OPINION

In the matter of:
Record Number:

Querist: Association of Personal Insolvency Practitioners
Agent: Ashtown Gate Solicitors
Counsel: Keith Farry B.L.

Re: Negative Equity and Deferred Debt Payments
Date: 05/05/16

Counsel has been asked to consider two matters;

1. Should negative equity be treated as an unsecured debt in the construction of a Personal Insolvency Arrangement (hereinafter "The First Question"),

2. In the context of the above, does section 102(6)(d), referring to deferral of secured debt payments, exclude warehousing of debt that is not previously contracted by way of mutually agreed amended mortgaged terms (hereinafter "The Second Question").

1. Factual Background

There is no factual background however counsel will use the following "facts";

- The query relates to a Principal Private Residence secured debt.
- The property is in significant negative equity.
- The property is valued at €150,000 with a mortgage balance of €300,000.
- The Principal Private Residence was in arrears pre January 2015.
- The Principal Private Residence is suitable for the needs of the family that reside therein.

- An undisputed class of creditors supported the PIA.

2. Matters requiring clarification

There are no matters requiring clarification.

3. Issues Arising

For the purposes of this opinion counsel has identified two issues. Firstly, whether there is an obligation to treat negative equity in a particular way in a Personal Insolvency Arrangement proposal and secondly, is the practice of warehousing a portion of a mortgage beyond the term of a Personal Insolvency Arrangement incompatible with law.

In considering the above, counsel has taken account of the development of Personal Insolvency Practitioner practice in the context of an exercisable determining veto by dominant creditors, and further, counsel has now looked beyond such a landscape in light of the new section 115A appeal mechanism. Of relevance to the herein opinion are the Central Bank of Ireland regulations on residential mortgage lending (S.I. No. 47 of 2015 Central Bank (Supervision and Enforcement) Act 2013 (Section 48) (Housing Loan Requirements) Regulations 2015) in the context of loan to value ratio ("LTV"), sustainability and affordability of new mortgage lending when considered with Personal Insolvency Arrangement mortgage restructures in mind.

3. 1. Definitions

In order to properly consider the questions posed above, a number of crucial definitions are required.

Personal Insolvency Acts 2012 to 2015 – Section 2

> **"creditor",** in relation to a debt, means a natural or legal person to whom a debtor owes that debt or to whom the debtor or otherwise has a liability in respect of that debt;

“debtor”, in relation to a debt, means a natural person who –

(a) owes a debt to a creditor, or
(b) otherwise has a liability to a creditor;

“insolvent”, in relation to a debtor, shall be construed as meaning that the debtor is unable to pay his or her debts in full as they fall due;

“secured creditor”, in relation to a debt, means a creditor of the debtor who holds, in respect of his or her debt, security (other than a guarantee or pledge referred to in section 35(8) of the Credit Union Act 1997) in or over property of the debtor;

“secured debt” means a debt the payment for which is secured by security in or over any asset or property of any kind;

“security” means, in relation to a debt, any means of securing payment of the debt and includes—

(*a*) a mortgage, judgment mortgage, charge, lien, pledge, hypothecation or other security interest or encumbrance or collateral in or over any property (whether real or personal and including choses-in-action),

(*b*) an assignment by way of security, and (*c*) an undertaking or agreement by any person (including a solicitor) to give or create a security interest in property;

“unsecured creditor”, in relation to a debt, means any creditor who is not a secured creditor;

“unsecured debt” means a debt in respect of which payment is not secured by security.

“mortgage” includes any charge or lien on any property for securing money or money’s worth; LCLRA

“annuity mortgage” means a mortgage wherein the principal sum advanced by the mortgagee (lender) is intended to be repaid by the mortgagor (borrower) in regular, usually monthly, instalments which comprise both principal and interest on the principal outstanding. Contrast with endowment mortgage.

“redemption” means the repayment of a mortgage debt whereby the equitable and legal estates merge in the mortgagor.

“credit” means the time which a creditor allows his debtor to pay a debt; the total amount he permits the debtor to borrow or to owe. *Credit* includes a deferred payment, cash loan, or any other form of financial accommodation: Consumer Credit Act 1995 s.2(1);

“credit agreement” means an agreement whereby a creditor grants or promises to grant to a consumer a credit in the form of a deferred payment, a cash loan or other similar financial accommodation: Consumer Credit Act 1995 s.2(1).

“credit facility” includes every kind of financial accommodation (including a loan facility, a line of credit, a hedging facility, a derivative facility, a bond, a letter of credit, a guarantee facility, an invoice discounting facility, a debt factoring facility, a deferred payment arrangement, a leasing facility, a guarantee, an indemnity and any other financial accommodation giving rise to a payment or repayment obligation) provided to a debtor or associated debtor, whether alone or together with another person or persons and whether as part of a syndicate or otherwise: National Asset Management Agency Act 2009 s.4.

Applicable provisions within the Personal Insolvency Acts 2012 to 2015

Not all of the sections detailed hereunder will be opened fully in the course of this opinion but may be required as a point of reference.

Section 98.— (1) Where a protective certificate has been issued, the personal insolvency practitioner shall as soon as practicable thereafter—

(*a*) give written notice to the creditors concerned that the personal insolvency practitioner has been appointed by the debtor for the purpose of making a proposal for a Personal Insolvency Settlement Arrangement and, subject to *section 101(2)*, invite those creditors to make submissions to the personal insolvency practitioner regarding the debts concerned and the manner in which the debts might be dealt with as part of a Personal Insolvency Arrangement, and such notice shall be accompanied by the debtor's completed Prescribed Financial Statement,

(*b*) consider any submissions made by creditors regarding the debts and the manner in which the debts might be dealt with as part of a Personal Insolvency Arrangement, including—

(i) any submission made by a creditor with respect to previous or existing offers of arrangements made by the creditor to or with the debtor, and

(ii) any submission made by a secured creditor in accordance with *section 102*.

Section 99(2)(*c*) where the debtor performs all of his or her obligations specified in a Personal Insolvency Arrangement, he or she shall not stand discharged from the secured debts covered by the Personal Insolvency Arrangement except to the extent provided for under the terms of the Personal Insolvency Arrangement;

Section 99(2)(*h*) a Personal Insolvency Arrangement shall not require that the debtor dispose of his or her interest in the debtor's principal private residence or to cease to occupy such residence unless the provisions of *section 104(3)* apply;

Section 99(2)(*k*) subject to *sections 102* to *105*, a Personal Insolvency Arrangement shall make provision for the manner in which security held by a secured creditor is to be treated; and

Section 100(2) The terms of a proposal for a Personal Insolvency Arrangement may include any one or more of the following: (*f*) in respect of

secured debts, subject to *sections 102* to *105*, an arrangement for the treatment of the security and the satisfaction or restructuring of the secured debt.

Section 102.— (1) Where a secured creditor has been notified by the personal insolvency practitioner that a protective certificate has been issued in respect of the debtor the secured creditor concerned shall furnish to the personal insolvency practitioner an estimate, made in good faith, of the market value of the security and the creditor concerned may also indicate, a preference as to how, having regard to *subsection (3)* and *sections 103* to *105*, that creditor wishes to have the security and secured debt treated under the Personal Insolvency Arrangement.

(2) In formulating the proposal for a Personal Insolvency Arrangement the personal insolvency practitioner shall—

(*a*) have regard to *subsection (3)* and *sections 103* to *105*, and

(*b*) to the extent that he or she considers it reasonable to do so, have regard to the preference of the secured creditor furnished under *subsection (1)* as to the treatment of the security and the secured debt.

(3) Subject to *sections 103* to *105*, the terms of a Personal Insolvency Arrangement may provide for the manner in which the security for a secured debt is to be treated which may include:

(*a*) the sale or any other disposition of the property or asset the subject of the security;

(*b*) the surrender of the security to the debtor; or

(*c*) the retention by the secured creditor of the security.

(5) 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.

(6) Without prejudice to the generality of *section 100*or *subsections (1)* to *(3)* and subject to *sections 103* to *105*, a Personal Insolvency Arrangement may include one or more of the following terms in relation to the secured debt:

(*a*) that the debtor pay interest and only part of the capital amount of the secured debt to the secured creditor for a specified period of time which shall not exceed the duration of the Personal Insolvency Arrangement;

(*b*) that the debtor make interest-only payments on the secured debt for a specified period of time which shall not exceed the duration of the Personal Insolvency Arrangement;

(*c*) that the period over which the secured debt was to be paid or the time or times at which the secured debt was to be repaid be extended by a specified period of time;

(*d*) that the secured debt payments due to be made by the debtor be deferred for a specified period of time which shall not exceed the duration of the Personal Insolvency Arrangement;

(e) that the basis on which the interest rate relating to the secured debt be changed to one that is fixed, variable or at a margin above or below a reference rate;

(*f*) that the principal sum due on the secured debt be reduced provided that the secured creditor be granted a share in the debtor's equity in the property the subject of the security;

(*g*) that the principal sum due on the secured debt be reduced but subject to a condition that where the property the subject of the security is subsequently sold for an amount greater than the value attributed to that property for the purposes of the Personal Insolvency Arrangement, the secured creditor's security will continue to cover such part of the difference between the

attributed value and the amount for which the property is sold as is specified in the terms of the Personal Insolvency Arrangement;

(*h*) that arrears of payments existing at the inception of the Personal Insolvency Arrangement and payments falling due during a specified period thereafter be added to the principal amount due in respect of the secured debt; and

(*i*) that the principal sum due in respect of the secured debt be reduced to a specified amount.

(11) Without prejudice to *section 103*, where a Personal Insolvency Arrangement includes terms providing for a reduction of the amount of debt (including principal, interest and arrears) secured by the security as of the date of the issue of the protective certificate to a specified amount, the terms of the Arrangement shall, unless the relevant secured creditor agrees otherwise, also include a term providing that the amount of such reduction shall:

(*a*) rank equally with, and abate in equal proportion to, the unsecured debts covered by the Arrangement; and

(*b*) be discharged with those unsecured debts on completion of the obligations specified in the Arrangement.

Section 103 - Protections for secured creditors in Personal Insolvency Arrangement.

Section 103(2) A Personal Insolvency Arrangement which includes terms providing for—

(*a*) retention by a secured creditor of the security held by that secured creditor, and

(*b*) a reduction of the principal sum due in respect of the secured debt due to that secured creditor to a specified amount,

shall not, unless the relevant secured creditor agrees otherwise, specify the

amount of the reduced principal sum referred to in *paragraph (b)* at an amount less than the value of the security determined in accordance with *section 105*.

(3) A Personal Insolvency Arrangement which includes terms involving—

(*a*) retention by a secured creditor of the security held by that secured creditor, and

(*b*) a reduction of the principal sum due in respect of the secured debt due to that secured creditor to a specified amount,

shall, unless the relevant secured creditor agrees otherwise, also include terms providing that any such reduction of the principal sum is subject to the condition that, subject to *subsections (4)* to *(13)*, where the property the subject of the security is sold or otherwise disposed of for an amount or at a value greater than the value attributed to the security in accordance with *section 105*, the debtor shall pay to the secured creditor an amount additional to the reduced principal sum calculated in accordance with *subsection (4)* or such greater amount as is provided for under the terms of the Personal Insolvency Arrangement.

Section 104 - Principal private residence in Personal Insolvency Arrangement.

Section 104.— (1) In formulating a proposal for a Personal Insolvency Arrangement a personal insolvency practitioner shall, insofar as reasonably practicable, and having regard to the matters referred to in *subsection (2)*, formulate the proposal on terms that will not require the debtor to—

(*a*) dispose of an interest in, or

(*b*) cease to occupy, all or a part of his or her principal private residence and the personal insolvency practitioner shall consider any appropriate alternatives.

(3) Where—

(*a*) the debtor confirms in writing to the personal insolvency practitioner that

the debtor does not wish to remain in occupation of his or her principal private residence, or

(*b*) the personal insolvency practitioner, has, having discussed the issue with the debtor, formed the opinion that, taking account of the matters referred to in *subsection (2)*, the costs of continuing to reside in the debtor's principal private residence are disproportionately large,

the personal insolvency practitioner shall not be required to formulate the proposal for a Personal Insolvency Arrangement on terms that will not require the debtor to cease to occupy his or her principal private residence.

Section 105 - Valuation of security.

Section **105**.— (1) Subject to the provisions of this section the value of security in respect of secured debt for the purposes of this Chapter shall be the market value of the security determined by agreement between the personal insolvency practitioner, the debtor and the relevant secured creditor.

3.2 Application of the law

1. The practical treatment of secured debt starts, from a practitioner's point of view, at section 98. In section 98(1) it is stated that:

> *subject to section 101(2), the PIP shall invite those creditors to make submissions to the personal insolvency practitioner regarding the debts concerned and the manner in which the debts might be dealt with as part of a Personal Insolvency Arrangement and thereafter, the PIP shall (b) consider any submissions made by creditors regarding the debts and the manner in which the debts might be dealt with as part of a Personal Insolvency Arrangement, including—*
>
> *(i) any submission made by a creditor with respect to previous or existing offers of arrangements made by the creditor to or with the debtor, and*

(ii) any submission made by a secured creditor in accordance with section 102.

2. Whilst section 98 is isolated at the start of the insolvency process it is at this point, normally within 14 days of the Protective Certificate being issued, that the creditor submission informs (or should inform) the Personal Insolvency Practitioner on how a creditor would like to proceed and therefore becomes relevant for the treatment of all debts but in particular the secured debt in the context of both the proposal itself, and potentially, the Court's considerations under a section 115A appeal.

3. In reading and applying the Act in sequence, then the next section, section 99 must be read as a section outlining the "warning" to debtors, the Personal Insolvency Practitioner and creditors, of the implications of the realities post Personal Insolvency Arrangement:

   Section 99(2)(c); where the debtor performs all of his or her obligations specified in a Personal Insolvency Arrangement, he or she shall not stand discharged from the secured debts covered by the Personal Insolvency Arrangement except to the extent provided for under the terms of the Personal Insolvency Arrangement.

4. The above section must be read to mean that the treatment of secured debt must be explicitly and carefully detailed in the Personal Insolvency Arrangement, and can only stand discharged to the extent provided in the terms of the Personal Insolvency Arrangement. This does, in the context of the opinion sought, clearly indicate that the secured debt will not be written down without an express provision providing for same.

5. As most of the Personal Insolvency Arrangements coming before the Courts concern a Principal Private Residence, and indeed, every section 115A application, any opinion must consider the underlying thrust of the legislation. The undisputed thrust of the legislation is to keep debtors in their family homes, as provided for in the Short Title to the Act and echoed by the High

Court on numerous occasions to date. Indeed, the Act itself, in Section 104 outlines such a position. Further, sequentially, after dealing with the matter of a discharge from certain portions of secured debt, the Act outlines (Section *99(2)(h)*):

> *A Personal Insolvency Arrangement shall not require that the debtor dispose of his or her interest in the debtor's principal private residence or to cease to occupy such residence unless the provisions of section 104(3) apply.*

6. I am therefore of the opinion that, indisputably, the underlying thrust of the legislation is to keep a debtor in their family home**.**

7. This leaves the Personal Insolvency Practitioner in a position where sequentially under the Act, and in practice, he or she must therefore deal with the secured debt in such a way as to keep a debtor in their Principal Private Residence:

> *99(2)(k) subject to sections 102 to 105, a Personal Insolvency Arrangement shall make provision for the manner in which security held by a secured creditor is to be treated.*

8. The above provision puts a serious onus on the Personal Insolvency Practitioner to carefully and contractually, for the eventual benefit of the debtor, the creditors and the relevant Court, detail the exact terms relating to the treatment of secured debt.

9. When considering how to treat the secured debt, the Personal Insolvency Practitioner is guided, but not limited, by section 100. Section 100 is entitled "*Non-exhaustive list of options as respects payments for inclusion in Personal Insolvency Arrangement*":

> *100(2) The terms of a proposal for a Personal Insolvency Arrangement may include any one or more of the following: (f) in respect of secured debts, subject to sections 102 to 105, an arrangement for the treatment*

of the security and the satisfaction or restructuring of the secured debt.

10. Firstly, the section clearly outlines that a Personal Insolvency Arrangement can treat security in a manner including the restructuring or satisfaction of the secured debt. Again, the Act gives creditors, more particularly secured creditors, a second opportunity to indicate a preference as to how they would like their secured debt treated. This, for all intents and purposes is a second protection and invitation for secured creditors to engage with the personal insolvency process:

> ***102**.— (1) Where a secured creditor has been notified by the personal insolvency practitioner that a protective certificate has been issued in respect of the debtor the secured creditor concerned shall furnish to the personal insolvency practitioner an estimate, made in good faith, of the market value of the security and the creditor concerned may also indicate, a preference as to how, having regard to subsection (3) and sections 103 to 105, that creditor wishes to have the security and secured debt treated under the Personal Insolvency Arrangement.*

11. At this point in the process, both in practice and sequentially under the Act, the Personal Insolvency Practitioner should be in receipt of a valid and complete Proof of Debt including a valuation of the security held by the secured creditor. This will give the Personal Insolvency Practitioner a clear indication of the value of the security and of the quantum of the debt. (For the purposes of this opinion counsel will not consider section 105 of the Act and the agreement of the valuation of security.) Indeed, the Act acknowledges that the value of the security may be less than debt and proceeds to guide the Personal Insolvency Practitioner on how to treat such a position:

> *(3) Subject to sections 103 to 105, the terms of a Personal Insolvency Arrangement may provide for the manner in which the security for a*

secured debt is to be treated which may include:

(a) the sale or any other disposition of the property or asset the subject of the security;

(b) the surrender of the security to the debtor; or

(c) the retention by the secured creditor of the security.

12. For the purposes of this opinion, and in the majority of actual cases, the opinion will proceed on the basis of the retention by the secured creditor of the security. Section 102(6) then guides the Personal Insolvency Practitioner in how to treat such by including a suggestive list of possible treatments. Indeed, this section, rather than merely being seen as a suggestive list could also be considered to provide the rules on implementation if one of the suggested options is chosen:

(6) Without prejudice to the generality of section 100 or subsections (1) to (3) and subject to sections 103 to 105, a Personal Insolvency Arrangement may include one or more of the following terms in relation to the secured debt:

(a) that the debtor pay interest and only part of the capital amount of the secured debt to the secured creditor for a specified period of time which shall not exceed the duration of the Personal Insolvency Arrangement;

13. In dealing with each subsection individually, subsection (a) outlines that a period of short term forbearance may be included in treating or restructuring the secured debt. It is of particular note that the Act expressly provides that forbearance in the form of interest and part capital may not outlive the term of the Personal Insolvency Arrangement. This, as will become evident, links directly with the requirement to return a debtor to solvency and deliver a sustainable mortgage at the end of a Personal Insolvency Arrangement. From

a banking perspective, such a restructure can be considered a deferral of part of the secured debt payment. Indeed, technically, a split mortgage which includes a warehoused portion could be considered an interest and part capital restructure.

> *(b) that the debtor make interest-only payments on the secured debt for a specified period of time which shall not exceed the duration of the Personal Insolvency Arrangement;*

14. Subsection (b) outlines that a period of short term forbearance, in the form of interest only payments, may be included. It is of particular note, again, that the Act expressly provides that this short term forbearance may not outlive the term of the Personal Insolvency Arrangement. This, as will become evident, links directly with the requirement to return a debtor to solvency and deliver a sustainable mortgage at the end of a Personal Insolvency Arrangement.

> *(c) that the period over which the secured debt was to be paid or the time or times at which the secured debt was to be repaid be extended by a specified period of time;*

15. Subsection (c) relates to a term extension, being a recognized treatment under the Central Bank Code of Conduct on Mortgage Arrears and Mortgage Arrears Resolution Process. In many cases, this will be a treatment employed before other restructure treatments are considered. On deeper reading, the provision does indicate that the “time or times” at which the secured debt was to be repaid may be extended. This is particularly relevant to the second question counsel is asked to address, being the warehousing of part of a mortgage debt. Counsel has considered this matter elsewhere. Further, the use of the term “time or times” brings the treatment of a secured debt judgment mortgage into the consideration of counsel. As a judgment mortgage will not be in the same original form as an annuity mortgage this

provision gives scope for a Personal Insolvency Practitioner to deal with same.

> *(d) that the secured debt payments due to be made by the debtor be deferred for a specified period of time which shall not exceed the duration of the Personal Insolvency Arrangement;*

16. The above provision causes both counsel and Querist issue. I am of the opinion that subsection (d) can be read in two ways, firstly, that the secured debt payment due on a monthly basis be deferred for a period of time. As 106(a) relates to interest and part capital, 106(b) relates to interest only, 106(c) relates to extending the term to reduce the secured debt payment on a monthly basis, then, sequentially, in my opinion section 106(d) provides for a complete moratorium on a short term basis. As this is also a short term forbearance treatment it is limited to the term of the Personal Insolvency Arrangement. The reasoning behind such a short term moratorium may include allowing the debtor a period of time to deal with life events, or to allow payments to the Personal Insolvency Practitioner and/or unsecured creditors for the greater good of the Personal Insolvency Arrangement and/or the secured creditor in the longer term.

17. The second reading of the deferral of secured debt payments is that a warehoused portion of a mortgage can not be deferred beyond the term of the Personal Insolvency Arrangement. It is suggested therefore that a warehoused portion of a mortgage is a deferral, whether simpliciter or indeed in the form of a deferral under the guise of an interest and part capital payment. This may be correct or may be an unintended consequence. Fundamentally, as credit is given to mean the time which a creditor allows his debtor to pay a debt then credit includes a deferred payment or any other form of financial accommodation as per the Consumer Credit Act 1995 then the second reading of deferred debt payments begins to take shape. Extending from such an understanding, a credit facility includes every kind of financial accommodation including a deferred payment arrangement being a financial accommodation giving rise to a payment or repayment obligation

then a warehoused mortgage must fall into such a definition. A warehoused portion of a mortgage is either, as already outlined, the payment of interest and part capital with the other portion of the capital being separated and warehoused or simply the deferral of a payment of a portion of the capital to a specified time or event.

18. The given understanding of split mortgages, taking the Keane Report from 2011 (Inter-Departmental Mortgage Arrears Working Group – 30th September 2011) onwards is that a portion of the main mortgage is parked for a period but subject to an annual or periodic review to that the deferred split amount can be reintroduced to the base loan. As is outlined in the Keane Report, and regularly criticised by debtor advocates, a split mortgage, and the deferred amount cause the mortgage holder constant uncertainty, constant issues with solvency, and leaves a situation that when the warehoused portion of a mortgage becomes due it could cause the mortgage holder to have repossessed, vacate, or sell their Principal Private Residence. This utterly conflicts with the Personal Insolvency Act, in particular, but to take but three specific instances, the long title to the Act, and then particularly section 54 and section 104.

19. Whilst counsel outlines the conflict of a split warehoused mortgage and the Personal Insolvency Act in May 2016, the Keane Report in September 2011 (pre the 2012 Act) equally foresaw such a position. To quote:

> "The early reform of personal insolvency legislation will be a central element in the resolution of the mortgage arrears problem by providing a catalyst for change in the relationship between the mortgage lender and the distressed mortgage holder. Rapid progress will be necessary in this area to provide for certainty on both the judicial and non-judicial mechanisms and to allow settlements to be reached. Such mechanisms need to be carefully calibrated to ensure that there is no suggestion that borrowers can easily leave outstanding debts behind them."

Further:

> "The current legislative framework for personal insolvency does not offer a meaningful resolution to any party – mortgage lender or mortgage holder. Given the full recourse nature of mortgages there is no current insolvency option for many mortgage holders who are in difficult or unsustainable mortgages – they could face permanent bankruptcy."

20. On the back of the Keane Report the Personal Insolvency Act was introduced. If now, with the benefit of section 115A appeals, and the powers of the Act as a whole, unsustainable split mortgages are not treated, noting that a Personal Insolvency Arrangement can only be availed of once, then the law is not being used to its full effect. To give effect to the law, warehoused debt must be considered a deferred debt payment which can only be considered a short term solution as anything beyond the term of the Personal Insolvency Arrangement would mean that there is no meaningful resolution for any party, mortgage lender or mortgage holder.

21. This was further considered in the Remarks prepared by Governor Patrick Honohan for the FMC2 Conference, Dublin on the 22nd and 23rd May 2013 in a paper entitled "Sustainable mortgage modification".

22. In light of the above, the Act therefore must be interpreted in such a way as to achieve a logical purpose. In Boyne v Dublin Bus/Bus Atha Cliath, Gilligan J noted the courts' preference for interpretations which give effect to an enactment's purpose:

> *"Indeed, in any question of statutory interpretation the court is bound to have in mind the purpose of a statutory rule or the mischief at which it is directed, insofar as such purpose or mischief can be ascertained. That is not to say, of course, that the court can simply give effect to that purpose, but where the court has to make a judgement about the*

proper meaning of a statute it is likely to want to consider whether it can by the process of interpretation give effect to its purpose or the mischief to which the statute is directed".

23. In the text Dodd, "Statutory Interpretation in Ireland", it is noted that:

"Where a proposition or interpretation is inconsistent with logic, it may be rejected by the courts for that reason."

Also, Dodd states:

"As between an interpretation which runs counter to or beyond the purpose of an enactment and one which is in keeping with the purpose of an Act, the latter will be presumed to be the one intended by the legislature. One can go further and say as between meanings that promote the purpose, the one that best promotes the purpose one that is presumed to be intended by the legislature".

24. In KSK Enterprises Ltd v An Bord Pleanála, the Court rejected an argument regarding a proposed interpretation of Order 84 of the Rules of the Superior Courts when Finlay J. stated:

"There is neither logic nor reason in such an interpretation".

Consequently, where two or more interpretations arise a logical interpretation will be accepted over an illogical one. As stated by Dodd:

"It is presumed that the legislature intends common sense to be used in construing an enactment and that where the language of a provision allows two or more meanings, the meaning which aligns with common sense is to be preferred".

25. In Lawlor v Mr Justice Flood, in the High Court, Kearns J expressly adopted the common sense construction rule and referred to the following passage in Bennion – Statutory Interpretation:

> *"It is a rule of law… that when considering, in relation to the facts of the instant case, which of the opposing constructions of the enactment would give effect to the legislative intention, the Court should presume that the legislature intended common sense to be used in construing the enactment".*

26. In following on from the Keane Report, the Code of Conduct on Mortgage Arrears as published by the Central Bank of Ireland defines a split mortgage as:

> *Split mortgage: means where a lender agrees to split a borrower's mortgage loan into an affordable mortgage loan, which the borrower continues to repay, and a remaining balance, which is set aside or "warehoused" to a later date.*

27. The express definition above therefore outlines that the remaining balance (a secured debt payment) is set aside, (deferred) to a later date. This must then be read in the context of section 106(2)(d);

> *(d) that the secured debt payments (mortgage) due to be made by the debtor be deferred (warehoused) for a specified period of time (usually to the end of the term) which shall not exceed the duration of the Personal Insolvency Arrangement;*

28. In further consideration of the issue of sustainability, which is a paramount concern for Personal Insolvency Practitioners, the Central Bank of Ireland Internal Guideline Sustainable Mortgage Arrears Solutions updated as of 13th June 2014 are of relevance.

29. It is outlined therein that:

> *Lenders need to satisfy themselves that the solution will be effective for the full remaining life of the mortgage and take account not just of capacity to pay interest for an interim period but also to service the (revised) mortgage contract on a lasting basis. A sustainable solution must be likely to enable the customer to meet the original or, as appropriate, the amended terms of the mortgage over the full remaining life of the mortgage, including repayment of the original or an agreed revised principal sum where offered. (This is to be understood to include the specific treatment of the warehoused portion of the split mortgage as outlined above). The revised mortgage servicing terms may be conditional on borrower's income; Lenders therefore need to be able to satisfy themselves – and demonstrate to the Central Bank – that any temporary term arrangement is part of a sustainable solution because the borrower will have a sufficiently improved capacity to service the debt at the end of the temporary arrangement.*

30. The above paragraph clearly captures the concerns raised and the rules provided for in section 102(6) and the Act as a whole. Further:

> *The Central Bank is concerned that lenders persist in relying on temporary forbearance measures even where a demonstrable ability of the borrower to resume the original contractual repayments at the conclusion of this forbearance term is unlikely. Therefore, where the borrower is unable to service fully the mortgage payments but where there is some reasonable prospect of the borrower's circumstances improving over a longer term, a split-mortgage solution may be considered as offering a sustainable solution. In the case of PDH loans, a split mortgage can allow the borrower the opportunity to remain in their home, while enabling the lender to recover an additional portion of the loan should the borrower's circumstances improve.*

31. A similar sustainability concern must be raised by a Personal Insolvency Practitioner in light of his professional status, duty of care, and duty to creditors and the debtor, and in light of his or her advices and Personal Insolvency Practitioner statements given to creditors and the Court. However, whilst the Central Bank may have had concerns regarding lenders persisting in relying on split mortgages there is no similar concern for Personal Insolvency Practitioners as the Personal Insolvency Act gives the Personal Insolvency Practitioner the tools to ensure sustainability, certainly and solvency for debtors and creditors alike.

32. It is also outlined that;

> *Sustainability of a split mortgage will be assessed by the Central Bank inter alia with regard both to the affordability of the unwarehoused debt payment schedule and with regard to the treatment of the warehoused loan at maturity.*

33. The above, again, in my opinion clearly recognizes the deferred nature of the split mortgage treatment, and the risks associated thereto. These concerns, in my view, can be properly addressed with the proper construction of a Personal Insolvency Arrangement.

34. Indeed, the Central Bank recognized the reality of a Personal Insolvency Arrangement when noting:

> *In order to reduce the incentive for a borrower to reject a particular offer in the hope of receiving something better through the PIA process, lenders will want to consider how the schedule offered compares (i.e. in terms of monthly disposal income post debt repayment).*

35. Unfortunately, as many Personal Insolvency Arrangements have to date have not considered the treatment of a split mortgage on maturity, as well as perhaps conflicting with section 102(6) a number of issues may arise.

> *A split mortgage solution which does not ensure the sustainable treatment of the warehoused part of the mortgage, as outlined above or with other measures of equivalent effect, will not be counted as a sustainable solution in the context of the targets.*

36. Whilst section 102(6)(d), if read in the context of warehousing being incompatible with law, may cause secured mortgage lenders great concern, a creative use of section 102(6)(d) coupled with a section 98 submission could actually be to the ultimate benefit, in monetary terms, of the secured lender. Counsel has considered this matter in a separate opinion. It is expressly noted that creative legal and financial thinking can ensure a secured creditor can manage this situation and return a substantial return on a mortgage debt.

37. Section 106(g) starts to reflect the reality of Personal Insolvency Practitioner practice, being the need to restructure and reduce secured debt in order to provide a sustainable mortgage and return to solvency, whilst achieving a greater return for creditors than bankruptcy. Section 106(g) provides that where such a reduction is made, a clawback provision must be included in the Personal Insolvency Arrangement. Such a provision prevents a situation where a debtor would make a profit at the expense of a creditor who was forced to take a reduction of their debt previously.

> *(g) that the principal sum due on the secured debt be reduced but subject to a condition that where the property the subject of the security is subsequently sold for an amount greater than the value attributed to that property for the purposes of the Personal Insolvency Arrangement, the secured creditor's security will continue to cover such part of the difference between the attributed value and the amount for which the property is sold as is specified in the terms of the Personal Insolvency*

Arrangement;

38. Section 106(i) further reflects the reality of Personal Insolvency Practitioner practice, being the need to restructure and reduce secured debt in order to provide a sustainable mortgage and return to solvency, whilst achieving a greater return for creditors than bankruptcy.

> *(i) that the principal sum due in respect of the secured debt be reduced to a specified amount.*

39. Section 106(11) moves, in practical terms, from section 106(g) and (i) and details how, if such a reduction to the principal sum is required, to how the reduced amount shall (must) be treated, and details that same must be treated as an unsecured debt and rank and abate equally with other unsecured debts, and be discharged in like terms. This, to address the question posed to counsel is contingent on the Personal Insolvency Practitioner deeming such a reduction necessary and drafting a proposal as such. The reduction of the principal secured debt, and/or the treatment of negative equity as an unsecured debt does not happen as of course.

> *(11) Without prejudice to section 103, where a Personal Insolvency Arrangement includes terms providing for a reduction of the amount of debt (including principal, interest and arrears) secured by the security as of the date of the issue of the protective certificate to a specified amount, the terms of the Arrangement shall, unless the relevant secured creditor agrees otherwise, also include a term providing that the amount of such reduction shall:*
>
> *(a) rank equally with, and abate in equal proportion to, the unsecured debts covered by the Arrangement; and*
>
> *(b) be discharged with those unsecured debts on completion of the obligations specified in the Arrangement.*

40. In circumstances, where I reiterate that practice often requires a reduction of secured debt, the Act has detailed in section 102 the protections for secured creditors in Personal Insolvency Arrangement. Indeed, it is my opinion that such a section expressed contemplated and foresaw the reality of how Personal Insolvency Practitioner practice, negative equity, and mortgage arrears were to be addressed.

> *102(2) A Personal Insolvency Arrangement which includes terms providing for—*
>
> *(a) retention by a secured creditor of the security held by that secured creditor, and*
>
> *(b) a reduction of the principal sum due in respect of the secured debt due to that secured creditor to a specified amount,*
>
> *shall not, unless the relevant secured creditor agrees otherwise, specify the amount of the reduced principal sum referred to in paragraph (b) at an amount less than the value of the security determined in accordance with section 105.*

41. If the principal sum is reduced, it is expressly provided that the reduction can not put the principal sum below the value of the security without the consent of the secured creditor. Again, as outlined previously, the valuation sought at section 98 and section 102 now become extremely relevant. Indeed, not to be considered herein, but section 105 confidently protects and assures any valuation to be correct. Section 102(2)(b) therefore opens a variety of permutations where the principal sum could be reduced to any sum, so long as same is above the value of the security. However, any such reduction, and the sum arrived at, must be justified and calculated with respect to both the debtor and the treatment of other creditors, most particularly any prejudice same may impose on unsecured creditors. I will return to this matter sequentially.

(3) A Personal Insolvency Arrangement which includes terms involving—

(a) retention by a secured creditor of the security held by that secured creditor, and

(b) a reduction of the principal sum due in respect of the secured debt due to that secured creditor to a specified amount,

shall, unless the relevant secured creditor agrees otherwise, also include terms providing that any such reduction of the principal sum is subject to the condition that, subject to subsections (4) to (13), where the property the subject of the security is sold or otherwise disposed of for an amount or at a value greater than the value attributed to the security in accordance with section 105, the debtor shall pay to the secured creditor an amount additional to the reduced principal sum calculated in accordance with subsection (4) or such greater amount as is provided for under the terms of the Personal Insolvency Arrangement.

42. As is provided in section 102(6)(g), if there is a reduction in the principal sum then the clawback provisions apply. To bring the treatment of secured debt generally to a conclusion, it can therefore be said that a secured debt can be reduced, but where reduced it can not be reduced below the value of the security, and where it is reduced there is a clawback.

43. As previously outlined, the thrust of the Act is to deal with Principal Private Residence debt and section 104 expressly provides for Principal Private Residence in Personal Insolvency Arrangement.

104.— (1) In formulating a proposal for a Personal Insolvency Arrangement a personal insolvency practitioner shall, insofar as reasonably practicable, and having regard to the matters referred to in subsection (2), formulate the proposal on terms that will not require the debtor to—

(a) dispose of an interest in, or

(b) cease to occupy, all or a part of his or her principal private residence and the personal insolvency practitioner shall consider any appropriate alternatives.

44. It is therefore clear, in my opinion, that the Personal Insolvency Practitioner can invoke the powers of 102 to achieve the aim as outlined in section 104. With the aim of the Act to allow Debtors remain in their Principal Private Residence a reduction of the principal amount due to the secured creditor is often necessary. However, to curtail such a position, the Personal Insolvency Practitioner is obligated, both at the start and at the end of the insolvency process to consider the alternatives and in turn consider the interests of creditors, both by obligation under the Act and by virtue of the submissions made by creditors.

45. In giving his or her initial advices, the Personal Insolvency Practitioner is obligated to have regard to a number of matters as set out in section 52.

52(3) In advising the debtor under subsection (1)(c) of the appropriateness of entering into a Personal Insolvency Arrangement or a Debt Settlement Arrangement, the personal insolvency practitioner shall have regard to—

(a) the value of the debtor's unsecured debts as compared to the value of the debtor's secured debts (if any),

(b) if applicable, whether the debtor has communicated with his or her secured creditors for the purpose of seeking to renegotiate or restructure the secured debts,

(c) whether the debtor has co-operated in good faith with his or her creditors who are secured creditors as respects the debtor's principal private residence in connection with any process relating to mortgage arrears operated by the secured creditors concerned which has been

approved or required by the Central Bank of Ireland and which relates to the secured debt concerned,

(d) whether any of the debtor's secured creditors have indicated to the debtor or the personal insolvency practitioner a willingness to vary the terms of the secured debt to facilitate the operation of a Debt Settlement Arrangement in respect of the debtor's unsecured debts (including, without limitation, any variation of the terms of the secured debt that would reduce the amounts payable by the debtor in respect of the secured debt for the duration of the Debt Settlement Arrangement),

46. Of particular note are sections 52(3)(b) which relates to previous negotiations or restructuring, and 52(3)(c) being the debtor's engagement with any process relating to mortgage arrears operated by the secured creditors concerned which has been approved or required by the Central Bank of Ireland. This provision is of note in that it clearly recognizes the reality of there being such provisions under the Mortgage Arrears Resolution Process. This is of relevance to the second question posed to counsel and of relevance to the section 115A appeals process. Further, 52(3)(d) is of note in that it suggests that a variation of secured debt terms may be appropriate to facilitate a Debt Settlement Arrangement.

47. In following the Personal Insolvency Practitioners initial advices to their natural conclusion, section 54(c) and (d) are of relevance.

54(c) having considered the Prescribed Financial Statement completed by the debtor, there is no likelihood of the debtor becoming solvent within the period of 5 years commencing on the date on which the statement is made;

(d) having regard to the debtor's circumstances as set out in the Prescribed Financial Statement, it is appropriate for the debtor to make a proposal for a Debt Settlement Arrangement as there is a reasonable prospect that the debtor entering into such an arrangement would facilitate the debtor becoming solvent within a period of not more than

5 years or, as the case may be, it is appropriate for the debtor to make a proposal for a Personal Insolvency Arrangement as there is a reasonable prospect that the debtor entering into such an arrangement would facilitate the debtor becoming solvent within a period of not more than 5 years.

4. Other Matters Arising

There are no other matters arising.

5. Conclusion

When one considers the aims and objectives of the Act as a whole and as detailed in the Short Title:

An Act to amend the law relating to insolvency, to amend the Bankruptcy Act 1988, to provide for the establishment and functions of a body to be known as the Insolvency Service of Ireland, and, in particular, in the interests of the common good (including the stability of the financial system in the state) and having regard to the following objectives -

(a) The need to ameliorate the difficulties experienced by debtors in discharging their indebtedness due to insolvency and thereby lessen the adverse consequences for economic activity in the state,

(b) The need to enable creditors to recover debts due to them by insolvent debtors to the extent that the means of those debtors reasonably permits, in an orderly and rational manner, and

(c) The need to enable insolvent debtors to resolve their indebtedness (including by determining that debts stand discharged in certain circumstances) in an orderly and rational manner without recourse to bankruptcy, and thereby facilitate the active participation of such persons in economic activity in the state

one can see that the aims are threefold; return debtors to solvency, keep debtors in their Principal Private Residence, and return a greater dividend to creditors than they would achieve in bankruptcy. In such a scenario negative equity writedown is permitted and, in many cases, needed to satisfy such aims. In returning a debtor to solvency one can not be said to be truly solvent if there is a liability outstanding at a deferred point in the future that can not be satisfied within the means of the debtor whilst respecting section 104 of the Act. Indeed, as the Act expressly has the objective of a return to economic activity, the construction of a split mortgage, usually with an annual review, flies in the face of such an objective. In this regard, the second question posed by Querist becomes relevant. Counsel can not see how a warehoused debt is needed in the context of a Personal Insolvency Arrangement. The mechanics of a Personal Insolvency Arrangement allow the principal sum be reduced to such an amount that warehousing does not become relevant. This is further emphasized by the application of section 99(2) in the last Personal Insolvency Practitioner statement given under 107(1)(c).

Nothing further occurs.

Keith Farry B.L.