ensure prudential lending by the regulated banks carrying on business in this State.
- The Committee also observed, through the vast number of very personal stories it received, that there are serious mental, emotional and psychological impacts of bankruptcy, which the Committee feels should not be ignored.
- The issues of bad faith and moral hazard were also raised. The Committee suggests that the appropriate safeguards are put in place to address situations where the bankrupt is not cooperative or acts in bad faith. Allowing the term to be extended to two or three years may be appropriate in such circumstances.
- As mentioned above, the Committee was also told in submissions of introducing a mortgage-to-rent scheme and that it be made a compulsory element of the process.
- Finally, the Committee also suggests that consideration is given to examining the enhancement of promotion of the Insolvency Service of Ireland and the alternative processes available to debtors.

Conclusions and Recommendation

Based on the submissions, the Committee concluded that a number of possible recommendations should be considered:

1. Retain the term at 3 years. As the term has only been reduced relatively recently it may be too early to further reduce it as any long term effects may not yet be apparent;
2. Reduce the term to 1 year. This is based on the view expressed in the majority of submissions;
3. Retain the 3 year term but allow for an application to be made for a reduced term in certain specified circumstances. A reduced term could be considered where there is no evidence of recklessness;
4. Reduce the term to 1 year but provide for an application for an extension by the Official Assignee of up to 3 years in certain circumstances.

A term of between 1 year and 3 years could apply to a bankrupt in certain circumstances, for example: where non-cooperation with the Official Assignee is evident; there is excessive unsecured debt (as opposed to mortgage or business debt); the “moral hazard” issue whereby bankruptcy is more attractive than other more equitable solutions.

Recommendation:

The Committee’s recommendation to the Minister for Justice and Equality is conclusion number 4 above – a reduction in the term to 1 year but provide for an application for an extension by the Official Assignee of up to 3 years in certain circumstances.