

# THE FRESH START GOAL OF THE *BANKRUPTCY ACT*: GIVING A TEMPORARY REPRIEVE OR FACILITATING DEBTOR REHABILITATION?

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*Providing debtors with the opportunity for a fresh start is popularly regarded as one of the main goals of bankruptcy legislation. However, there has been limited analysis of this goal. This article confirms that the fresh start is one of the main goals of the Australian Bankruptcy Act, and argues that this fresh start focuses on discharge of debt and does not explicitly address debtor rehabilitation. A review of the key goals could examine whether, and to what extent, rehabilitation should also be a focus of the fresh start in Australian bankruptcy law.*

## I INTRODUCTION

In Australia, slightly more than 20,000 individuals entered bankruptcy in 2012-13,<sup>1</sup> and most of these did so voluntarily.<sup>2</sup> For those choosing to apply for bankruptcy, it could be assumed that a decision has been made that the costs and restrictions of bankruptcy (including the surrendering of assets owned at the time of bankruptcy, or acquired during bankruptcy, and the potential employment and travel restrictions) are an acceptable trade for the opportunity of a so-called ‘fresh start’ at the conclusion of their bankruptcy. This fresh start is said to be one of the main goals of bankruptcy legislation, particularly in Anglo-American legal

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<sup>1</sup> See Australian Financial Security Authority, *Annual Statistics 2012-13* <<https://www.afsa.gov.au/resources/statistics/provisional-bankruptcy-and-personal-insolvency-statistics/annual-statistics/annual-statistics-2012-13>>. Note that the Australian Financial Security Authority (‘AFSA’) is the new name for the Insolvency Trustee Service Australia (‘ITSA’).

<sup>2</sup> During 2012-13, the regulator processed 18,993 debtor’s petitions and received 3,001 creditor’s petitions for processing: Insolvency and Trustee Service Australia Annual Report 2012-13 18.

systems,<sup>3</sup> and it is probably the most important goal from the perspective of debtors.<sup>4</sup>

There are numerous references in legal, policy and political documents that support the existence of a fresh start goal for the *Bankruptcy Act 1966* (Cth) (*'Bankruptcy Act'*), but these documents rarely explain the term. The existence and scope of the fresh start goal has also not attracted a great deal of attention in academic commentary in Australia.<sup>5</sup> Indeed, as David Morrison noted in 2009, there has been little bankruptcy research of any kind conducted in Australia,<sup>6</sup> although more recently, there has been some greater academic attention paid to this area of law.<sup>7</sup>

This lack of clarity about the existence and meaning of the fresh start goal makes it difficult to assess whether the *Bankruptcy Act* is achieving this goal. This is an important issue. Bankruptcy imposes significant costs on individuals, businesses, government and the community more generally, and it is important to be confident that the legislation is effective in light of its key goals. Without clarity

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<sup>3</sup> Although Jacob Ziegel has suggested that there is a distinction between the fresh start provided by in the United States (at least before the 2005 reforms) and what he calls a 'qualified' fresh start provided by the United Kingdom, Canada and Australia: Jacob Ziegel, 'Facts on the Ground and Reconciliation of Divergent Consumer Insolvency Philosophies' (2006) 7(2) *Theoretical Inquiries in Law* 299, 302.

<sup>4</sup> Zagorsky and Lupica suggest that the fresh start is 'the central theoretical objective of bankruptcy from the perspective of the debtor': Jay L. Zagorsky and Lois R. Lupica, 'A Study of Consumers' Post-discharge Finances: Struggle, Stasis, or Fresh-start?' (2008) 16(1) *American Bankruptcy Institute Law Review* 283, 283.

<sup>5</sup> Some exceptions include: Lynden Griggs, 'Bankruptcy Policy and the Decision of the High Court in *Pyramid Building Society (In Liq) v Terry*' (1999) 1(1) *University of Notre Dame Australia Law Review* 57, discussing the tension between the goals of the fresh start and of equal distribution to creditors; and John King, 'Moving beyond the 'hard' - 'easy' tug of war: a historical, empirical and theoretical assessment of bankruptcy discharge' (2004) 28 *Melbourne University Law Review* 654, discussing the appropriate length of bankruptcy.

<sup>6</sup> David Morrison, 'Recent developments: Bankruptcy research in Australia: a review' (2009) 17 *Insolvency Law Journal* 209, 209. In a 1997 paper, Bennetts was more critical of the lack of bankruptcy research, and suggested that 'the formation of our bankruptcy policy usually reflects fundamental assumptions of fact unsupported by empirical research': Keith Bennetts, 'Bankruptcy Reform: The Significance of Systematic Data and Consultative Processes in Developing Our Bankruptcy Law' (1997) 1 *Flinders Journal of Law Reform* 199, 201.

<sup>7</sup> There have been a number of studies analysing the official bankruptcy statistics, including Ian Ramsay and Cameron Sim, 'Personal Insolvency in Australia: an Increasingly Middle Class Phenomenon' (2010) 38 *Federal Law Review* 283 and Rachel Lee and David Morrison, 'Trends in Personal Insolvency in Australia : an Update' (2012) 20 *Insolvency Law Journal* 18; and John Tribe has compared discharge policies in England and Australia: John Tribe, 'Discharge in Bankruptcy: An Historical and Comparative Examination of Personal Insolvency Relief in England and Australia' (2012) 20(4) *Insolvency Law Journal* 240. A major study has also recently been funded by the Australian Research Council: Melbourne Law School, *Paul Ali, Ian Ramsay, Kathy Landvogt, Gerard Brody and Fiona Guthrie – ARC Linkage Project* (1 July 2013) University of Melbourne <<http://www.law.unimelb.edu.au/index.cfm?objectid=AD169B40-E1E0-11E2-94BC0050568D0140>>.

around the goals of the legislation, evaluating the achievement of the goals, and/or law reform proposals, is difficult at best.<sup>8</sup>

This paper therefore interrogates relevant primary and secondary sources of bankruptcy law in Australia to identify whether the fresh start is one of the goals of the *Bankruptcy Act*, and if so, what is the scope or meaning of this fresh start.

To set the scene, I first examine discussions about the fresh start in the academic literature, and find that expressions of the fresh start in bankruptcy appear on continuum. At one end, the idea of the fresh start focuses on discharge of debt (a 'debt discharge-focused fresh start'). At the other end of the continuum, the idea of the fresh start encompasses debt discharge, but also broadens to emphasise the debtor's rehabilitation through improved financial well-being (a 'rehabilitation-focused fresh start').

In the main part of the paper, I examine the legislation, parliamentary documents, legislation, law reviews, and case law to identify whether the fresh start is a goal of Australian bankruptcy law, and, if so, what is the type of fresh start that is provided. I find that these documents support the proposition that the fresh start is one of the primary goals of the *Bankruptcy Act*. There is not a consistent view across the documents about the scope of the fresh start; however, the majority of references, and the key parts of the Act itself, seem to describe a debt-discharge focused fresh start.

I then discuss the implications of these findings. Given the importance of the fresh start goal, and the lack of clarity about its meaning, I propose that the *Bankruptcy Act* should be amended to include an objects clause that sets out, with sufficient clarity, the various goals of the legislation, including the fresh start goal. As a first step, this objects clause could reflect a debt-discharged focused fresh start, consistent with the findings in this paper. However, given that a number of the key law reform documents have also emphasised debtor rehabilitation, I argue that a wider discussion about the appropriate goals for the *Bankruptcy Act* would also be timely. This should consider whether the fresh start goal should reflect a broader understanding, and encompass a focus on debtor rehabilitation.

## II UNPACKING THE FRESH START CONCEPT

References to a fresh start goal in community, policy and legislative documents about bankruptcy are frequent, but the term is rarely defined or explained, and there does not appear to be consensus on its meaning.<sup>9</sup> Instead, as Karen Gross notes, euphemisms are frequently used to describe the fresh start.<sup>10</sup> Phrases used to describe the fresh start potential of bankruptcy include 'a clean sheet',<sup>11</sup> and

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<sup>8</sup> Vanessa Finch makes this point in the context of corporate insolvency law: Vanessa Finch, *Corporative Insolvency Law: Perspectives and Principles* (Cambridge University Press, 2 ed, 2009) 1.

<sup>9</sup> Karen Gross, 'Demonizing Debtors: a Response to the Honsberger-Ziegel Debate' (1999) 37(1-2) *Osgoode Hall Law Journal* 263, 263.

<sup>10</sup> *Ibid* 264.

<sup>11</sup> Griggs, above n 5, 57.

'economic rehabilitation'.<sup>12</sup> Commentators also suggest that the fresh start and/or discharge is about the debtor "beginning again on the economic treadmill";<sup>13</sup> having a restored ability 'to participate in the open credit economy';<sup>14</sup> restoring their 'financial well-being',<sup>15</sup> or obtaining 'longer term financial health'.<sup>16</sup> Karen Gross argues that one of the reasons for difficulties in defining the meaning of the fresh start is that 'the definition requires that we delve deeply into issues many of us would prefer to ignore or forget', including issues about money, shame, and the fact that bankruptcy is not just a legal concept.<sup>17</sup> While these difficulties may be real, it is important to find a consensus about the meaning as it applies in Australia.

Reviewing recent literature on bankruptcy and the fresh start suggests that ideas about the scope of the fresh start in bankruptcy fall on a continuum. At the narrower end of the continuum, the fresh start is seen as being primarily about the relief from obligations to repay debts. The fresh start provides the debtor with a new slate or a clean slate, in the sense that he or she no longer has the burden of the existing debts hanging over their head. William Whitford provides an example of this approach, where he describes the fresh start idea as being summarised:

by the metaphor of a curtain falling on a debtor's affairs at filing ... Except to the extent that it is exempt, the debtor's property is used to pay creditors. Debts not paid in this way are 'discharged', meaning that the creditor cannot look to property subsequently acquired by the debtor for repayment of the debt. The debtor begins his/her financial life with a clean slate, or "fresh start".<sup>18</sup>

Similarly, Ross Buckley describes the fresh start as being embodied by the discharge of a debtor's debts.<sup>19</sup> A recent report prepared for the World Bank ('*the World Bank Report*') also directly links the idea of the fresh start with relief from debt, by suggesting that historically, the term fresh start 'refers to a straight discharge; that is, to the possibility to be freed from debt without a payment plan'.<sup>20</sup>

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<sup>12</sup> Katherine Porter and Deborah Thorne, 'The Failure of Bankruptcy's Fresh Start' (2006) 92(1) *Cornell Law Review* 67, 68.

<sup>13</sup> Griggs, above n 5, 69.

<sup>14</sup> Margaret Howard, 'A Theory of Discharge in Consumer Bankruptcy' (1987) 48 *Ohio State Law Journal* 1047, 1048.

<sup>15</sup> Zagorsky and Lupica, above n 4, 284.

<sup>16</sup> Jean Braucher, 'Consumer Bankruptcy as Part of the Social Safety Net: Fresh Start or Treadmill?' (2004) 44(4) *Santa Clara Law Review* 1065, 1070.

<sup>17</sup> Gross, above n 9, 267.

<sup>18</sup> William Whitford, 'Changing definitions of fresh start in U.S. bankruptcy law' (1997) 20(2) *Journal of Consumer Policy* 179, 179.

<sup>19</sup> Ross P Buckley, 'The Systemic Benefit of Insolvency Law: a Lacuna in the Australian Literature' (2003) 11 *Insolvency Law Journal* 38, 40.

<sup>20</sup> Working Group on the Treatment of the Insolvency of Natural Persons, 'Report on the Treatment of the Insolvency of Natural Persons' (Report 77170, World Bank, 2013) 115 ('*World Bank Report*'). This is contrasted with a delayed new start, where the debtor is relieved of debts but only after some time and/or after making at least some repayment to creditors: at 115.

To the extent that the fresh start is understood in this way, the terms fresh start and debt discharge are treated, implicitly or explicitly, as mutually interchangeable.<sup>21</sup> As a result, if a debtor has received a debt discharge (usually on discharge from bankruptcy), he or she has necessarily received a fresh start. As suggested in the *World Bank Report*, the practical problem of insolvency can be solved, and the fresh start can be achieved, ‘in one procedure’.<sup>22</sup>

Other commentators, however, seem to take a broader approach to the scope of the fresh start in bankruptcy. For these commentators, debt discharge is valuable and a necessary part of the idea of the fresh start, in that it provides some ‘breathing room’.<sup>23</sup> However, without more, they argue that debt discharge may not be sufficient to provide the opportunity for a fresh start for all, or even most, debtors. For example, Zagorsky and Lupica suggest that:

if instead financial distress is a symptom of the confluence of a complex web of social, economic and financial conditions, then perhaps the discharge is merely a palliative solution that fails to address debtors’ underlying problems in a meaningful way.<sup>24</sup>

Some commentators make a distinction between the *legal* fresh start provided by the discharge of debt, and a *financial* fresh start, which requires a focus on the debtor’s prospects for an improved financial future.<sup>25</sup> For example, Jean Braucher argues for an approach to the fresh start and bankruptcy that aspires “to improve the long-term financial health of debtors”.<sup>26</sup> This can be achieved, in part, through prevention of future indebtedness as part of the fresh start goal,<sup>27</sup> and, in this light, Gross and Block-Lieb support financial literacy education in the bankruptcy process,<sup>28</sup> although they are less convinced about the way that this goal has been implemented in the United States.<sup>29</sup> It also may involve attention to housing and/or employment prospects.<sup>30</sup> For another perspective, John Tribe has

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<sup>21</sup> For example, van Apeldoorn explicitly acknowledges that treats the terms fresh start and discharge as mutually interchangeable: Jan C van Apeldoorn, 'The 'Fresh Start' for Individual Debtors: Social, Moral and Practical Issues' (2008) 17 *International Insolvency Review* 57, 59.

<sup>22</sup> The World Bank makes this comparison between the problem of poverty, and the problem of insolvency: above n 20, *World Bank Report*, 12.

<sup>23</sup> Zagorsky and Lupica, above n 4, 288.

<sup>24</sup> Zagorsky and Lupica, above n 4, 287.

<sup>25</sup> For example, *ibid* 283; Gross and Block-Lieb also make this distinction between a legal fresh start and a financial fresh start: Karen Gross and Susan Block-Lieb, 'Empty Mandate or Opportunity for Innovation? Prepetition Credit Counselling and Post-Petition Financial Management Education' (2005) 13 *American Bankruptcy Institute Law Review* 549, 549.

<sup>26</sup> Braucher, above n 16, 1070; see also Zagorsky and Lupica, above n 4, 286.

<sup>27</sup> Assaf Lichtash, 'Realigning the American Consumer Bankruptcy System with the Goals of the Fresh-Start Doctrine: A Global Comparative Analysis' (2011) 34 *Loyola of Law Comparative and International Law Review* 169, 171.

<sup>28</sup> Gross and Block-Lieb, above n 25, 550; see also Susan Block-Lieb et al, 'The Coalition for Consumer Bankruptcy Debtor Education: A Report on its Pilot Program' (2004-2005) 21 *Emory Bankruptcy Developments Journal* 233, 257.

<sup>29</sup> See for example, Gross and Block-Lieb, above n 25, 569; The World Bank also suggest that there needs to be some attempts to change debtor’s attitudes concerning proper credit use, in addition to debt discharge: above n 20, *World Bank Report*, 115.

<sup>30</sup> See for example, Porter and Thorne, above n 12, 119.

argued that the fresh start also needs to encompass the debtor's ability to have access to an account that can be used receiving income and making payments.<sup>31</sup>

A fresh start goal that encompasses improved financial well-being, through changes to debtor circumstances, understanding, abilities and/or actions in relation to financial matters can be described as a rehabilitation-focused fresh start. Such a fresh start is located further along the fresh start continuum than a debt discharge-focused fresh start. Commentators using this wider idea of the fresh start acknowledge that it cannot be achieved through bankruptcy legislation alone. Attention may also need to be paid to other laws, policies and programs, for example, laws, policies and programs that influence housing security and employability.<sup>32</sup> However, bankruptcy legislation can also help or hinder the achievement of a rehabilitation-focused fresh start,<sup>33</sup> and bankruptcy can provide a trigger for access to programs and services outside the bankruptcy system that may be necessary if this wider idea of a fresh start is to be achieved.<sup>34</sup>

This discussion illustrates that commentators have different ways of understanding the fresh start concept in bankruptcy. Some emphasise the significance of debt discharge to delivering the fresh start, while others consider that more is needed if debtors are to truly receive a fresh start. These differences can perhaps be located along a continuum from a fresh start that is solely or primarily about debt discharge (the debt discharge-focused fresh start), to a fresh start that is about debtor rehabilitation in a broader sense (the rehabilitation-focused fresh start). In the next section, I explore the scope of the fresh start in Australia to identify where it is located on this continuum.

### III UNDERSTANDING THE EXISTENCE AND SCOPE OF THE FRESH START GOAL IN THE AUSTRALIAN *BANKRUPTCY ACT*

#### *A Identifying the fresh start goal*

The characterisation of the *Bankruptcy Act* as having a fresh start goal is a common one, but attention to the task of assessing the correctness of this characterisation, or the scope of the goal, has been lacking. This is despite the importance of such a task if an accurate evaluation of the legislation, or of any

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<sup>31</sup> Tribe, above n 7, 263; Although this may be less of an issue in Australia than in some other countries, given that in 2012, 96.9% of the population had a transaction account: Chris Connolly, 'Measuring Financial Exclusion in Australia' (Report, Centre for Social Impact (CSI) University of New South Wales, for National Australia Bank, June 2013) 13.

<sup>32</sup> See for example, the discussion of the issue of income security in the context of bankruptcy in Porter and Thorne, above n 12, 118-120.

<sup>33</sup> In Part III, I briefly discuss some of the provisions in the *Bankruptcy Act* that facilitate or potentially hinder the achievement of this wider sense of a fresh start.

<sup>34</sup> Karen Gross describes how the law has the potential to be a vehicle for social change in the context of bankruptcy: Karen Gross, *Failure and Forgiveness: Rebalancing the Bankruptcy System* (Yale University Press, 1997) 131, 249.

law reform proposals, is to be made. In statutory interpretation,<sup>35</sup> courts identify the purpose(s) or object(s) of legislation having regard to:

- Any objects clause in the legislation itself;<sup>36</sup>
- The terms of the legislation;<sup>37</sup> and
- Relevant extrinsic materials, including the explanatory memorandum, second reading speeches, and relevant Law Reform Commission reports.<sup>38</sup>

Consistent with this approach, in this section of the paper, I analyse the legislation and the relevant extrinsic material to identify the extent of the support for the existence of a fresh start goal for the *Bankruptcy Act*. I also identify the extent of judicial support for the fresh start as being one of the goals of the *Bankruptcy Act*. Finding that there is such support for the fresh start as a goal, I identify the scope of the fresh start that is envisaged, and currently provided for in the legislation.

### *B The fresh start goal in the text of the legislation*

As an express statement, an objects or purpose clause in legislation can make the overall objects of the legislation explicit.<sup>39</sup> However, there is no overriding objects clause applicable to the whole of the *Bankruptcy Act*. Instead, there are two objects clauses that are relevant to specific parts of the Act: those relating to the income contribution scheme<sup>40</sup> and the supervised account regime.<sup>41</sup> Neither of these objects clauses provides any guidance as to the objects of the *Bankruptcy Act* as a whole.

In the absence of an overarching objects clause, the text of the legislation provides guidance as to the existence and scope of any fresh start goal in the *Bankruptcy Act*. Perhaps most significantly, section 153 of the *Bankruptcy Act* provides that from the date of the conclusion of (or discharge from) their bankruptcy, the debtor is 'discharged' or released from their contractual obligations to pay the debts proved in the bankruptcy.<sup>42</sup> As debt discharge is an integral element of both the narrower and wider ideas of the fresh start described above, the existence of section 153 is consistent with the *Bankruptcy Act* having a fresh start goal.

Further, once a debtor has been discharged from bankruptcy, he or she no longer has any obligation to make income contributions to the creditors.<sup>43</sup> Margaret

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<sup>35</sup> The purpose of legislation is relevant when interpreting particular provisions of legislation: *Acts Interpretation Act 1901* (Cth) s15AA.

<sup>36</sup> Although an objects clause may not be an exhaustive statement of the objects of the legislation: Michelle Sanson, *Statutory Interpretation* (Oxford University Press, 2012) 99.

<sup>37</sup> See for example, *Municipal Officers' Association of Australia v Lancaster* (1981) 54 FLR 129, 153.

<sup>38</sup> See *Acts Interpretation Act 1901* (Cth) s15AB; *Bropho v Western Australia* (1990) 171 CLR 1, [16].

<sup>39</sup> Jan Rohde, 'The Objects Clause in Environmental Legislation - the Nature Conservation Act 1993 (Qld) Exemplified' (1995) 12 *Environmental Planning and Law Journal* 80, 82.

<sup>40</sup> *Bankruptcy Act* s 139J.

<sup>41</sup> *Bankruptcy Act* s 139ZIA.

<sup>42</sup> *Bankruptcy Act* s 153.

<sup>43</sup> During bankruptcy, income contributions are required once the debtor's income excess the relevant income threshold: *Bankruptcy Act* s 139P.

Howard has argued that ‘The availability of a debtor’s earning capacity as an asset free from the reach of creditors is what gives the debtor a new start’.<sup>44</sup> Upon discharge, the former bankrupt is also free to acquire assets without the risk of those assets being realised and distributed to creditors.<sup>45</sup> These provisions enable the full potential of the debt discharge to be realised, and are therefore equally consistent with the *Bankruptcy Act* having either a narrow or a wider fresh start goal.

The scope of the fresh start upon discharge is also impacted by the conditions imposed during bankruptcy. For example, during bankruptcy, creditors are not generally permitted to pursue the debtor for payment of a provable debt.<sup>46</sup> This facilitates one of the other goals of bankruptcy – equal treatment of, and distribution among, creditors.<sup>47</sup> However, this provision may also contribute to a rehabilitation-focused fresh start, because of the positive impact that ceasing creditor contact can have on the physical and mental health of debtors.<sup>48</sup> Also, subject to an obligation to make income contributions (mentioned below), the effect of this provision is that any income earned during bankruptcy can be used maintain basic living standards and/or take steps to improve the debtor’s financial future.

Certain property is also exempt from realisation and distribution to creditors. This includes basic household property, means of private transport, tools of trade, and superannuation interests.<sup>49</sup> These exemptions facilitate the bankrupt maintaining at least a basic standard of living and opportunity for employment and social engagement, both during bankruptcy and following discharge from bankruptcy. They therefore facilitate the wider, rehabilitation sense of the fresh start goal. Without such exemptions being made available, the former bankrupt’s opportunity to improve their financial future after bankruptcy is likely to be set back some years, as they spend post-bankruptcy income in restoring basic household goods, transport, and property needed for earning an income.<sup>50</sup>

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<sup>44</sup> Howard, above n 14, 1085.

<sup>45</sup> See *Bankruptcy Act* s 116(1), which provides that the bankrupt’s divisible property includes property belonging to, or vesting in a bankrupt at the commencement of the bankruptcy, and property acquired by the bankrupt after the commencement of bankruptcy and *before* discharge.

<sup>46</sup> *Bankruptcy Act* s 58(3).

<sup>47</sup> For example, see *Re McMaster; ex parte McMaster* (1991) 33 FCR 70, 72-73, as per Hill J, discussed below.

<sup>48</sup> In a 1987-88 study of consumer bankruptcies in Melbourne, 59% of respondents thought that creditor pressure played an important role in their decision to petition for bankruptcy, and 59% of respondents reported that bankruptcy had improved their health: Martin Ryan, *The Last Resort: a Study of Consumer Bankrupts* (Avebury, 1995) 153, 176.

<sup>49</sup> *Bankruptcy Act* s 116(2); *Bankruptcy Regulations 1996* (Cth) (‘Bankruptcy Regulations’) reg 6.03.

<sup>50</sup> If these items were not exempted from realisation and distribution to creditors at the commencement of bankruptcy, then there would be no point in the bankrupt purchasing such items during bankruptcy. They would be similarly subject to realisation and distribution to creditors: subject to the exemptions in *Bankruptcy Act* s 116(2), ‘after-acquired property’ vests in the trustee and is available for realisation and distribution to creditors: *Bankruptcy Act* ss 58(1), 58(6), and 116(1).



However, there are also some provisions in the bankruptcy legislation that potentially reduce the potential for debtors to receive a fresh start upon discharge, particularly in a wider rehabilitation sense. First, with a minimum bankruptcy period of at least three years, access to the fresh start is delayed for a not inconsiderable time, particular when compared to the length of bankruptcy in some other comparable jurisdictions.<sup>51</sup> Second, the discharge of debt will not be complete for all debtors. Some types of debts are not provable in a bankruptcy<sup>52</sup> and others are not dischargeable in a bankruptcy,<sup>53</sup> and thus the debtor will remain liable for those debts after discharge from bankruptcy. Further, a debtor will remain liable for debts arising out of obligations incurred during the bankruptcy.<sup>54</sup> Third, the public availability of bankruptcy information through the National Personal Insolvency Index ('NPII') can potentially hinder a bankrupt or former bankrupt in their efforts to maintain or gain employment and housing both during and after bankruptcy.<sup>55</sup> Fourth, debtors who earn income above a prescribed amount during bankruptcy will be required to make a contribution to the bankrupt estate from their income.<sup>56</sup>

Finally, while the rhetoric around bankruptcy refers to the need for a former bankrupt to 'learn' from their bankruptcy,<sup>57</sup> there is little in the bankruptcy system that facilitates such learning, or attempts to address the underlying problems that lead to the insolvency in the first place. For example, John King notes that all that is required under the *Bankruptcy Act* is for debtors to be provided with a brochure outlining options,<sup>58</sup> and argues that this means that 'any educative effect would be fortuitous and ancillary'.<sup>59</sup> On the other hand, a study of bankrupts in Melbourne

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<sup>51</sup> For example, in the United Kingdom, discharge is available after 12 months, or earlier in some circumstances: *Insolvency Act 1986* (UK) pt IX c 1, s 279. In Canada, discharge is available after 9 months for a first time bankrupt who is not required to make income contributions: *Bankruptcy and Insolvency Act*, RSC 1985, c B-3, s 168.1.

<sup>52</sup> *Bankruptcy Act* ss 82(2) – (3B).

<sup>53</sup> *Bankruptcy Act* ss 153(2) – (3).

<sup>54</sup> The debts provable in the bankruptcy are only those to which the bankrupt was subject at the date of the bankruptcy, or to which the bankrupt may be subject to before discharge as a result of an obligation incurred before the date of bankruptcy: *Bankruptcy Act* s 82(1).

<sup>55</sup> The National Personal Insolvency Index can be inspected by anyone on payment of a fee: *Bankruptcy Regulation* reg 13.06. See also Australian Financial Security Authority, *National Personal Insolvency Index* <<https://www.afsa.gov.au/resources/npai>>. The World Bank suggests that this issue of discrimination against former bankrupts is one that requires further research and consideration, suggesting that it is 'advisable that both researchers and legislators pay attention to the principle of non-discrimination in the future': above n 20, *World Bank Report*, 117.

<sup>56</sup> Income contributions are calculated on the basis of 50% of the excess income earned above the threshold: *Bankruptcy Act* s 139S. As at 23 October 2013, the income threshold for a person with no dependents was \$51,560.60: Australian Financial Security Authority, *Indexed Amounts* (23 October 2013) <<https://www.afsa.gov.au/resources/indexed-amounts>>. Note that debtors can request a higher threshold on the grounds of hardship: *Bankruptcy Act* s 139T.

<sup>57</sup> See, for example, Attorney-General's Department, 'Proposed Amendments to the *Bankruptcy Act 1966*' (Attorney-General's Department, 28 May 2009) 2 ('*Proposed Amendments Paper*').

<sup>58</sup> See *Bankruptcy Act* s 55(3A), *Bankruptcy Regulations* reg 4.11(1).

<sup>59</sup> King, above n 5, 685. Similarly, but in the context of business bankrupts, McAuley notes that 'the statutory framework does nothing to encourage or indeed facilitate business bankrupts to engage in education and counselling programs to avoid future bankruptcy': Steve McAuley,

in 1987 and 1988 reported that, for some participants, the time out from the credit economy that was provided by bankruptcy was sufficient to provide the necessary 'learning'.<sup>60</sup> Given the changes in the economy, and access to the credit since then, it would be interesting to examine the prevalence of such an attitude now.

This brief analysis suggests that the legislation facilitates at least a debt-discharge focused fresh start. There are some provisions in the legislation that also facilitate a wider, rehabilitation-focused, sense of the fresh start. However, these are counter-balanced by other provisions that potentially hinder the achievability of a rehabilitation-focused fresh start.<sup>61</sup> The text of the legislation therefore largely points to the *Bankruptcy Act* having a fresh start goal that is focused on debt-discharge; rather than a fresh start goal that is focused on debtor rehabilitation.

### C *The fresh start goal in the parliamentary documents*

The fresh start is mentioned in a number of parliamentary documents as being one of the goals of the *Bankruptcy Act*; however, the documents do not provide a consistent expression of the meaning of the fresh start. In some cases, the relevant goal of the legislation is said to be one that focuses on providing relief from debts; while in other cases, the goal is said to be one of debtor rehabilitation.

For example, in the Second Reading Speech introducing the *Bankruptcy Act 1924* (Cth) (the first Commonwealth bankruptcy legislation), the then Attorney-General referred, with approval, to a work by Ringwood ('The Principles of Bankruptcy'), and that author's assessment of the 'two great objects' of bankruptcy as being 'first, the distribution of the debtor's effects in the most expeditious, equal and economic manner; and secondly, his release from his creditors.'<sup>62</sup>

No further elaboration of the objects is provided, and the Attorney-General in this speech makes no reference to the concept of the 'fresh start', or of the debtor's rehabilitation.

In the Second Reading Speech introducing the legislation that became the *Bankruptcy Act 1966* (Cth), the then Attorney-General indicated that the Bill 'let the basic structure of the law established by the present Act undisturbed'. However, in comparing the 1965 Bill to the 1924 Act, the Attorney-General refers to rehabilitation, rather than debt discharge, when he notes the main emphases of the 1965 Bill as being 'first, the rehabilitation of debtors whose circumstances are due to misfortune; secondly a strengthening of the provisions aimed at the punishment of dishonest debtors; and thirdly, the encouragement of private trustees to take up the administration of bankrupt estates'.<sup>63</sup> The statement

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'Reducing the Minimum Bankruptcy Period' (2010) 22(2) *Australian Insolvency Journal* 34, 34.

<sup>60</sup> Ryan, above n 48, 247.

<sup>61</sup> A more detailed analysis of the extent to which provisions in the *Bankruptcy Act* hinder a rehabilitation-focused fresh start is the subject of a future article planned by the author.

<sup>62</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 27 June 1924, 1715 (Littleton Groom, Attorney-General).

<sup>63</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 20 May 1965, 1719 (Billy Snedden, Attorney-General).

appears to point more to the rationale for the changes introduced by the 1966 Act, rather than the goals of the legislation overall. However, there is no further discussion of what rehabilitation might mean in this context.

Similarly, there is not a consistent use of the terminology in the parliamentary documents supporting later amendments to the *Bankruptcy Act*. For example, in explaining the introduction of provisions given the Official Receiver the right to reject a debtor's petition on the grounds of abuse, the Explanatory Memorandum to the Bankruptcy Legislation Amendment Bill 2002 notes that 'One key purpose of the bankruptcy system is to allow people in a hopeless financial position to rule a line under their debts and be given a fresh start.'<sup>64</sup> While not using the terminology of fresh start, Senator Campbell's second reading speech for the Bankruptcy Legislation Amendment Bill 2002 (which, among other things, repealed the early discharge provisions) categorised bankruptcy as being 'designed to give people in severe financial difficulty relief, as a measure of last resort, from overwhelming debts'.<sup>65</sup>

On the other hand, the Explanatory Memorandum for the Bankruptcy Amendment Bill 1991, in reference to the introduction of an improved process for applying for early discharge, refers to the two principal aims of bankruptcy as 'first being the return of funds to creditors and second the rehabilitation of the bankrupt'.<sup>66</sup> For this Bill, early discharge was designed to 'allow the debtor to begin the process of financial rehabilitation at an early date'.<sup>67</sup> Again, however, there is no discussion of what rehabilitation might mean or might require.

Thus, the Parliamentary material does not indicate a consistent view about whether a key goal of the bankruptcy legislation, from the perspective of the debtor, is to provide for a fresh start solely by way of relief from debts, or also by way of facilitating debtor rehabilitation.

#### *D The scope of the fresh start as identified by the cases*

In this next section, I explore the extent to which the case law provides any type of guidance on the fresh start concept as a goal of the *Bankruptcy Act*. The cases are, of course, interpreting the legislation as it is written, and in response to the particular disputes that are litigated. In those circumstances, and where the text of the legislation does not appear to facilitate a wider, rehabilitation sense of the fresh start, it is not surprising that the case law also has little emphasis on a rehabilitation focus for the fresh start.

There are few references to a fresh start goal for the *Bankruptcy Act* in the cases decided in the superior courts. The High Court does not seem to have referred to

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<sup>64</sup> Explanatory Memorandum, Bankruptcy Legislation Amendment Bill 2002 (Cth) 17. See also an acknowledgement in the Explanatory Memorandum that the (bankruptcy) laws 'are intended to protect debtors who cannot pay their debts, and to give them a fresh start': Explanatory Memorandum, Bankruptcy Legislation Amendment Bill 2002 (Cth) 9.

<sup>65</sup> Commonwealth, *Parliamentary Debates*, Senate, 19 June 2002, 2091 (Ian Campbell).

<sup>66</sup> Explanatory Memorandum, Bankruptcy Amendment Bill 1991 (Cth) 2.

<sup>67</sup> Explanatory Memorandum, Bankruptcy Amendment Bill 1991 (Cth) 2.

the fresh start as a goal of the *Bankruptcy Act*. However, it has confirmed the importance of debt discharge as the one of the goals. For example, in the decision of *Storey v Lane*, Gibbs CJ in a judgment agreed to by Mason, Wilson and Brennan, stated that:

An essential feature of any modern system of bankruptcy is that provision is made for the appropriation of the assets of the debtor and their equitable distribution amongst his creditors, and for the discharge of the debtor from future liability for his existing debts.<sup>68</sup>

In the High Court decision of *Foots v Southern Cross Mine Management Pty Ltd*<sup>69</sup> ('*Foots*') (a decision about whether a costs order made after bankruptcy was a provable debt), both the majority and minority judgments appear to accept the proposition that debt discharge is an goal of the *Bankruptcy Act*. Both judgments refer to a statement of the purposes of the *Bankruptcy Act 1869* (UK) (on which the Australian legislation was based) set out in *Ex parte Llynvi Coal and Iron Co; Re Hide*.<sup>70</sup> In that case, James LJ remarked that 'The broad purview of this Act is, that the bankrupt is to be a freed man – freed not only from debts, but from contracts, liabilities, engagements and contingencies of every kind.'<sup>71</sup>

However, the majority judgment took the view that this broad purview should not obscure 'the current statutory description of what is and is not provable in bankruptcy', and found that the debt was not provable.<sup>72</sup> In contrast, in his dissent Kirby J suggested that 'To the extent that the statutory language permits, this Court should endeavour to advance, and not to frustrate, the attainment of this [free man] objective'.<sup>73</sup>

One of the most frequently referenced expression of the goals or purposes of the *Bankruptcy Act* is found in the Federal Court of Australia decision of *Re McMaster; ex parte McMaster* ('*Re McMaster*');

The modern bankruptcy law serves three purposes. The first is to ensure that the assets of the bankrupt are distributed rateably among creditors. The second, which is interrelated with the first, is to ensure that one creditor does not obtain an undue advantage over other creditors. The third is to bring about the discharge of the debtor from future liability for his existing debts, so that the debtor may start afresh.<sup>74</sup>

Numerous cases have referenced, with apparent approval, these three purposes as stated in *Re McMaster*, including majority decisions in the Full Court of the

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<sup>68</sup> *Storey v Lane* (1981) 147 CLR 549, 556 (Mason, Wilson, Brennan JJ agreeing).

<sup>69</sup> (2007) 234 CLR 52.

<sup>70</sup> (1871) LR 7 Ch 28.

<sup>71</sup> *Ex parte Llynvi Coal and Iron Co; Re Hide* (1871) LR 7 Ch 28, 32 (James LJ).

<sup>72</sup> *Foots v Southern Cross Mine Management Pty Ltd* (2007) 234 CLR 52, 58.

<sup>73</sup> *Foots v Southern Cross Mine Management Pty Ltd* (2007) 234 CLR 52, 92; see also Kirby J's dissent in *Coventry v Charter Pacific Corporation Limited* (2005) 27 CLR 234, 269-70, where he discusses the purposes of the *Bankruptcy Act*.

<sup>74</sup> *Re McMaster; ex parte McMaster* (1991) 33 FCR 70, 72-73 per Hill J.

Federal Court,<sup>75</sup> as well as decisions in other courts.<sup>76</sup> This expression of the purposes in *Re McMaster* has also been referred to by academic commentators as authority for the *Bankruptcy Act* having a fresh start objective.<sup>77</sup> Other cases have made specific reference to the goal of the legislation being to enable a fresh start by discharging liability for the debts existing at the time of bankruptcy.<sup>78</sup>

However, while the superior decisions focus on debt discharge as a goal of the *Bankruptcy Act*, there are also some cases where the judgment appears to reflect a concept of bankruptcy that, from the debtor's perspective, offers more than just debt discharge. For example, in *FWO Nominees v Jackson-Groze (No.1)*, the court suggests that the purpose of bankruptcy legislation is to:

[E]nsure that persons who do not have assets and who owe large sums of money are placed into the control of a trustee so that their affairs can be sorted out, a veil can be drawn over previous activity, and they can proceed to live in a normal financial state as soon as possible.<sup>79</sup>

In *Re Reilly; Ex Parte The Debtor*,<sup>80</sup> in considering whether he should grant an application for discharge, Lockhart J explained the authorities as saying that, unless satisfied that the debtor has sufficient income to support himself and any dependents, or is likely to inherit or succeed to property, the court ought not to impose on the debtor 'unduly burdensome conditions so that he cannot improve his position in life and remove all incentive for exertion on his part.'<sup>81</sup> Lockhart J also considered relevant the impact of the bankruptcy upon the bankrupt's plans to marry. In granting the application for discharge, Lockhart J also explained:

He is entitled to a fresh start in life and to make his decisions as to marriage and employment unfettered by his bankruptcy, notwithstanding that his application is made soon after his bankruptcy.<sup>82</sup>

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<sup>75</sup> For example, *Fraser v Deputy Commissioner of Taxation (Cth) and Official Trustee* (1996) 69 FCR 99, 112; *Pietropaoli v Travel Compensation Fund* [1998] FCA 1774.

<sup>76</sup> For example, *Otvosi v Ferella* (2008) 219 FLR 472, 477 (a decision on the scope of *Bankruptcy Act* s 58(3)); *Pedersen v Delaveris* [2010] FCA 536, [13]; *Rodway v White* (2009) 233 FLR 262, 271; *Steel Building Solutions Pty Ltd v Wright* [2011] FCA 328, [7]; *Moore-McQuillan v Scott* (2006) 149 FCR 486, 490.

<sup>77</sup> For example, King, above n 5, 658; Lynden Griggs also asserts that it is a principle of the legislation that the bankrupt should be freed from his or her liabilities: Griggs, above n 5, 59.

<sup>78</sup> For example, in *Fitz-Gibbon v Inspector General in Bankruptcy* (2000) 180 ALR 475, 479 Stone J refers to the 'well established' policy of bankruptcy legislation as being 'to strike a balance between the orderly winding up of the bankrupt's estate for the benefit of creditors and freeing the bankrupt from accumulated liabilities so that he or she can make a fresh start'. See also *Boral Johns Perry Industries Pty Ltd v Piccardi* (Unreported, Full Court of the Federal Court of Australia, Wilcox, Burchett and Hill JJ, 23 June 1989): 'The policy of the bankruptcy legislation is that an adjudication of bankruptcy will relieve a debtor from his debts, thus enabling him to make a fresh start and ensuring that the assets of the bankrupt are distributed rateably among his creditors'.

<sup>79</sup> *FWO Nominees v Jackson-Groze (No.1)* [2002] FMCA 194 (27 August 2002), [14].

<sup>80</sup> 1979) 23 ALR 357.

<sup>81</sup> (1979) 23 ALR 357, 367.

<sup>82</sup> *Re Reilly; Ex Parte the Debtor* (1979) 23 ALR 357, 367. The Court also referred to the 'personal sense of shame' of the bankrupt as impacting upon 'the uncertainty that surrounds any prospective marriage: 366-7.

Reference to the fresh start objective is also made in decisions on the scope of the 'tools of trade' exemption in the *Bankruptcy Act*.<sup>83</sup> In *Re Vaughan; Vaughan v Official Trustee in Bankruptcy* Heerey J explained the purposes of the *Bankruptcy Act* as follows:

But one of the underlying purposes of the Act is to give bankrupts the opportunity of a fresh start after surrendering virtually all their property for the benefit of their creditors. To allow a bankrupt to retain tools of modest value for the purposes of a trade that he or she can carry on, even one that had only been conducted in a minor way prior to bankruptcy, or perhaps not at all, is consistent with that purpose.<sup>84</sup>

This statement was not contradicted on appeal.<sup>85</sup>

Another decision that suggests that the fresh start goal of bankruptcy is about more than debt discharge is *Exell and Inspector-General in Bankruptcy*.<sup>86</sup> The case involved the review of a trustee's decision to remit realisation charges, and in discussing the hardship of imposing the realisation charge, the AAT President noted that the applicant was in a 'precarious financial position', had no earning capacity, and was not in a position to have the capacity to make a fresh start and retrieve her financial prosperity.<sup>87</sup> This suggests recognition of the possibility that, at least for this debtor, in the absence of a capacity to earn income, debt discharge would not be sufficient to provide a fresh start.

The above discussion demonstrates that there is not always a consistent view from the cases about the scope or meaning of any fresh start objective in the *Bankruptcy Act*. The discussion of the purposes in *Re McMaster*, with reference to the 'discharge of the debtor from future liability for existing debts' appears to have support, and is also consistent with the High Court's emphasis on debt discharge as in *Storey v Lane and Foots*. There are some judicial comments that suggest perhaps a wider view of the fresh start objective, with debt discharge not being the only focus, but these are not widespread. In addition, these comments are often not necessary to the decision, nor are they found in the majority judgments of appeal cases. They therefore have limited precedent value.

#### *E The fresh start goal in the law reform documents*

Finally, I turn to the major reviews of bankruptcy law, and consider what guidance these documents provide as to the existence and scope of a fresh start objective in the *Bankruptcy Act*.

In 1962, the Report of the Committee Appointed by the Attorney-General of the Commonwealth to review the bankruptcy law of the Commonwealth (*Clyne Committee Report*) was released. This report was the first major review of bankruptcy law in Australia since the implementation of the first Commonwealth

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<sup>83</sup> *Bankruptcy Act* s 116(2)(c).

<sup>84</sup> *Re Vaughan; Vaughan v Official Trustee in Bankruptcy* (1996) 66 FCR 121, 123-4.

<sup>85</sup> *Vaughan v Official Trustee in Bankruptcy* (1996) 71 FCR 34. See also *Tiver v The Official Trustee in Bankruptcy* (2010) 187 FCR 1, 11.

<sup>86</sup> (2000) 30 AAR 320, 327.

<sup>87</sup> *Exell and Inspector-General in Bankruptcy* (2000) 30 AAR 320, 327.

legislation dealing with bankruptcy (the *Bankruptcy Act 1924* (Cth)), and its recommendations formed the basis for the *Bankruptcy Act 1966* (Cth).<sup>88</sup> While the *Clyne Committee Report* did refer to the history of bankruptcy legislation in Australia and the UK (from where Australia's bankruptcy legislation was derived), the report did not engage extensively with the purposes of bankruptcy law. It noted that the need for bankruptcy law was not in dispute, and that the principles underlying bankruptcy law were 'firm and long established'.<sup>89</sup> The report considered that the principles included (at least in the case of honest debtors) the availability of both release from liabilities and "the opportunity to re-establish himself".<sup>90</sup> This reference to a debtor being able to re-establish him or herself might be seen as akin to the idea of debtor rehabilitation. Later, the report refers explicitly to the idea that an honest bankrupt should be given an opportunity to make a 'fresh start',<sup>91</sup> but does not provide any further discussion of what this might mean.

In 1977, the then Law Reform Commission (now the Australian Law Reform Commission) released its report, *Insolvency: the Regular Payment of Debts*,<sup>92</sup> ('*Regular Payment of Debts Report*') and this included an examination of the philosophy of bankruptcy. In this context, the report suggested that debtor rehabilitation is 'the prime concern of the bankruptcy process',<sup>93</sup> and that the law must 'enhance, rather than impede, opportunities for the financial rehabilitation of insolvent debtors'.<sup>94</sup>

Unlike much of the commentary on the fresh start and related concepts, the *Regular Payment of Debts Report* also engaged with what debtor rehabilitation might mean in the context of bankruptcy. It referenced (with approval)<sup>95</sup> reviews in United States and Canada that assert the importance of debtor rehabilitation,<sup>96</sup> and suggested that the following were needed for true rehabilitation:

- Present debt difficulties must be cured;

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<sup>88</sup> In the Second Reading Speech introducing the Bankruptcy Bill 1965, the Attorney-General explained that the bill presented to Parliament was 'for the most part, the bill as recommended by the Committee': Commonwealth, *Parliamentary Debates*, House of Representatives, 20 May 1965, 1713 (Billy Snedden, Attorney-General).

<sup>89</sup> Committee Appointed by the Attorney-General of the Commonwealth to Review the Bankruptcy Law of the Commonwealth, 'Report of the Committee Appointed by the Attorney-General of the Commonwealth to Review the Bankruptcy Law of the Commonwealth' (Government of the Commonwealth of Australia, 1962) 8.

<sup>90</sup> *Ibid* 8. The report also takes the view that there is community acceptance of the proposition that there should be equitable distribution of property amongst creditors, and that there needs to be provision for dealing with dishonest debtors: at 8; see also 33 in relation to equitable distribution.

<sup>91</sup> *Ibid* 16.

<sup>92</sup> The Law Reform Commission, *Insolvency: the Regular Payment of Debts*, Report No 6 (1977) ('*Regular Payment of Debts Report*').

<sup>93</sup> *Ibid* 67. The terms of reference for the review specifically ask the Commission to have regard to 'the community's interests in the financial rehabilitation of small but honest debtors': at v.

<sup>94</sup> *Ibid* 2.

<sup>95</sup> The Law Reform Commission notes that '[these] views have great force': *ibid* 67.

<sup>96</sup> *Ibid* 67.

- An improved sense of budgeting and of the danger of over commitment of meagre income;
- A proper understanding of credit and a sense of his own responsibilities in the payment of obligations freely undertaken<sup>97</sup> (acknowledging that, in some circumstances, this responsibility could be engendered through requiring income contributions).<sup>98</sup>

The Law Reform Commission argued that ‘the law relating to discharge and to income contributions reflects little concern for the rehabilitation of debtors’, and made a number of recommendations designed to reverse that situation. In particular, the Law Reform Commission recommended the introduction of automatic discharge for non-business debtors after six months, subject to the opportunity to object to discharge on limited grounds,<sup>99</sup> and that the need to rehabilitate debtors should be considered when determining whether discharge should be delayed or made conditional.<sup>100</sup>

However, the recommendations of the Law Reform Commission on discharge and rehabilitation were only partially implemented. The minimum bankruptcy period is now three years,<sup>101</sup> but this is significantly longer than the six months recommended by the Law Reform Commission.<sup>102</sup> Further, the impact of discharge on debtor rehabilitation is not a consideration in the process for reviewing a trustee’s objection to automatic discharge.<sup>103</sup>

A more consistent mechanism for assessing income contributions was also introduced in 1991,<sup>104</sup> perhaps addressing in part the LRC’s concern for debtor responsibility. However, there have not been any amendments that would explicitly facilitate the development of improved budgeting, or a proper understanding of credit, that were the other components of rehabilitation as identified by the Law Reform Commission.<sup>105</sup> Ultimately, it appears that the Law Reform Commission’s views about the importance of debtor rehabilitation have not been reflected in the bankruptcy legislation.

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<sup>97</sup> Ibid 68.

<sup>98</sup> Ibid 68.

<sup>99</sup> Ibid xi.

<sup>100</sup> Ibid xi.

<sup>101</sup> *Bankruptcy Act* s 149.

<sup>102</sup> Early discharge after six months was also available between 1991 and 2002 (see *Bankruptcy Act* div 3, subdiv D (repealed)). However, it was only available in limited circumstances, and the potential for debtor rehabilitation was not reflected in the criteria for access to early discharge. See also discussion of the rise and fall of early discharge in the *Bankruptcy Act* in King, above n 5, 664-5.

<sup>103</sup> The focus of a review of an objection is on whether the trustee had reasons for objecting that were directed to achievement of a purpose of bankruptcy law, for example, the recovery of assets for creditors: *Inspector-General in Bankruptcy v Nelson* (1998) 86 FCR 67, 78; 27 AAR 231, 241. See also s149N, which sets out the circumstances in which the Inspector-General must cancel the objection. None of these reasons refer to the impact of the objection on the debtor’s rehabilitation.

<sup>104</sup> See *Bankruptcy Act* Part VI, div 4B.

<sup>105</sup> This contrasts with the introduction of mandatory financial education for debtors entering and exiting bankruptcy in the United States. See discussion of the requirements in Gross and Block-Lieb, above n 25, 550-552.



The Law Reform Commission also published a more extensive report on personal and corporate insolvency in 1988, the General Insolvency Inquiry (*'Harmer Report'*).<sup>106</sup> This report did not directly spell out the overall goals or objectives of insolvency law, but it proposed nine 'principles that should guide the development of a modern [personal and corporate] insolvency law'.<sup>107</sup> None of these principles refer explicitly to the need for the debtor to gain a fresh start, or to be rehabilitated. The most relevant principle is that 'the end result of an insolvency administration, particularly as it affects individuals should, with very limited exceptions, be the effective relief or release from the financial liabilities and obligations of the insolvent'.<sup>108</sup> This is consistent with a fresh start that is primarily about debt discharge, rather than the wider idea of a fresh start that is focused on debtor rehabilitation.

The report included some references to the concept of the fresh start, but predominantly in the context of a discussion on debt-discharge.<sup>109</sup> There are also a number of references to the concept of debtor rehabilitation, and the associated discussion provides some support for the idea that debtor rehabilitation should be a consideration for bankruptcy law.<sup>110</sup> The report also made a number of recommendations that could facilitate debtor rehabilitation, including recommendations that:

- debtors be required to obtain pre-bankruptcy advice;<sup>111</sup>
- a federally funded advice service should be established;<sup>112</sup>
- early discharge be made available, following a trustee's report that considered factors such as the debtor's future financial prospects and aspirations and whether bankruptcy would adversely affect the debtor's employment prospects;<sup>113</sup>
- where the eligibility for discharge was being considered, the Court should be directed to factors such as the debtor's financial rehabilitation;<sup>114</sup>
- postponement of the sale of the debtor's residence be made available.<sup>115</sup>

None of these recommendations have been implemented.

More recently, a concern for debtor rehabilitation was expressed in some initial proposals for law reform identified by the Attorney-General's Department. In

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<sup>106</sup> The Law Reform Commission, *General Insolvency Inquiry*, Report No 45 (1988) (*'Harmer Report'*).

<sup>107</sup> Ibid 15-17.

<sup>108</sup> Ibid 16.

<sup>109</sup> For example, ibid 183, where the Law Reform Commission notes that voluntary bankruptcy 'is ... resorted to by many insolvent debtors to discharge impossible or unmanageable debt burdens and to enable a 'fresh start' to be made.'

<sup>110</sup> For example, ibid 230, 319, 345, 363.

<sup>111</sup> Ibid 200-201.

<sup>112</sup> Ibid 203.

<sup>113</sup> Ibid 235.

<sup>114</sup> Ibid 239. Under the Law Reform Commission's recommendations, a debtor who had been bankrupt in the previous five years would not be entitled to automatic discharge, and would need to apply to the court for discharge: at 236.

<sup>115</sup> Ibid 366-367.

2009, the Attorney-General's Department distributed a short document titled *Proposed Amendments to the Bankruptcy Act 1966* ('*Proposed Amendments Paper*'),<sup>116</sup> the purpose of which was to 'set out some ideas for responding to increasing numbers of bankruptcies and other personal insolvency administrations'.<sup>117</sup> This paper suggested that some restrictions and consequences of bankruptcy 'do not assist in rehabilitating the debtor or result in any greater returns for creditors',<sup>118</sup> and that 'the aim of the system should be to deal quickly with the person's insolvency and get them on track to start contributing once again to the economy'.<sup>119</sup> Specifically, the paper suggested that the goal of providing a fresh start is being hindered by the permanency of the public record of bankruptcy on the NPII.<sup>120</sup> The idea of rehabilitation is also specifically referred to in the context of arguing for a shorter bankruptcy period, where it is suggested that if a shorter period was made available, it would not be available for second time bankrupts, because a person who has failed once, should be expected to learn how to avoid failing a second time.<sup>121</sup> These comments suggest a preference for an understanding of the fresh start that is focused on debtor rehabilitation. However, the proposals for change to the NPII and early discharge have not been implemented.

These reviews by the Law Reform Commission and the paper released by the Attorney-General's Department focus on debtor rehabilitation as a goal of the *Bankruptcy Act*, however, the suggested amendments to facilitate rehabilitation have not been made, or have not been fully implemented.

#### *F Overview of the scope of the fresh start goal in Australia*

The idea of bankruptcy providing a fresh start for debtors is a popular one, and this analysis of the key primary and secondary documents supports the view that one of the objectives of the *Bankruptcy Act* is to provide the opportunity for a fresh start to debtors. The scope of the fresh start to be delivered by the *Bankruptcy Act* is not defined or made explicit in the legislative or judicial documents. However, the overriding emphasis of the legislation and the case law is on a relatively narrow idea of the fresh start, where the focus is on the debtor having a clean slate at the conclusion of bankruptcy, and this is achieved through the discharge of liability for the debts existing at the time of bankruptcy. This is also consistent with the relevant principle for a modern insolvency law, as set out in the *Harmer Report*,<sup>122</sup> and the objectives of the *Bankruptcy Act* as described by the regulator in its Annual Report.<sup>123</sup>

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<sup>116</sup> *Proposed Amendments Paper*, above n 57. Copy on file with the author. It is not clear how widely this document was circulated.

<sup>117</sup> *Ibid* 1.

<sup>118</sup> *Ibid* 1.

<sup>119</sup> *Ibid* 1.

<sup>120</sup> *Ibid* 3.

<sup>121</sup> *Ibid* 2.

<sup>122</sup> *Harmer Report*, above n 106, 16.

<sup>123</sup> Insolvency and Trustee Service Australia Annual Report 2012-13, 70. The most relevant objective is described by the regulator as 'to release insolvent debtors from debt'.

Some cases and the law reviews do provide support for a wider view of the fresh start concept, suggesting that matters such as financial literacy and financial capability, and constraints on the public availability of bankruptcy information are also crucial if a debtor is to receive the opportunity for a fresh start. However, despite these nods to the idea of a rehabilitation-focused fresh start, there has been little change to the legislation to facilitate this wider sense of the fresh start. Thus, the fresh start as it has been implemented in practice is focused on debt discharge, rather than debtor rehabilitation.

#### IV DISCUSSION AND IMPLICATIONS

##### A *Clarifying the fresh start goal*

As discussed above, there is a lack of clarity about the existence and scope of the fresh start goal in the *Bankruptcy Act*, and this will hinder attempts to assess the effectiveness or otherwise of the *Bankruptcy Act*. The examination of the relevant primary and secondary sources above suggests that providing a fresh start for debtors (or the opportunity for a fresh start) is one of the primary goals of the bankruptcy legislations, and that the type of fresh start that is envisaged is a fresh start that is focused on, and delivered by, discharge of liability for the debts existing at the time of bankruptcy. However, this goal is not explicitly stated in the legislation; nor are the other key goals of the *Bankruptcy Act*.

In the absence of an objects clause, the purposes or objectives of legislation can be determined from the text of the legislation. A formal objects clause, however, can provide some clarity and consistency as to scope of the objects or purpose of the legislation. It may also be able to provide some guidance as to how to proceed when there is a potential conflict of goals. A relevant example here is in relation to the question of whether a particular debt should be able to be proved or discharged in a bankruptcy. Non-provability or non-dischargability of a particular type of debt clearly inhibits a fresh start goal that is focused on debt discharge. However, in some cases, such a categorisation may reflect a view that the fresh start goal should be subjugated to another goal of the legislation.<sup>124</sup>

An objects clause has the primary function of assisting in the interpretation of the existing provisions of legislation. It does not give the judiciary any ability to introduce new clauses, or amend existing clauses, that might further the specified objects. However, clarifying the overarching objects of the legislation can potentially provide an impetus to the Parliament to consider whether change is needed to better facilitate the achievement of those objects, and can provide a framework for developing and assessing law reform proposals.

Introducing an objects clause into the *Bankruptcy Act* would provide the opportunity to clarify the key goals of the *Bankruptcy Act* and their scope. Any such clause should include a reference to the fresh start, and some guidance as to the scope or meaning of this goal. To be consistent with the scope of the fresh start goal as it is currently delivered by the legislation, and interpreted by the

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<sup>124</sup> As an example, see the discussion of *Pyramid Building Society (in liq) v Terry* (1997) 189 CLR 176; (whether a contingent debt is provable) in Griggs, above n 5, 57.

courts, the meaning would emphasise debt discharge. In relation to the fresh start goal, an objects clause could, for example, be based on the relevant principle from the *Harmer Report*, that ‘the end result of an insolvency administration ... should be the effective relief or release from the financial liabilities and obligations of the insolvent’.<sup>125</sup> Such a clause would also benefit from some general qualification of the types of debts from which there would be no release.

### *B Assessing the achievement of the fresh start goal*

If, as I have argued, the fresh start in the *Bankruptcy Act* focuses on discharge of debt, the task of assessing the extent to which the fresh start is achieved in practice is a relatively straightforward task, requiring, for example, information on:

- The number of people who exit bankruptcy with non-dischargeable and/or non-provable debts;
- The type and size of any such debts; and
- The number of people who exit bankruptcy free from all debts.

This information on the debts held by those exiting bankruptcy is not currently published or (to my knowledge) specifically collected or collated into one dataset. However, it may be able to be compiled or extrapolated from existing sources of information provided to AFSA and/or bankruptcy trustees during the bankruptcy process. For example, every debtor entering bankruptcy must submit a Statement of Affairs, and this must include information about all secured and unsecured debts; this should include debts that are not provable and/or not dischargeable in the bankruptcy.<sup>126</sup> Further, upon becoming bankrupt, a debtor must provide to the trustee all documents and papers relevant to their bankruptcy.<sup>127</sup> Creditors of a bankrupt will provide a proof of debt to the bankruptcy trustee,<sup>128</sup> and this may also contain relevant information for assessing the extent of non-provable or non-dischargeable debts, at least at the time of entering the bankruptcy.

There are also other existing datasets that are likely to contain information on a debtor’s credit position at the time of entering or exiting bankruptcy. For example, recent amendments to the *Privacy Act 1988* (Cth) will allow for the collection of more comprehensive information about credit commitments than has previously been permitted, including credit accounts held and credit limits on those accounts.<sup>129</sup> And a number of categories of non-dischargeable or non-provable debts will be recorded by the courts (for example, penalties and fines imposed by a court in relation to offences,<sup>130</sup> civil penalties imposed by the *Corporations Act*),<sup>131</sup> or other government agencies (for example, tertiary debts<sup>132</sup>

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<sup>125</sup> *Harmer Report*, above n 106, 16.

<sup>126</sup> See, *Bankruptcy Act* ITSA Form 3: Statement of Affairs.

<sup>127</sup> *Bankruptcy Act* s 77(1)(a).

<sup>128</sup> *Bankruptcy Act* s 84.

<sup>129</sup> See *Privacy Amendment (Enhancing Privacy Protection) Act (Cth) 2012*, Schedule 2 (this includes the introduction of a new Part IIIA on credit reporting).

<sup>130</sup> *Bankruptcy Act* s 82(3).

<sup>131</sup> *Bankruptcy Act* s 82(3AA).

will be recorded by the Australian Taxation Office). With appropriate privacy protections, this information (or subsets of it) could potentially be reviewed and analysed (on a non-identifiable basis) to facilitate an understanding of the extent to which debtors exit bankruptcy free of debts.

There is no guarantee that all of the information compiled from these sources will be complete.<sup>133</sup> However, it can begin to provide a picture of the extent to which a fresh start is achieved at the conclusion of bankruptcy.

Another option would be to collect data and information directly from individuals at the time of discharge from bankruptcy. The regulator has previously commissioned surveys of individuals who enter Part IX debt agreements, and these have informed the various amendments to the regulatory framework for debt agreements.<sup>134</sup> A similar approach could be taken to exploring the achievement of the fresh start.

Collecting and reviewing information about the existence and size of non-provable and non-dischargeable debts will enable an assessment of the percentage of debtors who receive a fresh start (defined as debt discharge) at the conclusion of their bankruptcy. If a significant percentage of debtors do not receive a fresh start in this sense, then attention may need to be given to the categories of non-provable and non-dischargeable debts. Such a review could ensure that the categories are appropriate, and that they mirror a community preference for other goals to prevail over the fresh start goal. In any case, clarity about the scope of the various goals of the bankruptcy legislation is the first step to addressing any conflict between the different goals.

However, information on the economic and social position of debtors after bankruptcy (particularly sometime after bankruptcy) would not be needed for an assessment of the achievement of a debt discharge-focused fresh start. Further, the level of repeat bankruptcies would not be directly relevant to an assessment of achievement or otherwise of the fresh start goal as envisaged here.<sup>135</sup>

### *C The need for a broader review*

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<sup>132</sup> *Bankruptcy Act* s 82(3AB).

<sup>133</sup> This is perhaps particularly the case of information in the Statement of Affairs, many people apply for bankruptcy without seeking advice from the regulator or an insolvency professional (23% of bankrupts in 2011: see Insolvency and Trustee Service Australia, *Profile of Debtors 2011* (2012) 14 <<https://www.afsa.gov.au/resources/statistics/profiles-of-debtors-documents/profiles-of-debtors-2011>>).

<sup>134</sup> See Measured Insights, 'Survey Research into the Experience of Debtors who Lodged their Debt Agreement Proposals with ITSA during the Period 1 November 2007 to 29 February 2008' (2008); The Empower Group, 'Debt Agreement Debtor Research Report' (2004) (copies on file with the author). These reports do not appear to be available on AFSA's website, but some of the findings are discussed in Ian Ramsay and Cameron Sim, 'The Role and Use of Debt Agreements in Australian Personal Insolvency Law' (2011) 19 *Insolvency Law Journal* 168.

<sup>135</sup> Note that the regulator does publish statistics on repeat bankruptcies, see Insolvency and Trustee Service Australia, *Profile of Debtors 2011* (2012) 15.

I have argued above that there is a need for clarity about the scope of the fresh start goal for the *Bankruptcy Act*, and that one way to provide this clarity would be to insert an objects clause into the *Bankruptcy Act*. In relation to the fresh start goal, this should be consistent with the debt-discharge focused idea of the fresh start that is dominant in the primary and secondary materials discussed above. However, there are also a number of references in the key documents to the importance of debtor rehabilitation, a concept that goes beyond the idea of debt discharge to incorporate changes in debtor behaviour, knowledge, opportunities and/or circumstances. In addition, there is often discomfort with the idea that individuals might use bankruptcy on more than one occasion;<sup>136</sup> and this also points to an expectation of debtor rehabilitation through the bankruptcy process. This concern for debtor rehabilitation is not encompassed by the concept of the fresh start as is currently provided, but its existence provides an opportunity to examine whether a wider meaning of the fresh start goal is more appropriate.

Examining the scope of the fresh start goal could be achieved as part of a comprehensive review of the *Bankruptcy Act*. As mentioned above, the most recent complete review of the *Bankruptcy Act* occurred in 1988 (the *Harmer Report*). Although this report came up with the nine principles for an insolvency law, it did not articulate these in the form of specific goals or objects for the *Bankruptcy Act*. Further, despite a number of references and recommendations relevant to debtor rehabilitation in the text of the report, rehabilitation of the debtor does not feature in the nine principles. In addition, the *Harmer Report* took place more than 25 years ago, and there have been significant changes in the economy, in credit markets, and in credit regulation since then. There have been various amendments to the *Bankruptcy Act* in the interim period, but these have often responded to particular issues or cases, and have been described as being ad-hoc or piecemeal,<sup>137</sup> rather than resulting from a considered and holistic assessment of the operation of the *Bankruptcy Act* in its totality.

While ad hoc development of the legislation is necessary if it is to be responsive to legal and economic developments, at some point it becomes appropriate to undertake a comprehensive review.<sup>138</sup> Among other things, a comprehensive review would provide the opportunity for clarification or expansion of the scope of the fresh start goal and other goals for the bankruptcy legislation, and to consider the relationship between the various goals. It would also be an opportunity to review the *Bankruptcy Act* in light of the preferred goals, and the extent to which the current provisions facilitate or inhibit the achievement of the various goals, including the (clarified) fresh start goal. In particular, if there was a preference for a wider rehabilitation-focused fresh start goal, a review could

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<sup>136</sup> See, for example, *Proposed Amendments Paper*, above n 57; *Harmer Report*, above n 106, 236.

<sup>137</sup> See for example, Ramsay and Sim, above n 7, 303; King, above n 5, 657, 688, where King suggests that Andrew Keay's criticism of the history of bankruptcy decision-making in the United Kingdom as 'ad hoc' could apply equally to Australia; Michael Murray and Jason Harris, *Keay's Insolvency: Personal and Corporate Law and Practice* (Thomson Reuters, 2011) 10, who suggest that changes in bankruptcy law have 'often been in response to a particular issue, or case'. See also *ibid* 686.

<sup>138</sup> Murray and Harris have called for 'a rewriting of our personal and corporate insolvency laws': *ibid* 698.

consider what (if any) legislative amendment is needed to better facilitate this fresh start goal.<sup>139</sup>

Finally, a review would be an opportunity to acknowledge the influence of matters outside the *Bankruptcy Act* in influencing the fresh start goal, and would facilitate consideration of any changes to other laws and aspects of social policy that similarly have the potential to affect the achievement of the fresh start goal.

If, as a result of such a review, a wider rehabilitation-focused fresh start became one of the objects of the *Bankruptcy Act*, it will not be enough to examine the extent to which debtors have non-dischargeable and/or non-provable debts at the conclusion of their bankruptcy in order to assess whether this wider fresh start goal is achieved. Instead, the assessment of the fresh start goal for individual debtors will need to consider a wider range of information, and possibly over a longer period of time, having regard to their individual financial position and circumstances in the post-bankruptcy phase. This information may be more difficult to collect, but it is not impossible.<sup>140</sup>

## V CONCLUSION

In Australia's recent past, more than 20,000 individuals have entered bankruptcy each year,<sup>141</sup> and many more individuals (for example, family members) have also been directly and indirectly affected by bankruptcy. Bankruptcy also has widespread effects on creditors, both small and large, and the wider community (including future creditors) more generally.<sup>142</sup> The *Bankruptcy Act* therefore plays a critical role in the economic and social framework.

Given the breadth of the impact of bankruptcy, evaluating the *Bankruptcy Act* against its goals should be a regular focus of politicians and policy makers. But, for such a task, clarity about the goals is needed. This paper has examined one of the assumed goals of the *Bankruptcy Act* – that of providing a fresh start (or the opportunity of a fresh start) to debtors, and argues that, although there is a consensus that the fresh start is a goal, the concept is currently not well defined. Introducing an objects clause to the *Bankruptcy Act* is a relatively straightforward

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<sup>139</sup> For example, the World Bank suggests that attention needs to be paid to the principle of non-discrimination between former bankrupts and others who have not previously been bankrupt: above n 20, *World Bank Report*, 119.

<sup>140</sup> Some examples of studies in the United States examining the achievement of the fresh start include those of Zagorsky and Lupica, who examine the time period over which it takes former bankrupts to 'catch-up' to non-bankrupt peers on various financial indicators: Zagorsky and Lupica, above n 4; and Porter and Thorne, who examine how debtors' view the impact of bankruptcy on their financial positions one year after bankruptcy: Porter and Thorne, above n 12.

<sup>141</sup> There have been more than 20,000 bankruptcies in each year since 2007-08, and this number increased to more than 27,000 in 2008-09 and 2009-10: Insolvency and Trustee Service Australia Annual Report 2012-13 71.

<sup>142</sup> For a discussion of the different interests in bankruptcy, see Andrew Keay, 'Balancing Interests in Bankruptcy Law' (2001) 30 *Common Law World Review* 206, 210-221. For a more expansive discussion on the community interest in bankruptcy, see Karen Gross, 'Taking Community Interests into Account in Bankruptcy: an Essay' (1994) 72 *Washington University Law Quarterly* 1031.

way to provide a clear guidance on the existence and scope of the fresh start goal. To be consistent with the understanding that has been identified in the primary and secondary documents in this paper, any objects clause should reflect a debt-discharge focused fresh start.

However, this need not be the final word. Instead, the somewhat ad hoc development of the *Bankruptcy Act* in the recent past suggest it could now be an opportune time to review the goals of the *Bankruptcy Act* (and indeed the operation of the *Bankruptcy Act* more broadly) and consider whether a fresh start goal that has a rehabilitation-focus would better reflect our complex, consumer society. Amending the *Bankruptcy Act* to include and facilitate such a goal might mean that bankruptcy could provide debtors with something more than a temporary reprieve; it could instead facilitate a real pathway to an improved financial future for many debtors entering bankruptcy to avoid the quagmire of unmanageable debt.