



Stressed borrowers must be allowed to live normally

If the banks set a very low standard of what is a reasonable standard of living, they will exclude large numbers of people from participation in the economy

COMMENT



By DJ O'Donovan

The issue of what is a "reasonable standard of living and reasonable living expenses" has the potential to become a very divisive issue when the new personal insolvency procedures come into practice.

We have seen in the past two years since the introduction of the Standard Financial Statement (SFS), which lenders are using to assess debt forbearance cases, that banks are scrutinising and challenging every aspect of a borrower's household expenditure, even down to what they spend on Christmas and birthday presents for their children.

Some borrowers do need to implement household budgets to manage their finances better, but in many cases, banks are effectively acting as receiver over the borrower's income in return for temporary relief on loan repayments.

In most instances, forbearance is only for six or 12 months. After that clients must submit an up-to-date SFS detailing all of their income and expenditure, as well as up-to-date bank statements and income details. Then, if the bank feels there is more to be squeezed out, it can challenge again.

The table above is a summary of what one institution thinks is an acceptable level of household expenditure. The reality here is that people with this level of expenditure will be excluding themselves from normal social aspects of life, including not having the ability to take a family holiday. Children in affected families may be denied a socially reasonable standard of living by not having the means to take part in extra-curricular activities, which could affect their education and welfare.

Borrowers have been asked about where they are doing their shopping, whether they cut back on groceries, cut out even the basic TV package and cancel their health insurance and pension contributions. We should not forget that our economy depends on households spending money in shops, restaurants and on services. It should be obvious to anyone walking down the streets of any of our main cities and towns that many businesses have closed because of the squeeze on household spending.

The **Association of Expert Mortgage Advisors** has seen mortgage arrears cases where clients are struggling to meet total loan repayments representing up to 70 per cent of their monthly net income. The fear we have for these people is that there is a force creeping into society that is setting reasonable living expenses at a level close to the poverty threshold. If this is not challenged, thousands of households will be forced into – or close to – poverty in order to repay their loans. This would exclude them from participating fully in the economy for what could be a lifetime.

The joint IBF/Mabs operational protocol Working Together to Manage Debt (June 2009) states that "Mabs Advisers aim to support clients to protect a standard of living for themselves which is acceptable and, at minimum, is above the poverty line". This is the root of the problem: the goal is to squeeze living expenses to this level, without any consideration for the consequences for the individuals, their families or the economy.

If you ask working people to live at welfare levels over a long-term basis, you effectively remove the incentive to remain working. In an economy crippled with unemployment, it would seem somewhat foolhardy to allow banks to unintentionally expand our welfare state.

The pain that banks expect borrowers to sustain must be commensurate with the reward, so if it's just an interest-only extension, it's hard to expect the homeowner to live on bread and water, but if there's a debt write-off deal on the table, borrowers are willing to take far more lifestyle pain.

There is a more equitable and fairer way to establish a reasonable standard of living and reasonable living expenses – it's the one banks

already use as part of their lending policies for approving home loans. Most banks will lend to someone purchasing a house by assessing the proposed monthly mortgage repayment plus any existing monthly loan repayments as a percentage of the borrower's net monthly income.

As long as the total of the proposed mortgage repayment and existing loan repayments do not exceed 40 per cent of the applicant's total net monthly income, the bank will approve the mortgage.

This would have been the same criterion used for most of the existing borrowers who are now in mortgage arrears, but because of reduced incomes, loss of employment or closure of a business the percentage of repayments to income has been turned on its head.

Why should the banks operate one policy for existing customers in mortgage arrears and another for those seeking mortgages? Why are they challenging borrowers' living expenses to the extent that some are left with as little as 30 per cent of their net monthly income to live off while banks believe new borrowers cannot be left with less than 60 per cent of their net monthly income?

We can appreciate that the banks have to protect their balance sheets and improve profitability for their shareholders (including the government and ultimately the taxpayers). However, if they continue to be so aggressive and demand such a large percentage of their customers' incomes, the banks and the greater economy will not recover without the inclusion of these people in society and in the economy.

*DJ O'Donovan is a member of the **Association of Expert Mortgage Advisors***

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Author: DJ O'Donovan

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Summary of one institution's acceptable household expenditure

	Sole Household	Joint Household, 1 Employed	Joint Household, 2 Employed
Basic guide expenditure	€1,200	€1,700	€2,000
Plus per child	€200	€200	€200
Medical Expenses	To be verified	To be verified	To be verified
Childcare Costs	Must be reasonable	Must be reasonable	Must be reasonable