MONEY

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Take the drama out of your debt crisis

Help is at hand for those suffering from the misery of mortgage arrears or facing bankruptcy because of mounting money problems, writes *Eithne Dunne*

The Big Short, the 2015 comedy-drama, focused on the problems caused when a number of subprime home loans are suddenly in danger of defaulting

Ireland has one of the most powerful personal insolvency systems in the world, which is good news for people shouldering mounting debts.

Although debts come in all shapes and sizes, the biggest problem in Ireland is mortgage arrears. According to the Insolvency Service of Ireland (ISI), while the overall number of mortgage accounts in arrears has fallen each quarter since this time in 2013, there are still more than 70,000 such accounts in arrears. These represent €13.5bn of debt and 10% of all mortgage accounts in Ireland.

While some people manage to deal with their debt by rejigging their budget, many more have no prospect of getting out from under it. And while lenders will sometimes agree to informal, alternative arrangements, these are not easy to secure. In these situations, it's worth knowing that there are several insolvency routes available.

Types of insolvency

For people who owe less than €35,000, do not own a home (or other large asset), have a low income, and are unlikely to be able to settle their debts within the next three years, a debt relief notice (DRN) might be a good option. This allows for the write-off of debt after a three-year supervision period.

For those who can keep up with their secured debts – mortgages or other loans secured against their home/ vehicle/other assets – but cannot pay their unsecured debts – credit cards, utility bills, medical bills – a debt settlement arrangement (DSA) may be suitable. This lets debtors settle a certain amount of their debts over five years, after which the loan is written off.

Then there is a personal insolvency arrangement (PIA), aimed at those who can pay neither their secured nor unsecured debts, have secured debts of no more than €3m, and have worked with their lender for at least six months to try to establish a repayment arrangement. This allows debtors to pay what they can towards both secured and unsecured debts over a period of six years, after which the unsecured debts are written off – in most cases, the secured debts will be restructured and will continue to be paid following the conclusion of the PIA.

Finally, there is bankruptcy. You can apply only if you do not qualify for any of the other insolvency arrangements – this will have to be confirmed in an affidavit – and only if your debts exceed your assets by at least €20,000. Once you have declared bankruptcy, you hand over your assets, your unsecured debts are written off and you are discharged from bankruptcy after 12 months. You can have only one DRN, DSA or PIA in your lifetime, but there's nothing restricting someone from declaring bankruptcy more than once.

Whom to contact

To get advice on and apply for a DRN, the Money Advice and Budgeting Service (Mabs) is your point of contact. For the rest, contact the ISI, which can advise you and put you in touch with a personal insolvency practitioner (PIP).

"PIPs are the best-kept secret in the country," said Shelagh Marshall, a Cashel-based PIP. Marshall is seeking nomination for Fine Gael in Tipperary largely because she wants to help address the mortgage arrears problem.

"Many debtors don't know who we are but, between us, we have done 4,000 cases in four years."

The process

In the case of a DSA or PIA, your PIP would apply for a protective cert. This lasts 70 days.

"The protective cert is like a ring of steel around the debtor," said Ross Maguire SC, the founder of PIP specialist New Beginning.

"No one can touch them in that time, during which the PIP tries to negotiate a deal between the debtor and creditor, based on what each party wants."

> "You may be putting your home at risk so we'll talk to people about whom they should pay first

Between the last quarter of 2013 and the second quarter of this year, almost 70% of DSA cases ended in a yes vote from the creditor; for PIAs, this figure was 56%.

If the creditor turns down the proposal, and the case involves a family home, the decision can be appealed through the court review system. This option does not apply, however, to unsecured debts.

"The PIA was set up specifically to deal with the mortgage arrears crisis; government policy is to try to keep people in their homes where possible," said Maguire. "There has been a series of decisions in the High Court where the courts have enforced very substantial debt writedowns."

Marshall said this has helped matters considerably but could be stymied by action taken by several banks to try to put the onus – and expense – of seeking these reviews back on the PIP, rather than the debtor.

Meanwhile, in a recent statement to the Oireachtas joint committee on justice and equality, the ISI head Lorcan O'Connor said that he did not believe creditors were constructively engaging with the personal insolvency legislation, with banks "rejecting proposals that produced a better return than repossession" and mounting challenges to PIAs "on technical rather than commercial grounds".

Costs

There is no charge for a DRN via Mabs; neither does the ISI charge fees. The cost of applying for bankruptcy is €270. However, if you need to contact a PIP, whether for a DSA or PIA, there will be a charge involved.

"A PIP will charge a consultation fee to go through a person's financial situation to determine whether they are eligible to apply for a DSA or PIA," said an ISI spokesman. "After that, any PIP fees are usually built into the DSA/PIA repayment plan."

That's assuming you do not qualify for a voucher from Mabs under the Abhaile scheme, which allows borrowers with mortgage arrears to meet a PIP for free advice. The priority is to find a sustainable solution that keeps a person in their home.

To qualify for Abhaile, you must have been in arrears on January 1, 2015.

Credit rating

While any insolvency option will show up on your credit history, that does not necessarily mean you will be precluded from getting credit in the future.

"If a person is in arrears on payments, this could already be known to credit rating reference agencies," said the ISI spokesman. "Entering into a PIA should indicate to potential lenders that a person is proactively addressing their financial situation and, on completion of the arrangement, they will be solvent, which means they could be more eligible to obtain credit."

Tackle your debt now

Despite the problems with the system, Marshall said she had many successes under the insolvency legislation, with positive outcomes.

"People coming in to us are very vulnerable, and you have to be realistic with them. But even though we're aware of these issues with the system, we don't want people to stop engaging. Go to a PIP; you will get good advice."

Maguire said people tended to react in one of three ways when they found themselves in excessive debt.

"Some people know they'll never be able to pay it, so they reckon there's no point in engaging [with the lender]. Some think they're just going through a bad phase and they'll be OK. And then you have the malingerers."

Helen Just is the Ireland services team leader with debt charity Step Change. She said some callers just wanted to talk to someone about their financial worries, while others needed advice as to which debts to prioritise.

"We often find that unsecured creditors shout louder than the mortgage lenders, and the normal human reaction is to pay the person shouting loudest," she said. "But you may be putting your home at risk by doing that, so we'll talk to people about whom they should pay first and why."

The charity asks callers about their concerns and then runs through their income and expenditure. It then helps them put together a budget, using the ISI's reasonable living expenses guidelines as a starting point.

The charity can put together a proposal for the person's lender. "Say someone is paying a mortgage of €1,000 a month but, after we've looked at their budget, we can see they have only €700 a month for it. We can ask the lender if there's anything they can do."

Failing that, Step Change will talk through the various types of personal insolvency and suggest which might suit. "We will direct people to Mabs for a DRN, or recommend a PIP if it looks like they'll need a DSA or PIA."

MARKET MOVER RHYS EVANS

Rhys Evans is fund manager of the Aviva Ireland Irish Property Fund, managing more than €330m of direct and indirect real estate investments within the Republic. His responsibilities include stock selection, delivering asset management initiatives and managing fund liquidity. The fund is available to all current Aviva life and pensions products from €100 per month.

Fund philosophy

The objective is to obtain optimum returns via income and capital appreciation, through direct real estate and property-related securities in Ireland. This is a daily-priced, daily-dealt, open-ended unit-linked vehicle with a retail investor client base (with a low risk appetite).

"A small number of redevelopments have also been undertaken when the fund has had both the opportunity to do so and a strong set of well-performing assets to maintain investor performance during the redevelopment," said Evans.

The fund has a well-diversified portfolio, with the majority invested into direct real estate and a portion indirectly, with exposure to the Green, Hibernia and IRES Reits. While it is a little ahead of its peers when it comes to a weighting towards retail, Evans said in-house research indicates that prime Irish retail should be "one of the best performing sectors within pan-European real estate over our forecast period".

Performance

"The fund has performed exceptionally well over the last five-year period; it won the IPD/MSCI European Property Investment Award 2016 for best-performing balanced real estate fund in the Irish market," said Evans.

"While we do not necessarily look at cumulative returns, over a five-year period, the fund has achieved cumulative performance of 94.6%, so €10,000 invested in 2011 would have almost doubled."

One of the fund's repositioning projects was a prime retail and office scheme at 26/27 Grafton Street, which was named Retail Project of the Year at the 2017 Irish Building & Design Awards and highly commended at the annual RIAI Irish Architecture Awards 2017. The former A Wear store now hosts & Other Stories.

The second redevelopment project, an office refurbishment at 7 Grand Canal, was delivered into a market starved of grade A space.

Outlook

The fund currently has a vacancy rate of just over 1%, against a benchmark of 7.5%, and a weighted average lease term of almost nine years. Combined, this delivers a property level income yield that is forecast to average 5% over the next five years.

In addition to the directly held portfolio, the indirect investments into the Reits provide the fund with an alternative investment angle.

The impact of the recent increase in stamp duty from 2% to 6% — both on the fund's existing holdings and the wider investment market — is being closely monitored, according to Evans. "It has capital reserves to deploy should the tax increase lead to investment opportunities, and a base portfolio with strong fundamentals on both the direct and indirect holdings."

Gary Connolly

Short-term bias shows why savers all need a good Nudge

It seems only fitting for a columnist who draws significant inspiration from behavioural economics to acknowledge the profession's newest Nobel prize winner.

This year's Nobel in economics was awarded to Richard Thaler of the University of Chicago. Thaler has been one of the most important forces for change in terms of the profession's positive influence within finance.

The idea that psychological research should even be part of economics still remains controversial and Thaler has been a lifelong campaigner for it to be taken seriously. His regular column – Anomalies – started 30 years ago in the Journal of Economic Perspectives, was arguably the start of the process towards broader acceptance of the influence of psychology on economics (and its subfield, behavioural finance).

In the column, he documented individual instances of strange economic behaviour that the standard theory could not explain, and rigorously debunked attempts at rationalisation.

His book Nudge (co-authored with Cass Sunstein) brought his theories into the policy environment and strongly influenced the establishment of behavioural policy units in American and UK government agencies. And his latest book, Misbehaving, is a superb account of the origins, and ultimately coming of age, of behavioural economics.

My favourite observations of Thaler relate to self-discipline or lack thereof. He asks the question – have you ever moved a bowl of nuts out of arm's reach at a dinner party to stop yourself from nibbling your appetite away?

As a student of economics I was taught that it does not make sense to place nuts out of arm's reach; if I did not want to eat them I would simply choose to stop eating. According to Thaler, the distinction between what we want and what we choose has no meaning in the rationalist theory of economics where self-control problems don't exist.

The bowl of nuts is a trivial and fun example but Thaler's insight is that such trivia might lead to important analytical and policy insights.

His most famous idea in the policy world is the use of behavioural insights in pensions policy – enrolling people in a pension scheme by default, while giving them the choice to opt out. And it is here, and more broadly in relation to savings, that Thaler-inspired interventions have had the greatest impact on our financial lives.

If you are asked to imagine yourself lying on a beach in your favourite destination in the world, a certain area of the brain lights up and can be picked up on scans. If asked to imagine yourself lying on a beach in your favourite place in the world 12 months from now, that same area of the brain fails to light up for most people.

Some people, when thinking about their future selves, do not actually picture an older version of themselves. Rather, they picture a stranger. This failure to identify with your future self is well recognised by Thaler and others and manifests itself in tendencies towards short termism. And this is in direct conflict with long-term financial planning and a reluctance to save. After all, if the future you is a stranger, why would you be concerned?

Behavioural economists have explored this phenomenon of "present bias," and the question that Thaler and others have tried to answer is, can the psychological gap between the two selves be closed, and would this affect willingness to save?

At New York University's Stern School of Business, they provided people with digital pictures designed to show them what they will look like a few decades from now. People who were shown images of their future selves significantly increased (and in some cases more than doubled) the amount of money that they allocated to their retirement account. The result was robust to age, with both college students and older age groups showing the same results.

People are often not the best judges of what will serve their long-term interests. So institutions, including government, can help people do better for themselves (and the rest of us) with small changes – nudges – in the structure of the choices we face.

To those that recoil at efforts at manipulation, especially by governments, I think if constructed in a completely transparent manner it should be embraced.

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