

## LAW REFORM COMMISSION CONFERENCE

### CONSUMER DEBT IN IRISH SOCIETY

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#### Introduction

In the early 1990s, when I began working in the Free Legal Advice Centres, consumer credit as we now know it was fairly thin on the ground particularly for those on low incomes and so as a result was consumer debt. Very few had heard of money advice except perhaps the kind provided by an accountant in return for a fee. I well recall attending a workshop on debt at the then premises of the Irish National Organisation of the Unemployed (INOU) in Fleet Street, where a small group of enthusiastic amateurs gathered to listen to a Community Welfare Officer talk about indebtedness and how the danger signs might be identified. It had not been that long since the publication in 1988 of 'Moneylending and Low Income families' (Mary Daly with Jim Walsh) by the Combat Poverty Agency, a pioneering piece of work that brought to the attention of a wider public the existence and high costs of moneylending and the risks associated with it, and the lack of access to credit options for those on low incomes or reliant on social welfare payments. It is generally accepted that this report was the catalyst for the setting up of the initial money advice pilot projects in 1992.

Around this time, FLAC was asked to take part in an EC project to identify existing legislation and case law on consumer credit across a number of EC countries. In those days, in an impoverished NGO's like ourselves, people used to line up to take turns on the computer. When it became apparent that a computer might be acquired as part of this project, it was decided to go for it. The next difficulty was to decide who should be assigned responsibility for tackling the work. FLAC had produced a leaflet on Moneylending and the Law in the 1980's but there was no queue of volunteers. One of my first tasks was to attend a conference on consumer debt in Birmingham organised by the Birmingham Settlement in the UK and the Hamburg-based IFF, definitely an occasion to follow a maxim my late father was very keen on – 'Better to keep your mouth shut and be thought a fool than to open your mouth and prove it'. Thereafter, for nearly a year, I researched the limited joys of consumer credit legislation in Ireland,

unearthing such pearls as the Moneylenders Acts 1900 and 1933 and the Hire Purchase Act 1946.

The necessity to transpose the EU consumer credit directive into law followed soon after. By then some of the small group of enthusiastic amateurs from the debt workshop had morphed into the Credit and Debt Policy group. Amongst other things, this group held a seminar on the Consumer Credit Bill and met with then Director of Consumer Affairs, Willie Fagan and then junior Minister for Enterprise, Trade and Employment, Pat Rabbitte TD on the transposition of the directive. At the meeting in Consumer Affairs, Willie Fagan came up with the memorable alternative understanding of the term APR (or Annual Percentage Rate of Charge) then about to be introduced as a common method of calculating the cost of credit across Europe. To some, he said, APR meant 'Any price is right'. In retrospect, in view of the credit fest that followed, how prophetic he was.

When the training service in the then National Social Service Board (NSSB), now Citizens Information Board, started to offer training to MABS money advisors, someone had to grapple with explaining the consumer credit legislation. Because the only other people in Ireland who appeared to be remotely interested in this subject were bankers and commercial lawyers generally intent on keeping the consumer in his or her box, I got the gig. It was easy to be an 'expert' back then; you just had to have read the Act a number of times. I remember pitching up to the Hotel Minella in Clonmel to deliver consumer credit training to money advisors. I had about 30 acetate slides prepared in differently coloured markers for the occasion, the height of sophistication! Many of the advisors present that day are still in MABS though I don't know how they survived the training. Notwithstanding, the relationship between FLAC and MABS survived due in no small part to the visionary efforts of former national MABS Co-ordinator, Liam Edwards and latterly the staff of MABSndI and money advisors countrywide. We continue to provide training and technical support to MABS to this day.

### **The FLAC reports**

Principally through the course of its work with MABS but also through our own network of voluntary legal advice centres, FLAC became aware in the course of the 1990's of deficiencies in the debt enforcement system that adversely impacted upon MABS clients and people on limited incomes generally. Primarily in response to a Fine Gael Private Members Bill to amend the enforcement of court

orders legislation, then Minister for Justice, Equality and Law Reform, John O Donoghue, TD announced in May 1998 that the government would be introducing an its own amending Bill. This would replace imprisonment for non-payment of fines or civil debt with an Attachment of Earnings system. To prepare for this, I carried out research into how attachment worked in other jurisdictions. This Bill however never materialised, and indeed it is an indictment of successive administrations that an instalment system for the payment of fines that might substantially reduce imprisonments is still pending. A third Fines Bill is still before the Houses of the Oireachtas, the previous two having lapsed with general elections.

The result of this research was the report entitled 'An End based on Means', published in May 2003. This work started out as an analysis of comparative attachment of earnings systems in the UK, Europe and the US but was broadened to also look at the developing area of debt settlement or consumer insolvency as well as a detailed analysis of the Instalment Order process that gave rise to imprisonments in the first place. The final section in that report called on the State to set up an expert group to review the debt enforcement system and proposed a number of recommendations as an agenda for reform.

Time does not permit going into these in any detail but a PDF of this report is available on our website at [www.flac.ie](http://www.flac.ie). In summary, we proposed that no decisions should be made on the payment of judgment debts without details of the debtor's financial circumstances, taking all debts into account. We suggested that debt enforcement matters be dealt with in private, as processing cases in open court constituted a substantial deterrent to the debtor's participation, leading to unrealistic and unsustainable orders. We also argued that an Enforcement Office might be established to ensure the appropriate and effective use of debt enforcement mechanisms. The report also called for an end to imprisonment in debt cases, simplification of legal documentation and greater access to legal assistance for those in debt, a comprehensive credit register and the regulation of debt collection.

We proposed that should attachment of earnings legislation be introduced to replace the imprisonment option in debt cases, it must incorporate substantial protections to protect the living standards and employment situation of the debtor and allow for consolidated attachment, i.e. one attachment to cover a multiple debt situation. Finally, in light of the dramatic increases in the provision of consumer credit that we documented at the time which subsequently mushroomed beyond recognition, we

proposed the adoption of debt settlement legislation to cope with cases of chronic over-indebtedness. Such legislation would promote voluntary agreements to be backed by the potential imposition of a settlement by an enforcement authority. The key principle of a fresh start and write-off of unsecured debt would apply, where the debtor in good faith adhered to a repayment programme over a defined period of time.

Despite solid indications from creditor groups, in particular the Irish Banking Federation (IBF), that the current system was not working from a creditor perspective either and that there was nothing in the report that they substantially took issue with, none of these proposed reforms were ever implemented and no review body was ever established. In the course of 2006, FLAC decided to initiate a further interview-based study to focus on largely the same territory, using MABS clients as a research source. On this occasion, the emphasis was on the experience of the debtor in the legal process, particularly the Instalment Order procedure. We wanted to assess the debtor's understanding of legal documentation and procedures, at what stage people sought assistance and were aware of assistance to help with their financial problems, the reasons for non-attendance at court hearings and the experience of court hearings for those who did attend. Ultimately, five of the 38 people interviewed in this study served sentences in Irish prisons due to non-payment of Instalment Orders, varying from two weeks to the maximum sentence of three months in one case. All were deeply traumatised by their experience.

This report was published in July of this year and is entitled 'To No One's Credit'. Again, the findings and recommendations of this report are lengthy. Hard copies are available outside for those who are interested. In summary, the respondents in the study generally confirmed the anecdotal evidence already available. There was a pronounced lack of understanding of legal documentation and procedures and in many cases a lack of awareness of where help could be obtained until it is was too late in the process. Participation at hearings to determine capacity to pay was very limited mainly because of the hearing in public element. Indeed, we wrote to the Courts Service during the course of this study looking for figures on attendance at such hearings. In their reply, they confirmed that such statistics were not available but they estimated that only one in five persons attended Instalment Order and Committal Order hearings. Non-compliance with such orders was therefore practically inevitable. For those who did attend without legal representation, there was little or no guidance available to present their case and the opportunity to present the relevant financial information was missed in some

cases because of this.

Further detailed recommendations for comprehensive reform of the debt enforcement system are in turn made in this report. These include changes that would facilitate offers of affordable repayments at earliest possible stage and detailed changes to the existing Instalment Order system that, it is argued, would immediately lead to effective improvements. Recommendations in relation to improved access to support services and clear information for debtors are also made. This report also calls for improved information gathering on debt-related proceedings and research to be carried out on the long term costs of over-indebtedness, as well as an end to imprisonment in debt cases. Finally, FLAC again calls for an alternative debt settlement approach to resolving problems of over-indebtedness and proposes a model Debt Rescheduling and Mediation Service.

### **The Changed Environment**

Thus, while much has happened in what is now nearly two decades, some things have not changed at all. While credit was extended and availed of on an increasingly widespread basis with seemingly little regard for the consequences, the legal system in relation to debt recovery remained steadfastly unchanged. Sometime and let us hope that it will be sooner rather than later, when Ireland as a country starts to emerge from the fog of financial and economic chaos that has befallen us, we should have a national enquiry about how we got here. What, for example, possesses a couple on a relatively modest combined income to indulge in daisy chain investment mortgage borrowing to build up a property portfolio on the backs of tenants paying exorbitant rents? Worse still, what possesses a credit institution to abandon all prudential sense to facilitate this display of greed at the height of a property boom? Is it that some post-colonial inferiority complex is responsible for the gorging on credit that some (though by no means all as some of the culprits are wont to suggest) indulged in, cheered on by government and credit institutions laughing all the way to their shareholder's meetings before the big bust came? Together with the lack of political vision that allowed this to happen with the minimum of regulatory safeguards and the failure to prepare for a downturn that was inevitable, the lack of maturity and the inability to think in anything but the short term is profoundly disturbing.

What was it that persuaded normally sane and intelligent people to think that Ireland could buck all

known economic trends and sustain a perpetual boom? In turn, why did the State in the midst of an acknowledged consumer credit explosion persistently refuse to modernise the debt enforcement infrastructure, so that, for example, 276 persons were imprisoned (some of them twice) relating to non-payment of civil debt court orders in 2008, while the only insolvency option continued to be the little used Bankruptcy Act 1988, its punitive and inaccessible procedure more reminiscent of a Dickensian age. When practically every State across the western world has responded sooner or later to the market's reliance on consumer credit as an instrument of economic growth by putting in place personal insolvency mechanisms, why does Ireland have to be different? Comparative consumer bankruptcy is now an international legal discipline. See for example, 'Consumer Bankruptcy in Global Perspective' (2003) edited by amongst others one of this afternoon's speakers, Professor Iain Ramsey of the University of Kent.

### **The road ahead**

When responding to a request for road directions, it is often jokingly said 'but I wouldn't start from here if I were you'. Unfortunately however, we are where we are and can only begin from here. How do we now put in place, in the midst of a financial thunderstorm, the necessary procedures to cope with the personal debt crisis that is being endured by many consumers and their families? In the Law Reform Commission's Consultation Paper on Personal Debt Management and Debt Enforcement lie many of the potential answers. It is a lengthy but meticulously researched and written piece that is proof positive that the issues of debt and of credit have finally moved centre stage in Ireland.

FLAC is delighted to see much of our research and proposals in this area generously cited in this work and a number of the recommendations we have made for reform of the law in this area are expressly approved. In turn, there are few domestic developments, reports and submissions of note that have gone unnoticed in this paper. In turn, the number of references to international research and developments is broad and wide ranging. The Paper also does due justice to another catalyst for change, what is now known simply as 'the McCann case', a legal challenge brought by our colleagues in the Northside Community Law Centre (through a MABS service). This case not only forced the repeal of outdated legislation but also helped to bring to a wider public consciousness how antiquated these laws really are. Following the judgment of Laffoy.J in the High Court in June of this year, the State was

compelled to introduce the Enforcement of Court Orders (Amendment) Act 2009. This legislation now clearly places the onus of proof on the creditor to show beyond reasonable doubt that a debtor is guilty of wilful refusal or culpable neglect in failing to meet the terms of an Instalment Order to pay a judgment. It also ensures that legal aid to a debtor to defend his/her position will be available and that the debtor will be present in court, in effect a reversal of the previous unconstitutional position. Let us hope that this will reduce the number of imprisonments related to non-payment of civil debt to zero or close to zero.

### **The Consultation Paper itself**

A detailed summary of the existing debt enforcement mechanisms in the Irish legal system and the Commission's detailed proposals for fundamental reform will be provided by Patricia Rickard-Clarke later this morning and I do not wish to encroach upon that terrain. However, one of the many impressive features of the Paper is that it takes a principles based approach to reform which informs the specific proposals for change that follow.

The Commission suggests that the law on debt enforcement should be drafted to take account of the different circumstances in which indebtedness arises and therefore should focus on distinguishing between 'can't pay' and 'won't pay' situations. The success of this approach depends on access to accurate information on the debtor's financial circumstances and the role of debt counselling and in the Irish context, the role of MABS is critical here.

The paper is clear that a creditor has a constitutional right to protect his/her property including the benefit of contracts so that effective mechanisms for enforcing court judgments must be in place. However, it concludes that legal proceedings should be a last resort to be used when other measures have failed or can be shown to be inappropriate. Debtors too have important rights including constitutional rights to liberty, privacy and fair procedures, as articulated by the High Court in the McCann case. A critical third interest is the public interest. This may (and in our view does) require the prevention and alleviation of over-indebtedness in society generally.

To reconcile these competing interests, the Commission recommends a 'proportionate enforcement'

approach. This means that debt enforcement mechanisms must be balanced; they must achieve a legitimate goal, must be the least restrictive on the rights of the debtor and must have a proportionate impact. An examination of current debt enforcement legislation, however, reveals that it was not designed with a credit society in mind. The view of debtors as delinquents refusing to pay is outdated, there is a clear failure to address multiple debt situations, procedures are inefficient, debtor participation is low and there is a general lack of information on the debtor's finances and assets. The Commission thus concludes that the current law must be updated and streamlined.

The Commission also endorses the six building block approach on legal solutions to indebtedness adopted by the European Commission in its 2008 report – 'Towards a Common Operational definition of Over-Indebtedness'. This essentially involves three preventative steps – ensuring responsible borrowing, responsible lending and responsible arrears management and three remedial steps – putting in place debt counselling, personal insolvency options and holistic debt enforcement procedures. This will (not may) involve 'the introduction of new court procedures and the establishment through legislation of a debt settlement scheme to operate as a non-judicial alternative and complement to a reform of bankruptcy law'. The Commission suggests that the law should favour the non-judicial option and that a centralised Debt Enforcement Office would monitor enforcement, ensure that it is appropriate and proportionate and have a decision making role in means assessment and debt settlement. I have little doubt that Patricia will provide further detail of the Commission's recommendations in this regard in due course.

### **National Strategy for dealing with Consumer Over-indebtedness**

With the publication of the Consultation paper, we fervently hope that the tide has definitively turned in terms of a fundamental review of debt enforcement and bankruptcy law in Ireland. However, it is also clear that the problems of consumer debt generally are now beginning to have serious side effects across Irish society. Reform of the legal system, although a hugely critical part of the solution may not be enough on its own.

Earlier this year, the now late lamented Combat Poverty Agency published a paper entitled 'A Policy Framework for addressing Over-Indebtedness' authored by Dr Stuart Stamp which called for a high level

government committee to be established to implement a national strategy to cope with the current debt crisis. With each week that passes, this call becomes more and more pressing and FLAC would like to reiterate it today. Later this week, the 2009 Consumer Financial Vulnerability Study produced by the Personal Finance Research Centre at the University of Bristol with the support of Genworth Financial will be published. Last year's index showed a dramatic increase in the vulnerability of consumers in Ireland and it is likely that the position in 2009 will have further deteriorated. Just this Monday, Dearbhail McDonald of the Irish Independent suggested that some 20,000 personal credit default cases have come before Irish courts in the first nine months of 2009 involving debts of €395 million. Applications for and orders of repossession doubled in 2008 over 2007 (admittedly from a low base) and have further increased in 2009. This comes at a time when it is clear that there is little appetite from many mortgage lenders to obtain vacant possession of properties that will not sell in the current climate.

Numerous government departments have a direct role in matters of consumer credit and debt – the Department of Finance oversees the regulation of the financial system, including the Financial Regulator and the Ombudsman for Financial Services. The Department of Justice is responsible for overseeing the administration of justice and initiating law reform. The Department of Social and Family Affairs funds the Citizens Information Board and the Money Advice and Budgeting Service and funds the payment of Mortgage Interest Supplement (MIS) through the network of Community Welfare Officers attached to Health Service Executive. The Department of the Environment is responsible for housing and local authorities and the Department of Enterprise, Trade and Employment incorporating the National Consumer Agency for matters of general consumer protection. Given the strong connection between over-indebtedness and potential ill-health, both physical and mental, and the importance that should be attached to financial education identified by the Commission in the Paper, both the Departments of Health and Children and Education are also important.

There have been whole forests cut down speculating on, analysing and parsing NAMA. Regardless of how one feels about it, it is a plan to deal with the financial crisis. By contrast, there appears to be no plan or even a recognition that a consumer debt crisis exists. It is no accident that increasingly; ordinary people are asking where the rescue plan is for them. An inter-departmental committee of high ranking civil servants, with access to appropriate expertise where necessary, should now co-ordinate a coherent strategy to alleviate the serious financial difficulty being suffered by consumers.

## **Mortgage Arrears**

This is particularly urgent in the case of mortgage arrears. Last Friday night two young couples appeared on the Late Late Show to speak about their mortgage difficulties. One of these couples has to vacate their family home in the next fortnight and the other couple are engaged in a desperate struggle to hold onto their home. They have four and three children respectively. Neither appears to have had an extravagant lifestyle. Both took out 90% mortgages providing a 10% deposit themselves, very standard five or so years ago when these mortgages were commenced. As a result of loss of employment, arrears began to accumulate on their mortgages from prime lenders and on other borrowings and both couples obtained consolidation loans at high interest rates from sub-prime lenders through mortgage brokers. With no hoped-for improvement in their finances, it was not long before arrears began on the consolidation loans. This time, with the extra high interest rates and penalties, the position deteriorated very quickly. No limits were placed by the State on the rates of interest charged by these operators and the sundry penalty charges appear to have been sanctioned by the Financial Regulator under the consumer credit legislation. One of these families is receiving 15 calls a week to see if their circumstances have changed. This is not debt collection, it is unregulated harassment.

These stories are far from untypical and are not, as some would have us believe, instances of reckless borrowing. On the contrary, these two couples got on the property ladder as they were encouraged to do at close to the height of the property boom. The worsening economy and resulting unemployment caused default in payment. The market value of both houses is now substantially less than the amount borrowed. Nor should we forget those in local authority or private rented accommodation who are also at risk of homelessness. Only last week I heard from a money advisor of a MABS client evicted from local authority accommodation.

Successive government spokespersons have referred to MABS and the mortgage interest supplement scheme as sources of assistance for people with arrears. MABS provides an excellent service but as a general rule is finding it increasingly difficult to find solutions for overwhelming over-indebtedness. Mortgage interest supplement is a useful support payment but too many conditions are imposed. For example, when the mortgage began, the applicant must have been able to 'afford the repayments', the house must not be up for sale and the amount of mortgage interest payable must be 'reasonable'.

The renewed programme for Government in turn contains a heading on protecting the family home but there is little by way of firm commitment. The Regulator's Code of Conduct on mortgage arrears will be further reviewed, it says. Apart from a moratorium on repossession proceedings for six months from the time arrears first arise (12 months in the case of AIB and Bank of Ireland) voluntarily extended by the Irish Banking Federation last week to a further six months, there is little currently in the Code that can offer comfort to those with substantial deteriorating arrears. It is also suggested that the IBF/MABS Protocol will be reviewed but in my view, that protocol is more relevant to the phased repayment of unsecured debt rather than mortgage arrears.

It is also suggested that more flexible mechanisms to avoid foreclosure will be examined including reduced rates, longer maturity dates, rolling-up of outstanding interest, the bank taking equity in the house, the bank taking ownership and leasing back to the resident with rent payments coming off the loan. There is also a commitment that the Government will examine ways of expanding its own mortgage support measures. These potential developments were announced on October 10<sup>th</sup> but no further detail has since been provided. Perhaps the forthcoming budget will bring some relief?

## **Conclusion**

On FLAC's behalf, I would like to thank the President of the Commission, Mrs Justice Catherine McGuinness, Commissioner Patricia Rickard-Clarke, Head of Research Raymond Byrne and the Principal Legal Researcher on this project, Joseph Spooner for a thorough consultation process and the invitation to speak at the conference this morning. The Law Reform Commission is to be warmly congratulated on an exceptional piece of work but there is unfortunately no room for complacency. Everyone in this august room who cares about fairness in our society must redouble their efforts to ensure that the recommendations in this paper are implemented and that other necessary complementary measures to protect indebted people who are victims of events outside their control are put in place. FLAC has worked for many years in this area and has consistently campaigned for reform. It will come as no surprise to you that we have no plans to depart the scene just now and we will continue to work on our own behalf and in cooperation with others for change.

Thank you most sincerely for your attention.