Queensland University of Technology

QUT Law Review

Volume 17 Number 1 2017

Special Issue

Personal Insolvency – A Fresh Start

General Issue – 2017

Queensland University of Technology

QUT Law Review

Volume 17 – Number 1 – 2017

Special Issue: Personal Insolvency – A Fresh Start

General Issue

This issue may be cited as (2017) 17 (1) *QUT Law Review*

October 2017 – Published by Faculty of Law, Queensland University of Technology

Faculty of Law
2 George Street
Brisbane
Queensland 4000
Australia

Table of Contents

Editorial

Special Issue on Personal Insolvency

General Issue 2017

QUT Law Review ISSN: Online-2201-7275
Volume 17, Issue 1, pp. i-iii DOI: 10.5204/qutlr.v17i1.731

GUEST EDITORIAL: PERSONAL INSOLVENCY – A FRESH START

ROSALIND MASON, JASON KILBORN, STEPHANIE BEN-ISHAI, JOSEPH SPOONER*

The international personal insolvency conference, ***A Fresh Look at Fresh Start: The Human Dimension to Bankruptcy*** was hosted by Queensland University of Technology, Brisbane, Australia in September 2016. The conference attracted delegates from a wide-range of disciplines including academics, accountants, economists, financial counsellors, lawyers, regulators, policy makers and non-profit organisations. They came from around the globe bringing perspectives from North America, Europe, Africa, Asia, and Oceania.

While the current focus in much insolvency scholarship or commentary is upon salvaging economic value for large businesses facing financial collapse, the harsh reality is that many more people experience financial stress as over-indebted consumers or 'owners' of micro/small/medium sized enterprises. This conference provided a forum for scholars, practitioners and policy-makers to discuss and present on the human experience of bankruptcy.

This Special Issue of the *QUT Law Review* contains a select number of articles based on papers prepared for the conference. The issue begins with an invited contribution by The Honourable Justice Andrew Greenwood of the Federal Court of Australia and is based upon his Opening Remarks to launch the conference. His article provides a fascinating insight, based upon original research into the court archives, into the bankruptcy of a prominent Australian lawyer, Sir Garfield Barwick. Early in his career at the bar, Barwick was made bankrupt as a result of legal obligations entered into in order to assist a younger brother — just prior to the Great Depression of the 1930s. Despite this, Barwick went on to become a leading figure in Australian and international legal circles as a King's Counsel; Minister of the Crown, including a term as the federal Attorney-General; a lengthy term as Chief Justice of the High Court of Australia; a judge of the International Court of Justice; and an occasional member of the Privy Council. Yet not many students of the law and his judgments would be aware that this 'archetypal self-made man, [who] was a fervent believer in free enterprise, which required "effective competition", and favoured small business'[1] had experienced the impact of bankruptcy on his professional and private life.

The second article, by Professor Iain Ramsay of the University of Kent, explores themes of the conference from a global perspective. Professor Ramsay is well-placed to delineate an

* Rosalind Mason, BA (University of Queensland), LLB (Hons) (University of Queensland), LLM (University of Sydney), PhD (University of Queensland), Professor of Insolvency & Restructuring Law, Centre for Commercial and Property Law Research Centre, Faculty of Law, Queensland University of Technology; Jason Kilborn, JD (magna cum laude) (University of Michigan), Van der Grinten Chair in International & Comparative Insolvency Law, Radboud Universiteit Nijmegen, Professor of Law, John Marshall Law School (Chicago); Stephanie Ben-Ishai, LLB (Osgoode Hall Law School), LLM (Harvard University), Professor of Law, Osgoode Hall Law School; Joseph Spooner, PhD (University College London) Assistant Professor of Law, Department of Law, London School of Economics.

[1] George Winterton, 'Garfield Barwick' in Tony Blackshield, Michael Coper and George Williams (eds), *The Oxford Companion to the High Court of Australia* (Oxford University Press Australia, 2001) 58.

emerging international paradigm on personal insolvency law, notably based on his former role as a co-author of a World Bank Report on the Treatment of the Insolvency of Natural Persons and his current Leverhulme Trust Fellowship, focusing on explanations for the patterns of development of personal insolvency in the US and Europe. The article includes a discussion of recent radical theories of consumer credit in contemporary capitalism and how these radical insights might contribute to future socio-legal research on personal insolvency law.

The next article is based on the conference's opening address by Professor Jay Westbrook, University of Texas Austin. Professor Westbrook, whose distinguished legal scholarship has analysed American bankruptcy law over many decades, reviews the US experience since the controversial 2005 amendments to the American bankruptcy law. Professor Westbrook likewise examines tensions between consumer credit and personal insolvency and suggests a reappraisal of the goals of consumer bankruptcy law in the 21st century. This includes abandoning the idea that bankruptcy law should be used as a collection device for professional creditors in consumer cases. The article discusses various possible approaches for a new reform while emphasising the importance of the continuing role of lawyers and courts in the consumer bankruptcy process.

The human dimension is central to the article by scholars from Leiden University, Jennifer van Kesteren, Professor Jan Adriaanse, and Professor Jean-Pierre van der Rest, a multi-disciplinary team who have undertaken a phenomenological study to gain an understanding of the private, personal and social implications of the legal procedure as experienced by bankrupt entrepreneurs in the Netherlands. While the notion of bankruptcy as a fresh start was a theme of the conference, this paper describes the experience as being comparable to losing a loved one. This paper depicts the subjects undergoing a psychological process similar to mourning — with a lack of empathy, respect and transparency by formal institutional representatives seen by the entrepreneurs as 'emotional punishment'. The mental health implications of bankruptcy and its effectiveness (or lack thereof) in reinvigorating small business entrepreneurs are receiving increasing attention and this article will contribute usefully to both of these areas of cutting edge scholarship.

Moving now to the Asia-Pacific region, Associate Professor Stacey Steele, Melbourne Law School and Associate Professor Jin Chun, Doshisha University Japan, provide a thorough comparative analysis as a basis for some suggestions for reforming Australia's personal bankruptcy law, based on the Japanese experience. At the turn of the 21st century, Japan introduced a new proceeding for individual rehabilitation. By comparing Japanese approaches to discharge, investigation and continuing obligations, including requirements for income contributions, the authors describe the proposed Australian reforms as conservative and not as debtor-friendly as those in Japan. The article also addresses the obstacles of adverse credit histories and enforcement of personal guarantees against entrepreneurs and describes these as problematic for an entrepreneur seeking a fresh start in both jurisdictions.

Next, Trish Keeper, Senior Lecturer, Victoria University of Wellington, examines pension laws and bankruptcy in New Zealand. Given the aging profiles of bankrupts, this issue raises relevant and significant policy issues in respect of whether some, or all, of a bankrupt's pension savings should be available to the estate for the benefit of a bankrupt's creditors. This paper critically examines a recent New Zealand proposal to expose more pension savings to the claims of creditors in bankruptcy, in stark contrast with a worldwide trend in the opposite direction. The basic policy objectives of personal bankruptcy are thrust into stark relief by this proposed incursion into debtors' old-age safety nets. An alternative, more sensible, humane,

and effective approach to sanctioning opportunistic ring fencing of assets available to creditors is proposed.

Finally, issues arising at the intersection of superannuation, taxation and bankruptcy laws are examined by Dr Jennifer Dickfos and Catherine Brown, Griffith University, and Jason Bettles, Partner, Worrels Accounting. Like the preceding paper on pension savings, this paper argues for a need to balance the protected asset status of superannuation funds, a significant personal issue for bankrupts, with other objectives, such as achieving a fair distribution of the bankrupt's assets among creditors.

It has been a pleasure to serve as Guest Editors of this Special Issue and to assist in compiling this selection from an excellent range of papers that contributed to a very successful and stimulating forum on the human experience of bankruptcy. The Guest Editors also thank the many anonymous referees from around the globe who have also assisted in bringing this Special Issue to fruition. The topics examined here are of increasing importance to policy makers worldwide. Several of the papers in this Special Issue have already been cited in major policy analyses by leading institutions such as the World Bank, and we are immensely proud to have played a role in bringing these valuable contributions to the attention of the international community.

QUT Law Review ISSN: Online-2201-7275
Volume 17, Issue 1, pp 1–14 DOI: 0.5204/qutlr.v17i1.723

BARWICK, BANKRUPTCY AND THE HUMAN DIMENSION

THE HON JUSTICE ANDREW GREENWOOD*

The overall theme of this conference is 'A Fresh Look at "Fresh Start": the Human Dimension to Bankruptcy.' The Queensland University of Technology prides itself, rightly, on being a University for the real world. The topics, the subject of this conference, engage that notion in a very direct and contemporary way. However, let me give you an old illustration of a contemporary problem.

I GARFIELD BARWICK

Garfield John Edward Barwick became one of Australia's most successful advocates. He dominated the High Court lists and as we all know, he was appointed Chief Justice of Australia on 27 April 1964 after a successful career in federal politics, upon the retirement of Sir Owen Dixon.[1] He was born on 22 June 1903. He was the eldest of three sons of Jabez Edward Barwick and Lily Grace Ellicott.[2] Jabez Barwick was a printer. He had also once been employed as a journalist working for country newspapers. Garfield Barwick believed that pursuing this occupation brought his father to Moree where he met the Ellicott family and Lily Ellicott. In Moree, Jabez changed his occupation from that of a journalist and became a printer, most likely working in a newspaper printery.[3] He continued to work in the printing industry and ultimately had to abandon his trade as he had become affected by lead poisoning from handling the moveable lead type by which printing was done at that time.[4] Jabez and Lily Ellicott moved to Sydney. Lily Ellicott was a Wesleyan Methodist who attended the Bourke Street Methodist Mission.[5] Both parents believed in the Methodist conception that hard work and discipline lead to the realisation of God's gifts in each individual.[6] As to these matters and other aspects of his

* Justice of the Federal Court of Australia. This is a slightly edited version of Opening Remarks delivered by His Honour at the international personal insolvency conference 2016, *A Fresh Look at Fresh Start: The Human Dimension to Bankruptcy*, (Faculty of Law, Queensland University of Technology, 7 September 2016). This paper was an invited contribution to this Special Issue and hence has not been peer-reviewed.

[1] The remarks at the ceremonial occasion of the retirement of Sir Owen Dixon from the office of Chief Justice of the High Court are recorded at (1964) 110 CLR at (v) and following. Interestingly, the Commonwealth of Australia was represented by the Prime Minister, Sir Robert Menzies. The remarks at the ceremonial occasion of the taking of the oaths of office by Sir Garfield Barwick are recorded at (1964) 110 CLR (xiv). This paper was also published as a speech at the Federal Court of Australia website – http://www.fedcourt.gov.au/digital-law-library/judges-speeches/justice-greenwood/greenwood-j-20160907. The paper will also be published in the Australian Law Journal in December 2017.

[2] Barwick's mother was always affectionately known amongst her family and friends as Lally: Garfield Barwick, *A Radical Tory: Garfield Barwick's Reflections and Recollections* (Federation Press, 1995) 3.

[3] Ibid 4.

[4] Ibid 9.

[5] Barwick described his mother as 'young and vigorous, physically and mentally strong-minded and a good administrator'. He also describes her as a woman who 'had those radical leanings so often associated with Wesleyanism'. He says that both his parents were intelligent, logical and courteous though forceful in discussion. Neither parent was dogmatic: Barwick, above n 2, 5.

[6] Barwick, above n 2, 5.

life, Barwick expressed some reservation about placing reliance upon the accuracy of David Marr's biography, *Barwick*.[7]

Garfield Barwick regularly attended Sunday School in Flinders Street, Darlinghurst and won many prizes in state-wide annual examinations in biblical knowledge. He attended Cleveland Street High School and won a bursary to the famous Fort Street High School.[8] Jabez Barwick's illness and the abandonment of his trade caused the Barwick family to move from their Glenview Street, Paddington home and become shopkeepers in the suburb of Burwood.[9] Barwick's Leaving Certificate results won him a bursary to Sydney University, which paid his fees and provided him with £5 annually for textbooks, and entitled him to free travel on suburban railway between Burwood and Central Sydney.

In 1929, Garfield Barwick married Norma Montier Symons.[10] After passing the Intermediate Certificate, Norma worked full-time in her mother's millinery business. She later managed a second shop for her mother in a neighbouring suburb. These millinery skills would become very important having regard to the events in 1930 that were to befall Garfield Barwick.

Barwick entered Sydney University at 16 years of age.[11] He graduated with a Bachelor of Arts in 1922 at the age of 19. He continued his law studies at the Law School in Phillip Street. He took up Articles of Clerkship with Mr HW Waddell to whom he was recommended by the Dean of the Law School.[12] Mr Waddell had grazing interests in country New South Wales at Merriwa. He went to his country property from time to time and sometimes for up to a week. In these periods, Mr Waddell entrusted important decisions in the conduct of the practice to Barwick. He gained vast experience in the practice of the law. In his third year as an Articled Clerk he was receiving ₤9 9s per week.[13] Barwick planned to go to the Bar. However, he had overlooked the need to register as a 'student at law', a step which had to be effected at least two years before applying for admission to the Bar. Notwithstanding that he had served three years as an articled clerk and had passed all the necessary exams and had acquired an Arts

[7] In the prologue to *A Radical Tory*, Barwick says this at p ix: 'It is not my intent to attempt any rectification of David Marr's text, but I must refute two statements he made about my parents. Firstly, it is said that when my parents met, their families were neighbours and related by intermarriage. … They were not neighbours: none of one family had met any member of the other. The Barwicks lived in the Monaro in the south of New South Wales, principally around Cooma. My father, Jabez Edward Barwick was born on 23 May 1874 at Monga, New South Wales, the son of Edward and Sarah Jane Barwick, nee Warne. The Ellicotts lived around Inverell and Moree in the north-east of New South Wales.' Secondly, as to the suggested distance between Barwick's parents, Barwick observes that his parents were devoted to each other all their lives, enjoyed a successful marriage and presided over a close-knit and happy family.

[8] At Fort Street, Barwick was influenced by Mr AJ Kilgour, the Headmaster, who was a qualified Barrister. Kilgour very much favoured a choice of law or medicine as the career for his students. Barwick had entered Fort Street with an interest in the law and at the end of his school days there he remained committed to following the law: Barwick, above n 2, 8.

[9] They were also encouraged to leave the Paddington house on medical advice due to Garfield Barwick's persistent bronchitis with its complications of asthma. The Burwood premises were in a 'drier climate'. Barwick's parents opened a novelty shop and they lived over the shop.

[10] Norma's father had died while she was very young. Her widowed mother and her grandmother lived above a millinery shop which Norma's mother conducted in Burwood Road, on the opposite side of the railway line to the novelty shop operated by Barwick's parents.

[11] Barwick recognises that he was too young to absorb all the benefits of University life: Barwick, above n 2, 12.

[12] At this time, it was customary for solicitors to ask for substantial premiums when agreeing to Articles of Clerkship. No premium was asked of Barwick by Mr Waddell. Waddell practised in Challis House, Martin Place. His practice was largely conveyancing but there was always some litigious work on hand: Barwick, above n 2, 13.

[13] This was a very significant sum for an Articled Clerk in about 1924.

degree and a Law degree, he nevertheless undertook two further years of studentship rather than apply to the Supreme Court for an exemption. In this period, he worked for a fellow Fort Street lawyer, Mr Roy Booth.

On 1 June 1927, Barwick was admitted to the Bar and commenced a search for chambers in Phillip Street. After many enquiries, Sybil Greenwood (sometimes known, according to Barwick, as Sybil Morrison) agreed to let Barwick share her chambers as a temporary arrangement in Campbell House.[14] Barwick was 24 when he commenced practice at the Bar, 'a man without capital and certainly one unable to pay high rent'.[15] In March 1929, Barwick and Norma Symons were married. Barwick was 26, and by this time, he was receiving 'steady work'.[16] He and Norma bought a cottage at Cheltenham financed by first and second mortgages and exhausting what little capital they had in the process. The feared recession was by now deepening into a depression.

The events I am now about to describe are based upon an examination of all the documents contained in the official file relating to the bankruptcy of Garfield Barwick. The actual file is held by the National Archives of Australia and is in a fragile condition, but the National Archives office has digitised the entire file at the request of the Federal Court,[17] and it is in this format that the entire file has been made available to the author. The file consists of approximately 400 pages of documents, including all the proofs of debt, the affidavits of Barwick sworn on 21 February 1930 and 29 October 1930, the extracts of Barwick's oral examination and the transcripts of cross-examination of Barwick and other witnesses relied upon by him in seeking to resist the making of a sequestration order. It contains the Official Receiver's report and other related court documents.

Garfield Barwick had two younger brothers. The elder, Douglas Frederick Barwick, was six years younger than Garfield Barwick. In September 1928, Garfield Barwick purchased for Douglas the lease (having a term of four years), stock and goodwill of a petrol service station known as the 'Super Service Station' at Parramatta Road, Ashfield for £550. Douglas was 19 years of age. Thus, he was a minor. To enable credit to be obtained for him, the lease, on purchase of the business, was taken up in Barwick's name and credit for the business was extended to Barwick in his personal capacity.[18] Barwick had no part in the management or control of the business, which was carried on by his brother, and a partner, a man named Plumstead.[19] Nor did he derive any profit from the business other than a payment by way of interest on monies made available by him in the purchase and development of the business.[20] In his Public Examination on 4 August 1930, Barwick explained that the purchase price of

[14] Campbell House was a two-storey double-fronted building next door to St Stephen's Church. On the first floor level, WA Holman KC occupied two rooms off a wide central hallway. Once Holman got to know Barwick, he gave Barwick the use of his secretary's room, which formed part of Holman's suite.
[15] Barwick, above n 2, 19.
[16] Ibid 26.
[17] The file is held by the National Archives as a client file of the Federal Court of Australia in view of the Court's jurisdiction in bankruptcy. At the time of the relevant events, the Supreme Court of New South Wales was exercising federal jurisdiction in bankruptcy.
[18] Affidavit of Garfield Barwick sworn 21 February 1930. Some accounts of this foundation transaction describe Barwick as the guarantor of the debts. This is incorrect. The transactions were directly with Barwick.
[19] In his Public Examination of 4 August 1930, Barwick said that he had an understanding with his brother that Douglas was to get a man named Plumstead in as a partner. Plumstead was not to put any money into the partnership with Douglas until Barwick had been paid back. Plumstead was to do the night work until the whole of the monies advanced by Barwick were paid back. Douglas and Plumstead were paid £5 10s each per week out of the business.
[20] Affidavit, Barwick, 21 February 1930, [3]. No interest was ever paid.

£550 was advanced to him by the *Bank of Australasia* as an extension to £1450 of an existing overdraft supported by the security of a deposit of the deeds to a Strathfield property purchased by Barwick out of earnings when employed by Mr Waddell and Mr Booth.[21] The business lost heavily, and in August 1929 Barwick sold the business but was unable to obtain more than a small payment in cash. The balance of the purchase money was represented by a Bill of Sale taken by Barwick from the purchaser over the plant and stock, a mortgage of the lease and the transfer of the purchaser's equity in a block of land.[22]

The business closed, with heavy commitments still outstanding, chiefly, monies due to three large petrol supply companies: Atlantic Union Oil Company Limited ('Atlantic Union Oil'), Vacuum Oil Proprietary Limited ('Vacuum Oil') and Shell Company of Australia Limited ('Shell'). The total liabilities of the business amounted to £2700. The amount due to the three oil companies amounted to £2200.

Before the sale of the business in August 1929, the Bank had called upon Barwick, in May 1929, to substantially reduce the overdraft facility. In order to do that, Barwick approached the three oil companies and sought credit for 60 days on all accounts to enable reductions to be made on the overdraft. The oil companies agreed to the extended credit arrangement. In August, the service station was sold to Arthur Knibb for £2000 on this basis: Barwick took over Knibb's equity in a property at Narrabeen, the equity being valued at £1250; Knibb gave Barwick a Bill of Sale for £750 over the lease and plant and agreed to pay for the stock in cash; Barwick received £220 for the stock. Of that, £160 was paid to Atlantic Union Oil.[23]

Not having provided against the contingency of a loss of this order, and having lost the availability of bank credit formerly available to him, Barwick found himself unable to meet his commitments 'in cash'. He was also unable to sell any property held by him 'even at sacrifice value'.[24] Barwick let the purchaser of the petrol station into possession of the premises. However, the landlord of the service station refused to accept the purchaser as a tenant and refused to assign the lease. The landlord treated Barwick's conduct as a breach of covenant and commenced an ejectment action against Barwick.[25] Barwick maintained in his statement of affairs that he had a good action against the landlord for £750.[26] Between the date of sale of the service station in August 1929 and 9 December 1929, Barwick contracted to sell certain assets which were expected to realise £1500 in cash. The transaction collapsed and on 9 December 1929, Barwick convened a meeting of his creditors and offered an annual payment of £500, suitably guaranteed, in payment of all his debts. The creditors refused the offer and required a Promissory Note for the total indebtedness of £2900 due in six months and appropriately endorsed. Barwick was unable to obtain such a Promissory Note.[27]

On 29 November 1929, judgment was obtained against Barwick by Atlantic Union Oil for £784 0s 1p with interest at the rate of seven per cent. On 7 January 1930, a bankruptcy notice issued and on 8 January 1930 the bankruptcy notice was served upon Barwick at his Chambers now at 164 Phillip Street, Sydney. On 20 January 1930, a petition issued in an amount of

[21] The Strathfield property then had a value of £1650. Barwick's overdraft at the time of purchase of the lease for the service station was between £300 to £400 less than the limit of £1450: Barwick's Public Examination of 4 August 1930.
[22] Affidavit, Barwick, 21 February 1930, [4].
[23] Barwick's evidence at the Public Examination on 4 August 1930.
[24] Ibid [6].
[25] Ibid [7].
[26] The landlord was Andrew Sinclair. He ultimately lodged a proof of debt for £164 6s 9p.
[27] Barwick's evidence at the Public Examination on 4 August 1930, [8]–[11].

£866 9s, based on an act of bankruptcy in failing to comply with the requirements of the bankruptcy notice on or before 16 January 1930.[28]

In his Public Examination, Barwick said that at about the time of the issue of the bankruptcy notice, another meeting of creditors was called. He said that he offered them an assignment in an attempt to protect the lease of the garage but that the creditors would not accept the proposal unless Barwick personally paid the landlord and his solicitor's costs of about £250. On Friday, 24 January 1930, the landlord, in possession, sold the lease for partial recovery of unpaid rent. These remarks of Barwick in the Public Examination are directed to the following matter, which became significant a little later on. A meeting of Barwick's creditors was convened at the offices of Mr Ross at 2.30 pm on 13 January 1930. The preservation of the lease of the service station, as an asset of the estate, required the landlord's claim for rent and legal costs to be paid. Barwick contended, consistent with a copy of a resolution on the file, that a resolution was passed to the effect that in the event that Barwick paid the landlord's unpaid rent and legal costs (about £250 in all) on or before 16 January 1930, Barwick would then execute an assignment of his estate for the benefit of his creditors to Mr AN Ross as sole trustee with power to dispose of the assets of the estate to best advantage. This would avoid a sequestration of Barwick's estate. The resolution then contemplated that failing payment of the rent and costs by Barwick, and failing an assignment to Mr Ross, Atlantic Union Oil would proceed on the basis of the bankruptcy notice served upon Barwick.

Barwick contended that he had reached agreement with the creditors to an assignment, consistent with the resolution, and that a cheque for £250 had been provided to the creditors for payment of the unpaid rent and legal costs of the landlord. The creditors denied that any such agreement had been reached or such a resolution passed. The contended agreement seems not to have been reached (if at all) at the meeting on 13 January 1930. That seems clear enough from the documents on the file. Further meetings of the creditors occurred later in January. Barwick contended that arrangements were struck on or about 23 January 1930 and then acted upon on 24 January 1930 and in the immediate following days and, in particular, 28 January 1930. A further meeting of the creditors occurred on 30 January 1930. Barwick contended that this meeting led to the election to serve the bankruptcy petition the following day. Money was to be advanced to Barwick to fund the arrangement by a man called Vere Terrill. An amount of £250 was provided for the payment of the debt to the landlord and legal costs.

Apart from the debt due to Atlantic Union Oil, Shell was owed £685 13s 7p; Goodyear Tyre and Rubber Co. was owed £160 8s 3p for which they had obtained judgment on 10 February 1930; Commonwealth Oil Refineries Limited was owed £184 9s; Vacuum Oil was owed £707 12s; and the Law Book Company of Australia Limited was owed £25 1s 9p. All of these companies lodged proofs of debt. The Bank of Australasia was owed £1626 7s 10p. The remaining proofs of debt were lodged by trade creditors of the business.

From 23 or 24 January, or at least by 28 January 1930, Barwick maintained that he had an arrangement with the creditors. However, on 31 January 1930, Stafford Smith, the New South

[28] The Bankruptcy Notice and the Creditor's Petition were prepared by Mr NN Chippindall, the solicitor retained by Atlantic Union Oil on all of its collections work. The company's commercial solicitors, Hughes Hughes & Garvin would later take over the petition proceedings against Barwick. Mr Hughes of that firm (the father of Mr Tom Hughes QC), would ultimately act as the solicitor in the petition proceedings resulting in the Sequestration Order of 11 June 1930. He instructed the 'heavyweights' of the day, Mr D Maughan KC and Mr Nicholas, for Atlantic Union Oil. Mr LS Abrahams was retained by Barwick to resist the making of the sequestration order.

Wales credit manager for Atlantic Union Oil served Barwick with the bankruptcy petition issued by that company on 20 January 1930. Barwick was served, according to Smith's affidavit, at his chambers at 164 Phillip Street, Sydney in the afternoon. The bankruptcy petition came on for hearing before the Judge in bankruptcy in the Supreme Court of New South Wales, Reginald Heath Long Innes J, on 17 March 1930. Barwick relied upon his affidavit sworn 21 February 1930 and other material. Having regard to the contended arrangement with the creditors, Long Innes J dismissed the petition.

A curious event then occurred which unleashed a firestorm. Two days later on 19 March 1930, Barwick issued a writ for defamation for £10 000 against Atlantic Union Oil and its national credit manager, David William Dalley-Watkins to whom Stafford Smith reported. Dalley-Watkins removed the matter from the company's collections solicitor, NN Chippindall, and appointed the company's standing commercial solicitor, Mr Hughes (the father of Tom Hughes QC) from Hughes Hughes & Garvin. That firm was appointed to deal with the dismissal of the bankruptcy petition and the new question of the defamation suit. Dalley-Watkins, in cross-examination by Barwick's counsel, LS Abrahams, gave evidence that the change to Mr Hughes was very much in contemplation before the service of the defamation writ. Barwick contended that the three oil companies had entered into an arrangement (perhaps a conspiracy) to damage Barwick by persisting with the service of the bankruptcy petition in the face of the contended compromise. Hughes retained one of the pre-eminent silks of the day, D Maughan KC, for Atlantic Union Oil. The company made an application under section 26 of the *Bankruptcy Act 1924–1927* (Cth) to review and secure the rescission of the order of 17 March 1930 dismissing the bankruptcy petition. Many affidavits were put on for the company.[29] Barwick put on a number of affidavits.[30] As to the application, Mr Hughes described the considerations this way in a document dated 19 September 1930:

> In this case it was necessary to establish to the satisfaction of the Court that a previous Order made dismissing the Petition was made under a misapprehension as to certain material facts and that there was material evidence available that was not called at the previous hearing. This involved attendances not only on those who gave evidence on the previous hearing but on other possible witnesses, a careful perusal and consideration of all the documentary and oral evidence which had been given and a close analysis of the documents and letters relating to the transactions involved and the Judge's notes. …
> In this case there was a direct conflict of evidence as to material interviews and as was anticipated it was alleged by the Debtor's counsel that the witnesses for the Petitioning Creditor had conspired together to concoct evidence since the first hearing of the Petition. This involved extreme precautions to keep all witnesses apart and separate interviews with each of them on all material points, so that no witness was aware of any of the other's evidence. It was essential to attack the credibility of the witnesses for the Debtor particularly VW Terrill and RK Daniel and in order to do this material had to be gathered for their cross-examination as to credit. This necessitated exhaustive enquiries into their past history and many interviews with persons in a position to give information as to their past transactions and associations. Included in these enquiries were interviews with five firms of Solicitors and obtaining and perusing large numbers of documents relating to the association of Terrill with certain transactions of [another company] and litigation concerning that company. In addition to these enquiries

[29] The affidavits included affidavits from Dalley-Watkins, Stafford Smith, NN Chippindall, Matthew Parkin (the Australian credit manager for Vacuum Oil), William Godwin (the assistant company secretary for Atlantic Union Oil), EL Townsend (credit manager for Shell), and AU Ross who attended the creditors' meeting on 30 January 1930.

[30] Affidavits by Barwick; RK Daniel (a financier); and three affidavits of VW Terrill (a person who had agreed to provide financial assistance to Barwick).

> searches were made in the Firms Register and attendances made to obtain copies of transcript in other litigation in which their evidence was disbelieved. …

It seems from the cross-examination of Mr Terrill that Mr Townsend was particularly hostile to Barwick. The following exchange occurred between Terrill and Mr Maughan KC [emphasis added]:

> Q: You made an affidavit in this case eventually, on the 11th April, as to what took place at the Atlantic Union Oil Company's office on 24 January?
> A: Yes I made an affidavit.
> Q: You told Mr Abrahams originally, when you were under examination orally, that you did not get a document signed in writing because you trusted the honour of those present?
> A: Yes.
> Q: In your affidavit of the 29th April, according to you, one at least of those that were present expressed the greatest hostility to Mr Barwick — do you remember that?
> A: Yes.
> Q: Which one was that?
> A: Mr Townsend, mostly.
> Q: And, according to you, he said he would like to see him **on the street**?
> A: Yes.
> Q: And he would like to **put him out of practice**?
> A: Yes.
> Q: He adopted a **very hostile attitude**?
> A: Yes.

Mr Maughan KC then tested the making of the arrangement in this way:

> Q: You told the Court that within 20 or 30 minutes of [Townsend] making those statements, you accepted the document [as to the arrangement] without a signature, relying, as you say, on his moral obligation?
> A: Quite so.
> Q: I suppose, when the document was handed to you, you had a vivid recollection of what Mr Townsend had said within the previous half hour?
> A: Yes.
> Q: Were you surprised when there was any alternative suggestion at all that these three gentlemen, including Mr Townsend, were prepared to make any alternative suggestion or offer?
> A: I was quite surprised for some reasons.
> Q: You tell the Court now that notwithstanding Mr Townsend's attitude at the early part of the [meeting], you were satisfied with his word?
> A: Together with the others. … Yes, I thought it did not matter what disparaging remarks he made about Barwick, he would stand up to his word of honour with regard to the agreement.
> Q: Did you ask any of these gentlemen to date or attest this document?
> A: No.

The application before Long Innes J was heard on 14, 15 and 16 April 1930. In the result, Long Innes J ordered that the order of 17 March 1930 dismissing the petition be 're-heard … on 13 May 1930 in order that [the Court] may consider whether it's said order dismissing the petition should be reviewed rescinded or varied'.[31] Directions were made for the filing of further affidavits. The matter was heard over a number of days. Barwick was cross-examined on 10

[31] See above n 17.

June 1930. He accepted that at the date of filing the petition (20 January 1930) he was insolvent and that his unsecured liabilities were £2742 2s 10p. Barwick also admitted that on 23 January 1930 when Terrill approached Atlantic Union Oil on his behalf to facilitate a discussion about payment of debts, he had no defence to the petition. The following exchange occurred [emphasis added]:

Q: What you are relying on is something which took place firstly on the 24th, and secondly on the 28th January?
A: It occurred subsequent to the 23rd.
Q: What you are relying on as a defence to this petition is an interview on the 24th January reported to you by your agent, and followed by certain action on the 28th?
A: I do not know when the actual petition was served.
Q: You are relying on certain events of the 24th and 28th January as affording you a defence to this petition?
A: Things have happened subsequent to the 23rd.
Q: Your **contention** is that some agreement resulted from those events?
A: I put the **facts** before the Court. I am **not contending anything** at the moment.
Q: You **complain** that on the 31st January the petitioning creditor committed a breach of some agreement by **serving** the petition on you?
A: **Broadly** that would be the position.
Q: They did go on with the petition and it was eventually heard on the 17th March?
A: I do not remember the date.
Q: Approximately **seven** weeks afterwards?
A: Sometime afterwards.
Q: They went on with the petition which they served on you on the 31st January?
A: Yes.
Q: Which you say was in breach of some agreement that had been made?
A: Yes.
Q: The petition then came on to be heard before His Honour and was dismissed, and the bankruptcy proceedings came to an end for the time being. On the 19th you took steps to issue a writ for £10,000 damages?
A: Yes.
Q: Do you **conscientiously** tell his Honour between the 31st January and the 17th March, you suffered damage to the extent of £10,000 by reason of what happened?
A: No.
Q: Your **garage business** had come to an end as a matter of fact **long** before that?
A: It was sold in August or September.
Q: You do **not pretend your practice as a barrister** had suffered damage by reason of these proceedings?
A: **It has.**
Q: Between the 31st January and the 17th March your practice suffered damage?
A: Some damage and that has been accentuated since.
Q: Do you suggest it is anything approaching £10,000 damages you suffered? [Question not pressed]
Q: You went to a meeting of the creditors on the 24th March?
A: Yes.
Q: And you went there according to yourself to plead for some better terms?
A: I asked for a re-consideration, yes I did.
Q: You went there to ask for better terms?
A: Yes.
Q: To get a better and more reasonable bargain?
A: Yes.
Q: Did you say a single word to the creditors then about this **tremendous loss** you had suffered between the 31st January and the 17th March?

A: I did not get a chance. I was put out.
Q: Did you tell them there [were] actually two writs out claiming £10,000 damages from them?
A: **No.**

The reference to whether Barwick was *conscientiously* contending that between 31 January 1930 and 17 March 1930 he had suffered damage to the extent of £10 000 was a carefully framed question as it invoked notions of 'good conscience' before a well-respected equity lawyer and equity Judge, Long Innes J Maughan's cross-examination of VW Terrill, in particular, and also RK Daniel, achieved the outcome Mr Hughes (and counsel) sought to achieve. The cross-examination seriously called into question the credit of the witnesses and thus the reliability of their versions of the events. Although it is not entirely clear from the papers on file, it seems that Barwick was represented on the petition proceedings by Mr LS Abrahams and Mr Ernest Street.

In the result, an order was made on 11 June 1930 rescinding the order of 17 March 1930 dismissing the petition. The order recognises that an act of bankruptcy had been committed by reason of Barwick's failure on or before 16 January 1930 to comply with the requirements of the bankruptcy notice served by Atlantic Union Oil on him on 8 January 1930. A sequestration order was made against Barwick as a person carrying on a business as Super Service Station at Parramatta Road, Ashfield and also practising as a barrister-at-law at 164 Phillip Street, Sydney. Charles Fairfax Waterloo Lloyd was constituted as the Official Receiver of the estate. For those of you with an historical interest in the costs of these things, it is interesting to note that in 1930 Mr Maughan KC's fee on the motion for re-hearing was £32 10s and conferences were charged at £5 10s. The fee on the hearing of the petition was £43 and refreshers were charged at £29 2s per day. The fee on settling the affidavits was £52 9s. Each conference of three hours was charged at £13 2s. The fees charged by the junior counsel were two-thirds of senior counsel's fees.

One of the most powerful images in children's literature is JM Barrie's crocodile, constantly pursuing Captain Hook.[32] The crocodile had swallowed a clock and Hook was conscious of the crocodile's presence by the sound of the 'tick tock, tick tock'. The clever idea that Hook, like all of us, is constantly stalked by devouring time is a powerful image. Barwick must have felt that the impending bankruptcy was pursuing him in a way that might well foreclose his career with the result that he might be 'put out on the street', as Shell would have it. He may also have felt that he was stalked by bankruptcy, as his father Jabez, once he lost his trade and other ventures failed, also became bankrupt.

The administration of the bankruptcy took its course. Barwick's Public Examination occurred on 4 August 1930. On 27 August 1930, he applied for a discharge. The application was listed for hearing on 30 September 1930 before Lukin J,[33] and all the creditors were notified of the application. The hearing was adjourned to 1 November 1930 and judgment was given by Lukin J on 29 November 1930. The Official Receiver published a report on 24 September 1930 and Barwick responded to it by affidavit on 29 October 1930. In the report, the Official Receiver contended that Barwick fell within the elements of section 119(7) of the *Bankruptcy*

[32] Featuring in the play and books by JM Barrie, *Peter Pan or The Boy Who Would Not Grow Up* (1904); *Peter Pan in Kensington Gardens* (1906); *Peter and Wendy* (1911).
[33] The hearing was held at the Supreme Court at Taylor Square. There is a certain irony in the location, as Barwick, as Chief Justice of the High Court would spend much time in the court room at Taylor Square.

Act, most relevantly, paragraphs (b), (c) and (d).[34] As to (b), the Official Receiver contended that neither a cashbook nor a creditors' ledger had been kept properly. As to (c), the Official Receiver contended that in the period September 1929 to June 1930, credit had been obtained from four creditors in an amount of £1604 11s 6p and that in the period January to September 1929, credit had been obtained from nine creditors in an amount of £1273 1s 9p. The statement of affairs shows 31 creditors to the value of £2940 18s. As to (d), the Official Receiver contended that the debts to the value of £1604 11s 6p, as mentioned, had been incurred in circumstances where there was no reasonable or probable expectation of the debts being paid.

Barwick put on material addressing all of the circumstances leading to the bankruptcy and the matters addressed by the Official Receiver. There is no doubt on the basis of that material that Barwick's brother, Douglas, and his partner Plumstead, failed to keep proper records within the business of the service station. Barwick gives an indication of the scope of that problem in these terms:[35]

> 12. In May 1929 my Bank asked me to reduce my overdraft and I found that to do so I would have to get an extension on the current month's bills. This I did and obtained from the majority of the suppliers sixty days credit for that month.
> 13. This caused me to make an examination of the business for the first time and I found that while there was a fair turnover the overhead was out of all proportion and that there had undoubtedly been leakages through the staff, more than one hundred gallons of petrol alone being lost in a week. It then appeared that the business was not making the Eleven pounds odd that my brother and Plumstead were drawing out of the business.

On 29 November 1930, the Court was satisfied that proof had been made by the Official Receiver of, relevantly, the matters contemplated by section 119(7)(b), (c) and (d) of the *Bankruptcy Act*. The Court ordered that Barwick's discharge be suspended for a period of six months and that he be discharged from bankruptcy as and from 1 June 1931. The order was entered on 10 December 1930. Having obtained his Certificate of Discharge as and from 1 June 1931, Barwick made an application to the Official Receiver to purchase his 'Law Library and office furniture' for £65 with a deposit of £25 payable and the balance to be paid at the rate of £8 a month. The proposal was accepted on 17 July 1931.

These matters concerning Barwick's bankruptcy are worthy of examination in a contemporary setting because they demonstrate again that in the right or relevant circumstances, anyone might become bankrupt. The Barwick bankruptcy demonstrates just how confronting the stress and difficulty of bankruptcy can be. Barwick describes the matter:[36]

> Through the good offices of Ernest Street who appeared for me in the sequestration proceedings, the Bar Counsel was assured that I had not myself been trading; no question of my continuing in practice arose. But of course, Norma and I had to begin again. I had to buy our cottage again by arrangement with the second mortgagee, who had foreclosed.

[34] Sub-s (7)(b) contemplates that the bankrupt has omitted to keep such books of account as are usual and proper in the business and as sufficiently disclose transactions and the financial position of the business within the preceding five years; sub-s (7)(c) that the bankrupt has, after knowing himself to be insolvent, continued to trade, or obtained credit to the amount of £50 or upwards; sub-s (7)(d) that the bankrupt has contracted any provable debt without having at the time any reasonable or probable ground of expectation of being able to pay it after taking into consideration his other liabilities at the time.

[35] Affidavit, Barwick, 29 October 1930.

[36] Barwick, above n 2, 26, 27.

> To make matters worse, the Depression deepened. I doubt if anyone who did not pass through it can appreciate the distress it caused. Norma and I suffered along with so many others. To supplement what small income I had I did some coaching of law students and Norma went to work in her trade as a milliner. Our joint efforts and mutual determination to succeed pulled us through, though the depth of the penury we experienced was almost devastating.
>
> The bankruptcy proceedings were not an encouragement to solicitors to brief me, and having to attend to financial affairs had distracted me to no small degree. So, the growth of my practice was much retarded.

Barwick always had a sense of, and an eye to, the human dimension of the way in which the law worked. He was conscious of it in developing his own style of advocacy, which he described in his autobiography:

> I thought I should act on the footing that the jury were intelligent, honest and capable of being instructed in even the most complicated matters of fact and that they could apply principles of law if these were simply expressed; that in general they would listen closely to what counsel and the judge had to say. I thought my task would be to persuade them by logic and good sense. I realized that there is room in appropriate cases to press the jury to give effect to human values where the law seemed not to do so. [37]

II BANKRUPTCY POLICY IN MODERN REGIMES

The concept of a 'Fresh Start' is widely considered a key policy goal in modern bankruptcy regimes. That follows because an *objective*, at least, of bankruptcy is to provide an insolvent person with a release from insolvency and a reintroduction to economic participation. The fresh start objective can be contrasted with what is sometimes described as the 'punitive approach' to bankruptcy which seeks to *deter* debtors from insolvency, or the particularly creditor-focused objective of identifying, gathering in and distributing the debtor's assets efficiently.

There is, perhaps, some taxonomic inconsistency in the use of the term 'fresh start'. The debate about the term engages, in part at least, the extent to which the *personal concerns* of insolvent persons are supported. At one end of that debate, a fresh start focuses upon the speed with which a bankrupt is discharged from his or her debts (the so-called *discharge focused fresh start*). At the other end of that debate, a fresh start comprehends wholesale financial rehabilitation and support for a bankrupt so as to bring about financial *well-being* (the so-called *rehabilitation focused fresh start*). A rehabilitation focused fresh start would generally include education and social services support. The concept of the 'human dimension' of bankruptcy is now increasingly recognised as an important aspect of bankruptcy policy. Plainly, policy needs to consider the personal and emotional cost of insolvency. This is particularly true in the context of the financial pressures and stresses of impending financial dislocation and bankruptcy and its relationship with depression and suicide.

The conference organisers emphasise that this conference is designed to provide a forum for scholars and policy-makers to discuss and examine the human experience and human dimension of bankruptcy. There are a number of sub-themes to be examined in the course of the conference:

- Fresh start: is it just rhetoric or reality?

[37] Ibid 19.

- What are the policy tensions between enabling a fresh start and sustaining commercial certainty and continuity?
- How might personal insolvency law be reformed?
- What are the alternatives to bankruptcy?
- Are there insights which might be derived from a multi-disciplinary approach to the questions?
- What comparative approaches have been adopted by other civil societies?
- What are the perspectives of lenders?
- How does the bankruptcy regime intersect with human rights and how might a properly crafted regime intersect with human rights?
- What are the health effects of over-indebtedness?

A *A Principled Foundation and the Human Dimension*

One of the difficulties in delivering a fresh start, which might properly take account of the human dimension to bankruptcy is dealing with the notion reflected in some of the debates in Australia that bankruptcy is too easy; that insolvent persons can too easily step aside from the consequences of their conduct; that a reduced period of bankruptcy discourages debtors from striking arrangements with creditors to settle debts; that bankruptcy no longer has what some people seem to think is the important social utility of the deterrence effect of an appropriate degree of stigma or shame. Erving Goffman describes 'stigma' as 'an attribute that is deeply discrediting' or 'an undesired differentness' that makes an individual seem 'not quite human'.[38] For my own part, I struggle with the notion that deterrence in the form of stigma or shame provides any principled foundation for a bankruptcy regime.

A *principled foundation* engages an understanding of the objectives of such a regime and the powers, authorities and duties conferred and to be exercised and discharged by the relevant participants in furtherance of the objectives of the regime. Nicola Howell and Professor Rosalind Mason pointed out in 2015[39] that there is very little empirical evidence about the extent or impact of bankruptcy 'stigma' in Australia. Professor Paul Ali, Lucinda O'Brien and Professor Ian Ramsay have also observed[40] that the relationship between the law and social attitudes is difficult to gauge in Australia where the history of bankruptcy law has received less scholarly attention than, for example, in the United States. However, in the last 10 years, a number of studies have been undertaken, particularly in 2010 and 2012; and I note that in 2014 the Australian Research Council funded a study at the Melbourne Law School as part of an ARC linkage project.[41] Scholarly writing and analysis in this area is critical. Universities are places to which society turns for critical thinking, thought leadership and empirical analysis. The Academy must shape the debate and provide a principled foundation upon which policy makers might act, considering the contributions of other disciplines including the professions. This conference comes at a time when interest in bankruptcy scholarship and policy analysis has been growing significantly. Much of the academic literature emphasises that Australian bankruptcy law has unclear objectives that seem to lead to conflicting policies. Several historical accounts of the development of bankruptcy laws stress that bankruptcy has evolved

[38] Erving Goffman, *Stigma: Notes on the Management of Spoiled Identity* (Penguin, 1968).
[39] Nicola Howell and Rosalind Mason, 'Reinforcing Stigma or Delivering a Fresh Start: Bankruptcy and Future Engagement in the Workforce' (2015) 38 *University of New South Wales Law Journal* 1529.
[40] Paul Ali, Lucinda O'Brien and Iain Ramsay '"Short a Few Quid": Bankruptcy Stigma in Contemporary Australia' (2015) 38 *University of New South Wales Law Journal* 1575.
[41] Paul Ali, Lucinda O'Brien and Iain Ramsay, 'Bankruptcy and Debtor Rehabilitation: An Australian Empirical Study' (2017) 40 *Melbourne University Law Review* 688.

to respond to changing economic circumstances but has failed to fully resolve clear objectives. The lack of empirical research is seen as a contributing factor.

B *Examining the Policy Objectives Underlying Bankruptcy Regimes*

The literature suggests three broad objectives. The first is *moral policing*. Historical accounts of English bankruptcy law outline its origins in the 16th century as a quasi-criminal area of the law, enforcing social and moral norms through harsh penalties. The development of a credit dependent capitalist economy is understood as the driver of the emergence of a more liberal regime. However, modern bankruptcy laws continue to contain elements of moral policing, it is said.[42] While Australian policy has become more liberal, it continues to stress the need to avoid abuse and punish unscrupulous debtors. Over the last 20 years, bankruptcy policy in Australia has taken up both these notions and also whether bankruptcies are caused by misfortune or misdeed. In 1991, the Keating Government introduced an early discharge, which was subsequently reversed by the Howard Government in 2002 due, in part at least, to concerns about what was described as debtors 'gaming the system'. Early discharge is again a key proposal of the Turnbull government's innovation agenda.

The second objective is to promote *economic efficiency*, one of the central objectives of modern bankruptcy regimes. The Law Reform Commission's 1988 *Harmer Report*[43] cemented this objective as the central concern of Australian policy makers. The *Harmer Report* positioned insolvency regimes as a commercial process rather than a punishment, with the aim of distributing assets amongst creditors and thereby re-deploying economic value. While recent bankruptcy policy has begun to shift the focus from the creditor to the experience of the debtor, economic considerations represent a primary rationale underpinning the bankruptcy regime.

The third objective is *social welfare*. While economic efficiency remains a core objective of policy makers, the academic literature seems increasingly focused on the human experience of the debtor. This discussion has centred on the discharge versus rehabilitative conceptualisation of the fresh start. While the economic approach is mainly concerned with the re-deployment of resources through discharge, a social welfare approach is more concerned with how bankruptcy impacts the debtor's stress level, family cohesion, health and social standing. Much of this concern is compatible with an economic approach in the sense that effective rehabilitation will reduce social costs and increase economic participation. The distinction is perhaps most clear in the policy debate over the 'homestead exception' — the exclusion of the debtor's residence from bankruptcy proceedings. On the one hand, the family home is likely to be a key asset for the benefit of creditors. On the other hand, losing the family home is likely to lead to stress, family breakdown, and barriers to economic rehabilitation. In giving attention to the importance of the social welfare of debtors much of the literature calls for a more rehabilitative focus in bankruptcy.

Although these three approaches have overlapping elements, they are also often in conflict. A major complaint is that the *Bankruptcy Act* contains no provisions setting out the objectives of the legislation (and thus the regime), which makes it difficult, it is said,[44] to assess whether the statutory regime is achieving its goals. The literature broadly agrees that the objectives of

[42] See eg Iain Ramsay in this edition for discussion of the issue of moral hazard and a policy focus on lengthy payment plans versus debt relief. See also Howell and Mason, above n 39; Ali, O'Brien and Ramsay, above n 40.
[43] Australian Law Reform Commission, *General Insolvency Inquiry* (Report No 45, 1988).
[44] See eg Nicola Howell, 'The Fresh Start Goal of the *Bankruptcy Act*: Giving a Temporary Reprieve or Facilitating Debtor Rehabilitation?' (2014) 14 *Queensland University of Technology Law Review* 29.

bankruptcy laws need to be more clearly defined. I think there is some force in that observation. This issue of the social stigma of bankruptcy is an important matter for policy makers. The issue is clearly linked to the historical development of bankruptcy law and its unresolved objectives. In many ways, it is a case study of how the moral policing objective of bankruptcy continues to linger and conflict with economic and social welfare objectives. Fundamentally, the interest in the social stigma related to bankruptcy is a concern about the ways that bankruptcy laws interact with social and community norms. Bankruptcy laws do not operate in a vacuum. The historical origins of bankruptcy as a quasi-criminal concern, in the early days, means that despite the supposed moral neutrality of modern bankruptcy laws, their effects have wide-ranging social impacts. The social stigma effect is seen as a key social welfare issue as it causes stress and poor health and impedes economic rehabilitation. Social stigma is also increasingly seen as an economic issue as it promotes risk aversion in business, and impedes re-engagement by failed business persons. The academic literature discusses the way legislation facilitates or exacerbates the effect of the stigma of bankruptcy[45] and therefore impedes economic and social welfare objectives. Some examples are the role that professional licensing plays in excluding bankrupts from employment and the establishment of a permanent publicly accessible database of bankrupt persons.

Economic policy has increasingly become interested in the role of the entrepreneur in driving innovation and growth. Policy makers interested in replicating the entrepreneurial culture of places like Silicon Valley have identified insolvency regimes as an important factor in mitigating the risk of business start-ups. Recent policy documents in Australia include a Productivity Commission Report on *Business Set-up, Transfer and Closure*[46] and a proposals paper from the Australian government as part of its National Innovation and Science Agenda ('NISA').[47] Both documents highlight the government's interest in the role of bankruptcy policy in fostering entrepreneurialism. The key recommendation of the Productivity Commission's report is the reduction of the bankruptcy or 'exclusion' period from three years to one year. This recommendation has been taken up by the NISA as its personal insolvency proposal, and the proposal has been put forward for public consultation.

The rationale behind this policy is driven by concern for economic value rather than concern for the human experience. In this respect, it follows closely the precedent set by the *Harmer Report*. The rationale is as follows: first, entrepreneurs assessing the risk of initiating a start-up will factor in the consequences of failure, and shorter bankruptcy periods lower the risk; second, the stigma of bankruptcy contributes to a culture of fear of failure and entrepreneurialism; and third, first time business bankrupts are valuable contributors to the economy and they should be free to use their skills and access credit.

Although the wider academic literature makes reference to the nexus between bankruptcy and entrepreneurialism, it is largely sceptical of its impact.[48] In Australia, business related bankruptcies make up only around 20 per cent of all bankruptcies. The academic literature, which generally focuses on the human dimension, is more concerned with improving the bankruptcy experience for the remaining 80 per cent.

---

[45] See eg Howell and Mason, above n 39, and references cited there; Ali, O'Brien and Ramsay, above n 40.

[46] Productivity Commission, *Business Set-up, Transfer and Closure: Inquiry Report* (No 75, 2015).

[47] The Treasury (Aust), *Improving Bankruptcy and Insolvency Laws: Proposals Paper* (2016) <http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2016/Improving-bankruptcy-and-insolvency-laws>.

[48] See eg Howell and Mason, above n 39; Productivity Commission, above n 46; see also the discussion in this edition, *QUT Law Review*, 17(1) by van Kesteren, Adriaanse and van der Rest.

QUT Law Review ISSN: Online-2201-7275
Volume 17, Issue 1, pp. 15–39 DOI: 10.5204/qutlr.v17i1.713

TOWARDS AN INTERNATIONAL PARADIGM OF PERSONAL INSOLVENCY LAW? A CRITICAL VIEW

IAIN RAMSAY*

This article analyses three issues related to the global spread of personal insolvency laws. First, it outlines the emergence of an international paradigm on personal insolvency law and its central feature of a policy preference for partial repayment alternatives as the norm with residual immediate relief reserved for the deserving poor debtor. Second, it examines critically this paradigm in the light of existing empirical studies of the extent to which personal insolvency law achieves economic and social objectives associated with the fresh start such as financial inclusion. The mixed empirical findings on the success of personal insolvency law in achieving these objectives, particularly for individuals subject to instability of employment or poverty raises further questions about the role of personal insolvency law as a modestly progressive safety net for overindebtedness. The final section of the article considers therefore recent radical theories of consumer credit in contemporary capitalism which conceptualise credit as exploitative and personal insolvency law as a disciplinary and legitimating institution which individualises default and may neutralise collective responses to debt and its wider causes such as limited public support or provision. The article concludes by outlining how these radical insights might contribute to future socio-legal research on personal insolvency law.

I INTRODUCTION

Personal insolvency law became more significant after the Great Recession of 2008 when international institutions identified household debt as a potential systemic risk for the international financial system.[1] The subsequent Eurozone crisis accelerated insolvency law reforms within the European Union ('EU'), which proposed a directive on insolvency and restructuring law in 2016.[2] Emerging economies have also introduced or reformed personal

* LLB (Hons) (Edinburgh University), LLM (McGill University). Professor of Law, University of Kent, Canterbury, UK. This article is a revised version of a keynote address at the QUT Faculty of Law, Personal Insolvency Conference, 8 September 2016. I am grateful to those who commented on the paper at the conference and to Toni Williams and the anonymous reviewers for the *QUT Law Review* for very useful comments.

[1] Susan Block-Lieb, 'Best Practices in the Insolvency of Natural Persons: Rapporteur's Synopsis' (World Bank Insolvency and Creditor/Debtor Regimes Task Force Meetings, Washington DC, 11 January 2011) [17], citing closing remarks of Vijay Tata (Chief Counsel, World Bank LEGPS) '… one of the lessons from the recent financial crisis was the recognition of the problem of consumer insolvency as a systemic risk and the consequent need for the modernization of domestic laws and institutions to enable jurisdictions to deal effectively and efficiently with the risks of individual over-indebtedness….'.

[2] See European Commission, *Proposal for a Directive of the European Parliament and of the Council on Preventive Restructuring Frameworks, Second Chance and Measures to Increase the Efficiency of Restructuring, Insolvency and Discharge Procedures*, Directive 2012/30/EU, COM (2016) 723 final, 2016/0359 (COD). For Latin America see Consumers International, *A Model Law on Family Insolvency for Latin America and the Caribbean* (2011). Colombia was the first Latin American country to introduce a personal insolvency law with discharge as an important aspect. See *General Code of Procedure* (Columbia), Law No 1564 of 2012, Title IV (ss 531ff). Article 40 of the revised UN Guidelines on Consumer Protection states that 'Member states should

insolvency laws.[3] It is not an exaggeration to identify a 'global proliferation' of personal insolvency laws.[4] This article explores three questions related to this phenomenon. First, it outlines the contours of an emerging international paradigm on personal insolvency law, identifying issues which seem to have a transnational salience, such as the promotion of entrepreneurialism through a liberal insolvency law discharge. The article finds partial repayment alternatives to be the preferred policy instrument in this paradigm, combined with residual immediate relief for the deserving poor, sometimes described as No Income No Asset Debtors ('NINAs'). The article highlights both the points of consensus and continuing uncertainties in the paradigm, including the scope of its application to both consumers and traders. Paradigms are a mixture of scholarly ideas and political interests. The Washington consensus is an example.[5] This is also true of personal insolvency law. I do not attempt to document comprehensively the conjunction of interests and ideas shaping the emerging international paradigm; that is the topic of a separate article.

Second, the article examines this paradigm in the light of existing empirical studies of the extent to which personal insolvency law achieves objectives associated with the fresh start, such as increased entrepreneurialism, and financial and social inclusion.[6] These studies represent the second wave of personal insolvency law research. The first wave addressed the demographics of insolvents, the reasons for individuals choosing insolvency and, particularly in the United States ('US'), the question of whether individuals were abusing the system.[7] I suggested in 1997 that research might focus on the longitudinal effects of bankruptcy and the fresh start,[8] and an increasing number of such studies now exist, primarily in the US, but also in Europe, and Australia. Some studies draw attention to the gap between the promise and the reality of insolvency relief for at least a significant portion of the bankrupt population.[9] These studies also question the dominance given to repayment alternatives in the emerging paradigm and raise questions about the role of personal insolvency law in addressing issues faced by NINA debtors. Responses to these findings might include measures to make the fresh start more effective through the reduction of existing disabilities and barriers facing bankrupts,[10]

---

ensure that collective resolution procedures are expeditious, transparent, fair, inexpensive and accessible to both consumers and businesses, including those pertaining to over-indebtedness and bankruptcy cases'.

[3] For example, India (2016), Russia (2015). China may introduce a personal insolvency law within this decade.

[4] See Frank Trentmann, *Empire of Things: How We Became a World of Consumers, from the Fifteenth Century to the Twenty First* (Allen Lane, 2016) 432: 'The global proliferation of bankruptcy laws, finally, is a recognition that overindebtedness is a problem in all affluent societies, including social market and welfare states'.

[5] Sarah Babb, 'The Washington Consensus as Transnational Policy Paradigm: Its Origins, Trajectory and Likely Successor' (2013) 20 *Review of International Political Economy* 268.

[6] Jose M Garrido, 'The Role of Personal Insolvency Law in Economic Development: An Introduction to the World Bank *Report on the Treatment of the Insolvency of Natural Persons*' (2014) 5 *The World Bank Legal Review* 111 (referring to the suicide of farmers in India and social conflict in Hungary over problematic mortgage loans).

[7] The classic US studies from this period are: Teresa A Sullivan, Elizabeth Warren, Jay Westbrook, *As We Forgive Our Debtors: Bankruptcy and Consumer Credit in America* (Oxford University Press, 1989); Teresa Sullivan, Elizabeth Warren and Jay Westbrook, *The Fragile Middle Class: Americans in Debt* (Yale University Press, 2000).

[8] Iain Ramsay, 'Models of Consumer Bankruptcy: Implications for Research and Policy' (1997) 20 *Journal of Consumer Policy* 269, 286. See also Jay Westbrook, 'Empirical Research in Consumer Bankruptcy' (2001–02) 80 *Texas Law Review* 2123, 2147: 'We know very little about consumer bankrupts after they leave the bankruptcy court, except that they rarely file again. … We know little about the financial situation of debtors after bankruptcy…the gaping holes in our knowledge make it hard to evaluate how successful bankruptcy is in providing a fresh start.'; Jean Braucher, 'Consumer Bankruptcy as Part of the Social Safety Net: Fresh Start or Treadmill?' (2004) *Santa Clara Law Review* 1065, 1090.

[9] See below, Part III.

[10] US writers argue for simplification of the process to reduce costs and increase access. See eg Ronald J Mann, 'Making Sense of Nation-level Bankruptcy Filing Rates' in Johanna Niemi, Iain Ramsay and William C Whitford (eds), *Consumer Credit, Debt and Bankruptcy: Comparative and International Perspectives* (Hart, 2009) 243;

more careful screening of those wishing to file for insolvency, or better social and economic policies to address directly the problems associated with insolvency such as job insecurity or limited health coverage.[11] Bankruptcy research functions in this last case as the 'canary in the mine', identifying wider problems in society.[12]

The gap identified between the promise and reality of the 'fresh start' leads to my final topic, reflection on the role of personal insolvency in contemporary capitalism. A conventional view is that the fresh start in bankruptcy is a modestly progressive safety net for addressing over-indebtedness. Certainly, this assumption underlies the emerging paradigm and much contemporary research on personal insolvency law. Since the Great Recession, theoretical writing on the role of credit and debt in capitalism has mushroomed.[13] A few writers[14] have reconceptualised bankruptcy as a disciplinary and legitimating device in a contemporary capitalism defined by debt. Bankruptcy law mediates the contradictions between the imperatives of a contemporary capitalism defined by credit-led accumulation and the inevitable problems of non-repayment for certain groups in society.[15] This perspective challenges the progressive assumptions about insolvency law, and I examine briefly the significance of this perspective for future research on personal insolvency.

II AN EMERGING INTERNATIONAL PARADIGM?[16]

A policy paradigm represents a framework of ideas on the goals of a policy, the instruments that can be used to attain the goals and the nature of the problem at issue.[17] In the area of corporate insolvency law,[18] an international paradigm[19] has emerged since the Asian financial crisis of the late 1990s, when a modified Anglo-American 'rescue culture' was

Ronald Mann and Katherine Porter 'Saving Up for Bankruptcy' (2010) 98 *Georgetown Law Journal* 289, 336: 'the filing patterns suggest a group of debtors for whom the decision to file bankruptcy is deferred by a lack of funds'. See also the suggestions in Nicola Howell and Rosalind Mason, 'Reinforcing Stigma or Delivering a Fresh Start: Bankruptcy and Future Engagement in the Workforce' (2015) 38 *University of New South Wales Law Journal* 1529.

[11] See eg Jacob S Hacker, 'The Middle Class at Risk' in Katherine Porter (ed) *Broke: How Debt Bankrupts the Middle Class* (Stanford University Press, 2012).

[12] Westbrook, above n 8, 2125.

[13] Literature here includes: Wolfgang Streeck, *Buying Time: The Delayed Crisis of Democratic Capitalism* (Verso, 2014); Adair Turner, *Between Debt and the Devil: Money, Credit and Fixing Global Finance* (Princeton University Press, 2016); David Graeber, *Debt: The First 5,000 Years* (Melville House, 2011); Greta R Krippner, *Capitalizing on Crisis: The Political Origins of the Rise of Finance* (Harvard University Press, 2011); Susanne Soederberg, *Debtfare States and the Poverty Industry: Money Discipline and the Surplus Population* (Routledge, 2014).

[14] See below, Part IV.

[15] See Soederberg, above n 13, and discussion below in Part IV.

[16] Some of the material in this section draws on chapter 6 of Iain Ramsay, *Personal Insolvency In the 21st Century: A Comparison of the US and Europe* (Bloomsbury, 2017).

[17] See the classic article by Peter A Hall, 'Policy Paradigms, Social Learning, and the State: The Case of Economic Policymaking in Britain' (1993) 25 *Comparative Politics* 275, 279. A more ambitious concept is that of a transnational legal order: 'the transnational production of legal norms and institutional forms in particular fields and their migration across borders regardless of whether they address transnational activities or purely national ones': Gregory Shaffer (ed) *Transnational Legal Ordering and State Change* (Cambridge University Press, 2014) 6.

[18] See Terence Halliday and Bruce G Carruthers, *Bankrupt: Global Lawmaking and Systemic Financial Crisis* (Stanford University Press, 2010); Susan Block-Lieb, 'Settling and Concordance: Two Cases in Global Commercial Law' in Shaffer, above n 17.

[19] Terence Halliday and Gregory Shaffer (eds) *Transnational Legal Orders* (Cambridge University Press, 2015) 11: 'transnational legal order' defined as 'a collection of formalized legal norms and associated organizations and actors that authoritatively order the understanding and practice of law across national jurisdictions'.

internationalised as part of the international financial architecture of economic development. This order is embedded in the United Nations Commission on International Trade Law ('UNCITRAL') legislative guide on insolvency, providing best practices for assessing a state's insolvency law, and functioning as part of structural adjustment programmes under loan conditionality. In contrast, personal insolvency was viewed historically as not significant internationally in terms of the international financial architecture. Along with the topic of over-indebtedness it raised social, cultural and political issues which were best left to individual states.[20] Until the 1990s, many industrialised nations had no — or limited — personal insolvency systems which provided a discharge of debts. Where discharge was available it was usually limited to traders.[21] However, developments in Europe and elsewhere since the recession of the early 1990s and the subsequent Great Recession of 2008 suggest the contours of an emerging paradigm of personal insolvency.

A policy paradigm assumes agreement on the nature of the problem at issue. The immediate problem addressed by personal insolvency is that of over-indebtedness, but disagreement has existed as to whether factors such as unemployment or individual behaviour through overspending are the primary causes of over-indebtedness.[22] The EU Commission identifies over-indebtedness mostly with unemployment, divorce and illness,[23] while a recent Bank of France study indicates a 'conjuncture of events' as the primary reason (see Table 1). The Insolvency Service in England and Wales identifies both exogenous and individual causes for insolvency (Table 2). These official statistics on reasons for bankruptcy are important politically because they suggest the nature of a policy response, contribute to ongoing political debates, and shape dominant narratives about the nature of failure. However, the limits of the categorisations in these data and their partial construction of the social reality of over-indebtedness mean that they should be treated with caution.[24]

Table 1: France: Principal Causes of Over-Indebtedness 2014

Unemployment or degradation of employment	23
Budget Constrained	17
Routine use of credit	14
Conjuncture of events	41
Intergenerational assistance	5

Source: Bank of France, Study of Paths Leading to Overindebtedness (2016).

[20] See eg Donna McKenzie Skene and Adrian Walters, 'Consuming Passions: Benchmarking Consumer Bankruptcy Law Systems' in Paul Omar (ed) *International Insolvency Law* (Ashgate, 2008) 137: 'hardly any attention has been paid at the international level to the potential global socio-economic impact of consumer over-indebtedness. This contrasts with the global interest in business insolvency and rescue.'

[21] Writing in 2003 we noted that, 'Twenty years ago an academic book about consumer bankruptcy systems around the world would not have been possible. Most countries did not have a consumer bankruptcy system.' 'Introduction' in Johanna Niemi, Iain Ramsay and William C Whitford (eds) *Consumer Bankruptcy in Global Perspective* (Hart, 2003) 1.

[22] Resulting in significant differences between systems for example in relation to access criteria, institutional frameworks, time to discharge and discharge exceptions.

[23] European Commission, above n 2, 4.

[24] I discuss the limits of statistics on reasons for bankruptcy and the various research studies on causes of personal insolvency further in Ramsay, above n 16, 16–24.

Table 2: England and Wales: Bankruptcies by Cause of Insolvency as Recorded by the Official Receiver 2015.

	Non-Trading Cases (n=11095) (%)	All Cases (n=14905∗) (%)
Business related failure	--	25
Living Beyond Means	19	14
Relationship breakdown	16	12
Loss of employment	12	9
Illness/accident	11	8
Reduction in household income or significant reduction in bankrupt's income	24	18
Speculation	1	1
Other	17	13

Source: Insolvency Service, Bankruptcies by age gender and cause of insolvency 2015. https://www.gov.uk/government/statistics/individual-insolvencies-by-location-age-and-gender-england-and-wales-2015>. In 955 cases, the cause was recorded as 'unknown/non-surrender'. These cases are not included in the Table.

After the Great Recession, writers linked individual debt problems to macroeconomic issues.[25] The policy problem now was that significant numbers of over-indebted individuals created a debt overhang and acted as a drag on economic growth. One response was therefore the provision of access to a swift deleveraging of debt. This swift deleveraging narrative was, as I will argue in the next section, initially adopted by the International Monetary Fund ('IMF'), but ran into headwinds in its application within the EU. This debate over the nature of the problem of individual failure to repay suggests that laws will continue attempting to balance debt relief with provisions intended to address moral hazard and individual behaviour.

The goals of individual insolvency policy are encapsulated in the idea of the fresh start but the concept of the fresh start is ambiguous, even in a country sometimes regarded as its source, the US. A fresh start may simply mean being free from the burden of existing debt, but might also include ideas of financial and social reintegration.[26] Promoting entrepreneurialism through a swift fresh start has become an influential idea. Several European states, such as Germany and the Netherlands, promoted social reintegration through the use of independent debt counselling agencies as the primary intermediaries. Individual counselling provided a substitute for rollbacks in welfare provision.[27] Although counselling could be justified in terms of an enabling welfare state which would help individuals to participate again in the labour market rather than receive cash transfers, the limited funding for counselling and patchy national

[25] See Atif Mian and Amir Sufi, *House of Debt: How They (and You) Caused the Great Recession, and How We Can Prevent it from Happening Again* (University of Chicago Press, 2015).

[26] See eg discussion in Margaret Howard, 'A Theory of Discharge in Consumer Bankruptcy' (1987) 48 *Ohio State Law Journal* 1047, 1069, where Howard concluded that 'discharge in the context of non-tort claims should have only one goal — to restore the debtor to economic productivity and viable participation in the open credit economy. This standard calls for making discharge broadly available, since viable economic participation is restored by lifting the burden of impossible debt. No one advocates discharge on demand, however. Thus, some limitation is necessary...'.

[27] See Johanna Niemi, 'The Role of Consumer Counselling as Part of the Bankruptcy Process in Europe' (1999) 37 *Osgoode Hall Law Journal* 409, 411.

coverage, as in Sweden, undercut its potential effectiveness.[28] In contrast, the US and Canada now mandate financial counselling for bankrupts, based partly on a perception that individual financial mismanagement leads to insolvency, as well as the political influence of financial institutions. The EU Directive highlights the economic benefits for investment, lending and promoting consumer demand through a swift discharge.[29] It focuses on the economic rather than social benefits of the fresh start.

Repayment plans with residual immediate relief for the deserving poor represent the preferred instruments for achieving the fresh start while addressing concerns about moral hazard. This represents the most solid aspect of the paradigm. We noted this trend in 2009.[30] It is certainly the continental European model. The development of debt adjustment systems in Europe, often introduced by conservative governments in the 1990s represented an adjustment to a more neoliberal model of the role of the market and social provision.[31] European studies and soft law initiatives during this period outlined an optimal policy for personal insolvency, partly inspired by Chapter 13 of the US Bankruptcy Code.[32] It included the idea of a moratorium or stay, a realistic payment plan, usually no more than four years subject to majority approval by creditors, adequate exemptions determined by member states, professional debt counsellors acting as advisers and administrators, financing partly by creditor levies, with immediate discharge for the hopelessly indebted. By 2009, Jason Kilborn argued that European policymakers were converging on a 'unitary paradigm of consumer insolvency treatment' involving less demanding repayment plans and greater possibilities for the residual discharge of debts.[33] These developments reflect partly a social learning process concerning the fact that many individuals had little payment capacity, and partly state concerns about the public costs of processing debtors. For example, the introduction of the English NINA procedure was driven by a desire to minimise court and government processing costs.

A significant ambiguity in the scope of the paradigm concerns its application to both individual consumers and traders, and whether traders should have a swifter period of discharge than consumers. The promotion of entrepreneurialism through a liberal discharge procedure is an

[28] This was the conclusion of the Hedborg Report in 2013 in Sweden SOU 2013 *Out of the Debt Trap.* I discuss this at greater length in Ramsay above n 16, ch 5.

[29] 'Shorter discharge periods have a positive impact on both consumers and investors, as they are quicker to re-enter the cycles of consumption and investment. This boosts entrepreneurship': European Commission, above n 2, 4. The social aspects of insolvency have less salience in the Directive. The EU Economic and Social Committee had recommended for consumers in 2014 'a free procedure, a moratorium on claims, ability to keep main residence and the possibility of cancelling debts in most extreme situation. The goal is to find a solution that will enable households to avoid social exclusion and where possible to pay off their debts as far as their means allow': see 'Opinion of the European Economic and Social Committee on Consumer Protection and Appropriate Treatment of Over-indebtedness to Prevent Social Exclusion' (Exploratory Opinion) INT/726 Rapporteur-general Reine Claude Mader (2014).

[30] See Niemi, Ramsay and Whitford, above n 10, 7: 'Today most countries sponsor repayment plans, with or without a discharge option upon conclusion, and even common law countries that traditionally have emphasized nearly unconditional access to a discharge procedure increasingly emphasize repayment plans as an alternative.'

[31] See Johanna Niemi, 'Consumer Bankruptcy: Market Failure or Social Problem? (1999) 37 *Osgoode Hall Law Journal* 473, 502.

[32] See Nick Huls, 'Towards a European Approach to Overindebtedness for Consumers in the EC Member States: Facts and Search for a Solution' (1993) 16 *Journal of Consumer Policy* 216; Udo Reifner et al, *Consumer Overindebtedness and Consumer Law in the European Union: Final Report* (Commission of the European Communities, 2003). Huls noted (at 224) that 'our model is constructed as a combination of those elements of European solutions that are promising and some elements from the American bankruptcy code'. He noted in 1993 that over-indebtedness was primarily viewed as an issue in Northern European states but not in Italy, Greece, or Spain. In application of the model 'member states could learn from each other without any interference from Brussels'.

[33] See Jason Kilborn, 'Two Decades, Three Key Questions' in Niemi, Ramsay and Whitford, above n 10, 329.

integral aspect of the emerging international paradigm. The EU Directive of 2016 proposes a maximum three-year discharge period for the honest entrepreneur as part of wider policies to enhance entrepreneurialism in the EU, with the possibility of applying this period to consumers.[34] In Britain, the new Labour government at the beginning of the century embraced entrepreneurialism in the 2002 liberalisation of the English discharge procedure.[35] The shortening of the discharge period in Germany from six to three years in 2014 for individuals able to pay a portion of their debts is also intended to promote entrepreneurialism.[36] Some European countries have recently introduced special provisions to make it easier for entrepreneurs to fail (Sweden, France, Spain). Australia recommends liberalisation of the discharge process to promote entrepreneurialism.[37]

Consumers, the self-employed and small businesses represent overlapping categories of debtors. Many self-employed individuals use personal credit cards to finance their business and mortgage the family home to support a business. In the 'gig economy', with workers no longer employed in traditional 9–5 jobs,[38] the self-employed are little different from employees. Moreover, consumers are, like businesses, encouraged to be responsible risk takers, investing in education or training, and managing their financial future in an increasingly financialised culture.[39] The concept of the individual as an 'entrepreneur of the self' managing one's human capital erodes distinctions between the entrepreneur and the consumer.[40]

A *International Institutions and the Emerging Paradigm*

International institutions have contributed to the development of the contemporary paradigm since the Great Recession. The IMF promoted in some documents the importance of a swift deleveraging of household debt in the wake of the crisis, arguing that such measures would benefit primarily those with a higher propensity to consume (average to lower income consumers) and thus drive a recovery.[41] However this 'swift deleveraging' approach received more muted support in the actual work of the IMF in Europe after the Eurozone crisis, suggesting political resistance by states and other actors such as the European Central Bank. An IMF working paper in 2013 argued from cross-country experience that reforms should

[34] European Commission, above n 2, art 20; and see Recital 15 where the Commission notes that consumer over-indebtedness is a matter of 'great economic and social concern'.

[35] The Insolvency Service Annual Report 2014–2015 states at the outset that 'Entrepreneurialism and a drive for business growth will be accompanied by financial failures as well as successes'.

[36] Frank Fossen quotes the German Minister of Justice stating that the 'reform of insolvency law is one of the most important projects in business law' and that 'those who exhibit the entrepreneurial spirit deserve legal protection that encourages them in their decision to depart into self-employment': Frank M Fossen, 'Personal Bankruptcy Law, Wealth, and Entrepreneurship — Evidence from the Introduction of a "Fresh Start" Policy' (2014) 16 *American Law and Economics Review* 269, 274.

[37] See Productivity Commission, '12.3 Issues in Personal Insolvency', *Business Set-up, Transfer and Closure: Inquiry Report* (No 75, 2015): recommendation 12.1, for a one-year discharge period. Individuals with excess income would be required to make payments for three years (see at 343).

[38] Matthew Taylor, *Good Work, the Taylor Review of Modern Working Practices* (Department of Business, Energy and Industrial Strategy (UK), 2017) < https://www.gov.uk/government/publications/good-work-the-taylor-review-of-modern-working-practices >.

[39] See Neil Fligstein and Adam Goldstein, 'The Emergence of a Finance Culture in American Households, 1989–2007' (2015) *Socio-Economic Review* 1.

[40] But media discourse may still reflect the distinction between entrepreneurs and consumers describing how the former 'bounce back from bankruptcy'. See Sue Tabbitt, 'Bouncing Back from Bankruptcy', *The Guardian*, 29 October 2012, <https://www.theguardian.com/small-business-network/2012/oct/29/bouncing-back-from-bankruptcy>.

[41] See International Monetary Fund, *World Economic Outlook* (2012), and other documents discussed in Ramsay, above n 16, 159.

provide a fresh start for 'financially responsible' individuals, typically after three to five years. It also proposed a swift 'no income no asset procedure' for those with no repayment capacity.[42] This latter procedure recognises the limits of existing European repayment systems where significant numbers of individuals have no repayment capacity and may be unable to pay for accessing the insolvency system in those countries which impose a fee.[43] The idea of a special NINA procedure originated in New Zealand and was implemented in England and Wales in 2009. Writers appeal to this idea as a model for US bankruptcy simplification.[44] The English model is a means-tested administrative procedure involving an online application to the Insolvency Service through a limited number of primarily publicly subsidised[45] 'approved intermediaries',[46] who act as screening agencies checking the eligibility of the debtor.[47] The order can be used every six years. A debtor must inform the Insolvency Service of any change in her or his financial status (for example, increase in income) during the one-year period.[48] The use of the term 'Debt Relief' rather than bankruptcy is intended to avoid the stigma of bankruptcy, which might deter some applicants.[49] The objectives of the procedure are to

[42] See Yan Liu and Christoph B Rosenberg, 'Dealing with Private Debt Distress in the Wake of the European Financial Crisis: A Review of the Economic and Legal Toolbox' (IMF Working Paper, No 13/44, 2013). See also International Monetary Fund, Spain: 2013 Article IV Consultation: Selected Issues (IMF Country Report, No 13/245, 2013) 25. The IMF persuaded Cyprus to adopt a law which includes: a three-year discharge for bankruptcy; the possibility of a restructuring plan in relation to secured and unsecured debts subject to approval of 75 per cent in value of creditors; a no income no asset programme with discharge after one year for individuals with debts under €20 000. See also Greece, *Memorandum of Understanding between EU and Greece* (2015) 18–19,
<http://ec.europa.eu/economy_finance/assistance_eu_ms/greek_loan_facility/pdf/01_mou_20150811_en.pdf>.
India has adopted a no-asset procedure in its recent reform. See the *Insolvency and Bankruptcy Code 2016* Part III Chapter 11 introducing a 'fresh start process' for debtors with limited income, assets and debts. The debtor is discharged after six months (s 92).

[43] See in Canada: Stephanie Ben-Ishai and Saul Schwartz 'Bankruptcy for the Poor?' (2007) 45 *Osgoode Hall Law Journal* 471.

[44] See eg Ronald J Mann, 'Making Sense of Nation-Level Bankruptcy Filing Rates' in Niemi, Ramsay and Whitford above n 10 243–4; Elizabeth Warren et al, *The Law of Debtors and Creditors: Text, Cases and Problems* (Wolters, Kluwer, 7th ed, 2014) 320. But see Angela K Littwin, 'The Affordability Paradox: How Consumer Bankruptcy's Greatest Weakness May Account for Its Surprising Success' (2011) 53 *William and Mary Law Review* 1933. See also Hermie Coetzee and Melanie Rostoff, 'Consumer Debt Relief in South Africa — Should the Insolvency System Provide for NINA Debtors? Lessons from New Zealand' (2013) 22 *International Insolvency Review* 188.

[45] Citizens Advice, a registered charity, is the major intermediary. Citizens Advice aims 'to provide the advice people need for the problems they face' and improve the policies and principles that affect people's lives', a research and campaigns agenda known as 'social policy', <https://www.citizensadvice.org.uk/about-us/>. It receives the majority of its funding from central government and each local bureau may also receive funds from institutions such as the National Lottery. A central office provides expertise, but it relies heavily on volunteers in local bureaux. Its website indicates that there are '338 individual charities… Of the 28 500 people who work for the service, over 22,000 of them are volunteers and nearly 6,500 are paid staff'.

[46] See *Debt Relief Orders (Designation of Competent Authorities) Regulations 2009*, reg 3(2)(b)(i).

[47] Access is limited to individuals with non-exempt assets below £1000, a vehicle valued at less than £1000, unsecured debts less than £20 000, and no more than £50 in surplus income, based on a formula tracking reasonable expenditures of individuals in the bottom income quintile. Data indicate that about 1 per cent of applications are rejected by the Insolvency Service with further information requested in about 5 per cent of cases. Individuals must pay for the service (£90) with £10 going to the approved intermediary. Access is barred to individuals who have entered into a transaction at an undervalue or given a preference within the previous two years, and debtor behaviour can be sanctioned through a DRO restriction order. A restriction order may be made either through the court, or an undertaking by the debtor to the Insolvency Service. A broad discretion exists to make such an order where it is appropriately structured by a list of factors such as 'incurring, before the date of the determination of the application for the [DRO], a debt which the debtor had no reasonable expectation of being able to pay': see *Insolvency Act 1986*, sch 4ZB(2)(h).

[48] *Insolvency Act 1986*, s 251J(5).

[49] This description was proposed in a 2004 research paper on administration orders where the authors noted that 'some of the people we interviewed were very resistant to the idea of bankruptcy, and were deterred by the stigma

provide debt relief for those who are unable to pay the costs of accessing bankruptcy (approximately £700) and to prevent financial exclusion.[50]

In 2013, the World Bank, after recognising the international significance of consumer insolvency in 2011,[51] published a *Report on the Treatment of the Insolvency of Natural Persons*.[52] This document did not outline best practices,[53] but recognised the dominance internationally of payment plans as a condition of relief.[54] It was implicitly critical of long repayment plans imposed on individuals with no repayment capacity as in Germany (six years) and Sweden (five years). Although individuals may be given a 'zero repayment plan' in these jurisdictions, they are not discharged until the end of the plan. The World Bank report, like the IMF, also highlighted the problem of the NINA debtor, the individual with no assets or repayment capacity or resources to pay for insolvency. German studies suggest that 80 per cent of debtors on plans are *nullinsolvenz*, that is, they have no capacity to make repayments over the six-year waiting period.[55] In Sweden, approximately 40 per cent of debtors on the five-year restructuring plans have no repayment capacity.[56] Figure 1 shows the rise in France of *rétablissement personnel*, providing an immediate discharge to individuals with no likelihood of repaying their debts. The World Bank Report also recognised the issue of moral hazard in a bankruptcy system, but concluded that there was a danger that focus on this issue could

---

they would face given the relatively small sums of money they owed … A simplified debt procedure would therefore seem more appropriate for people on very low incomes that are unlikely to increase. This could be called something other than bankruptcy, to overcome the stigma that people feel, and differentiate it from the full bankruptcy procedure.' Elaine Kempson and Sharon Collard 'Managing Multiple Debts: Experiences of County Court Administration Orders among Debtors, Creditors and Advisors' (DCA Research Series 1/04, Department for Constitutional Affairs (UK), July 2004).

[50] 'Part 5 [of the *Tribunals Courts and Enforcement Act 2007*] introduces a package of targeted measures that improve and extend the range of solutions available to assist debtors with relatively low income and debts. Those solutions seek to promote financial inclusion and are targeted, in particular, at those who are disproportionately affected by debt and are generally least able to deal with a range of creditor demands.' United Kingdom, *Parliamentary Debates*, House of Lords, 29 November 2006, HL Vol.687, col.766. 'DROs were introduced in April 2009 following research that identified that there were people in long-term debt difficulties who had nothing to offer their creditors and who could not afford to make themselves bankrupt. Delivered in partnership with the professional debt advice sector, DROs provide low-cost easy access to debt relief for those overwhelmed by relatively low levels of unmanageable debt. They are designed to provide a fresh start for the most vulnerable people trapped in debt.': United Kingdom, *Parliamentary Debates*, House of Commons, 9 November 2010, c7-8WS (Edward Davey). Lady Justice Hale has described the procedure as 'a new and simplified way of wiping the slate clean for debtors who are too poor to go bankrupt': *Secretary of State v Payne* [2011] UKSC 60, 63.

[51] See, Block-Lieb, above n 1, [17] '[R]ecent events suggest that the expansion of access to finance, the extension of modern modes of financial intermediation, and the mobility and globalization of financial flows may have changed the character and scale of the risk of consumer insolvency in similar ways in many different economies'.

[52] See, World Bank, *Report on the Treatment of the Insolvency of Natural Persons* (2013). This was the work of a small group of academics, (the author was a member of the drafting committee, chaired by Jason Kilborn), within the context of a World Bank Task Force comprised of lawyers, government representatives, academics, judges (primarily US bankruptcy judges), and representatives of UNCITRAL.

[53] The reasons were the potential diversity of cultural, and social issues associated with personal insolvency. World Bank above n 52, [12]. While these reasons have some weight, the approach taken by the Report was also driven by political factors. The Bank wished to publish a report quickly, and any attempt to state best practices might result in the project being taken over by UNCITRAL. See discussion in Ramsay, above n 16, ch 6.

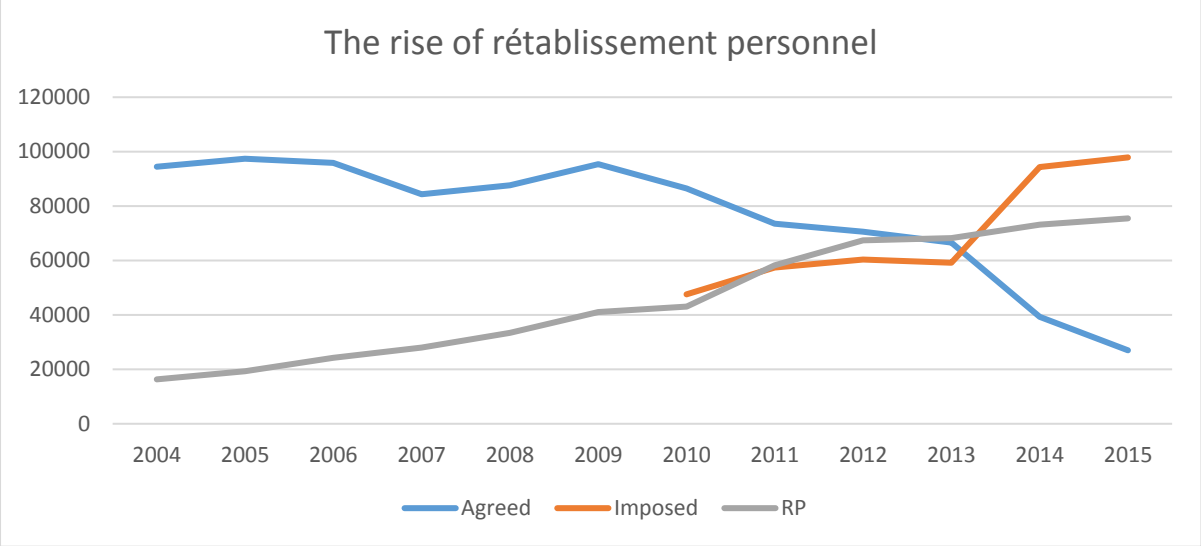
[54] World Bank, above n 52, 134.

[55] Information provided by Jan Heuer citing 2015 statistics on over-indebtedness where 46 per cent of debtors are unemployed, 37 per cent without formal job qualifications, 38 per cent with debts below 10 000, 29 per cent with debts between 10 000 and 25 000, 48 per cent with incomes below 900 euro a month: Jan Heuer, 'The New Poor Person's Bankruptcy: International and Comparative Dimensions' (Workshop presentation, University of Kent, 28 April 2016) on file with author.

[56] See Ramsay, above n 16, ch 5.

overshadow the many benefits of debt relief, and existing evidence did not suggest moral hazard was a significant problem.[57]

Figure 1: France: The rise of rétablissement personnel 2004–2015



Source: Bank of France: Annual Overindebtedness Statistics

B *Are Anglo-Saxon Systems Different?*

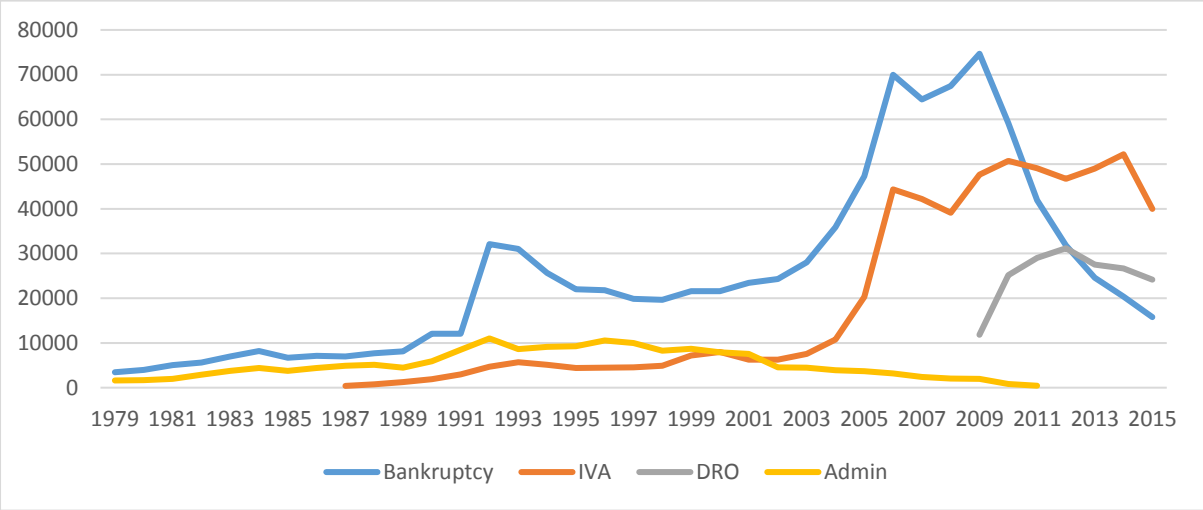
It might be argued that Anglo-Saxon systems do not fit the paradigm of a preference for repayment plans, given the historic role of straight bankruptcy providing a bankruptcy discharge without the necessity of an income repayment order. Moreover, individuals in Anglo systems may choose their insolvency solution, whereas states such as Germany impose a standard solution on debtors. These differences might suggest the persistence of legal origins in creating difference.[58] However, common law systems have witnessed the rise of formal repayment alternatives, for example the Individual Voluntary Arrangement ('IVA') in England and Wales (Figure 2) promoted by entrepreneurial debt intermediaries, the consumer proposal in Canada (see Figure 3),[59] or the debt settlement arrangement in Australia (Figure 4).

[57] World Bank, above n 52, [113]–[119].

[58] Rafael La Porta, Florencio Lopez-de-Silanes and Andrei Shleifer, 'The Economic Consequences of Legal Origins' (2008) 46 *Journal of Economic Literature* 285.

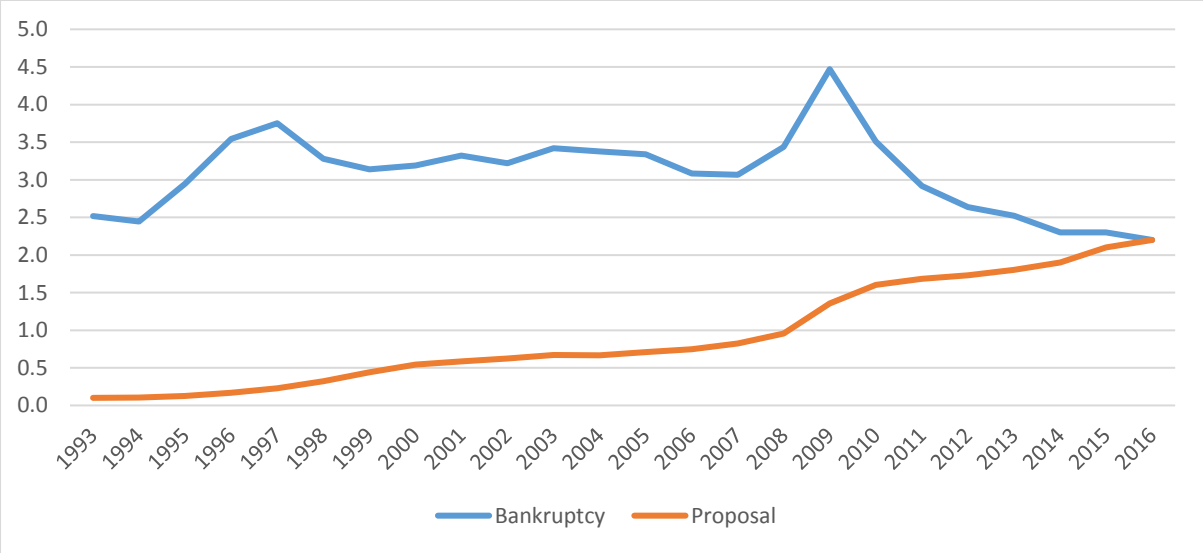
[59] The increase in Canada is partly a function of the increase in 2009 of total unsecured debt permitted in a proposal from CAN$75 000 to $250 000. Evidence also exists of increased steering by intermediaries towards debt repayment rather than straight bankruptcy. See Office of Superintendent of Bankruptcy Canada, *Review of Licensed Insolvency Trustee Business Practices in Relation to Administration of Consumer Insolvencies* (2017) <https://www.ic.gc.ca/eic/site/bsf-osb.nsf/eng/br03754.html>. See the comparative discussion of repayment alternatives in Jean Braucher, 'A Law in Action Approach to Comparative Study of Repayment Forms of Consumer Bankruptcy', in Niemi, Ramsay and Whitford, above n 10, ch 16.

Figure 2: England and Wales Bankruptcy, IVAs, Debt Relief Orders, 1979–2015 (Administration Orders 1979–2011)



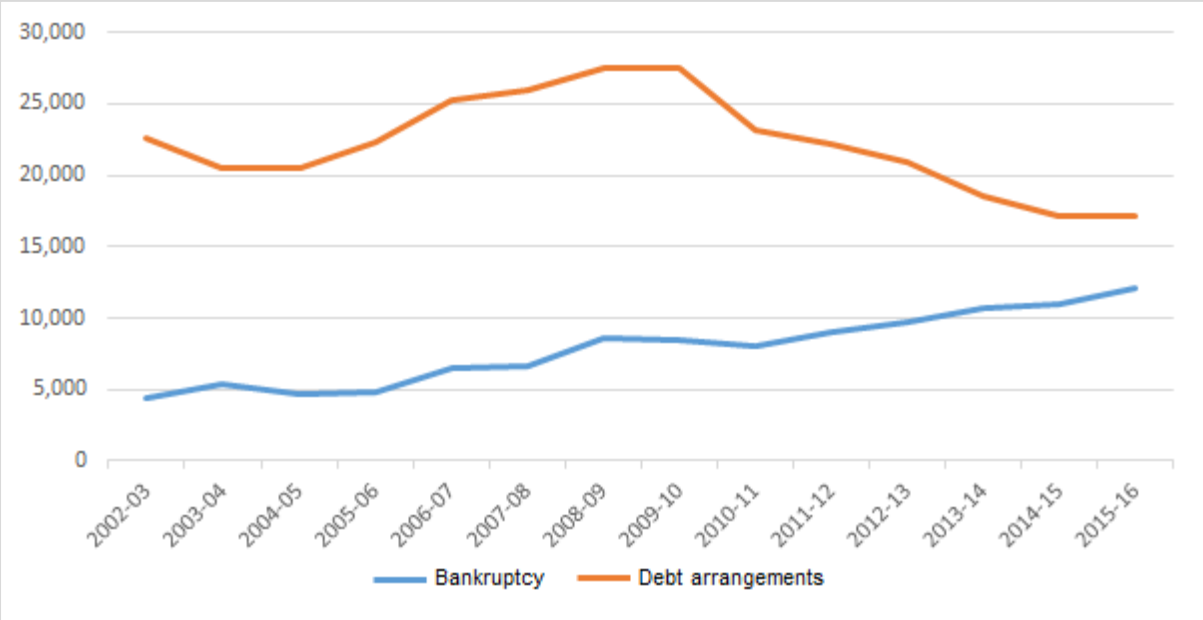
Source: Insolvency Service England and Wales, Annual Insolvency Statistics

Figure 3: Canada Bankruptcies and Proposals per 1000 Capita 1992–2016



Source: Office of Superintendent of Bankruptcy, Canada. Note that the ceiling for debt in consumer proposals increased from CAN$75 000 to CAN$250 000 in 2009.

Figure 4: Australia, Debt Arrangements and Bankruptcy 2002–2016



Source: Australian Financial Security Authority, Annual Personal Insolvency Statistics

---

The UK, Canada and Australia have also introduced 'surplus income' requirements so that individuals may be making payments for up to three years after they are discharged. Even in the US, the non-dischargeability of significant debts such as student loans and the use of re-affirmation agreements mean that individuals may continue to repay debts notwithstanding the discharge.[60] US legislators have historically demonstrated a preference for Chapter 13, the partial repayment alternative, as the primary remedy for consumer debtors at least since the *Bankruptcy Reform Act 1978*, even if in practice this preference was frustrated by debtor choice and the reality of debtors' circumstances.[61] In the UK, government as well as insolvency professionals share a master narrative of 'can pay should pay'. The major professional body, R3, is lobbying for an extension of the standard bankruptcy discharge period to three years, with a swift discharge reserved for the deserving poor under the Debt Relief Order ('DRO').[62] Straight bankruptcy is a suppressed political alternative[63] for debtors in the UK.

---

[60] The US Supreme Court noted that the 2005 amendments were based on an ideology of 'can pay, should pay'. See, Kagan J in *Ransom v FIA Card Services, N. A* 562 U.S. 61, 64 (US Supreme Court, 11 January 2011): 'In particular, Congress adopted the means test — [t]he heart of [*Bankruptcy Abuse Prevention and Consumer Protection Act 2005*'s] consumer bankruptcy reforms… and the home of the statutory language at issue here — to help ensure that debtors who can pay creditors do pay them.'

[61] See, Ramsay, above n 16, ch 2.

[62] R3, *The Personal Insolvency Landscape; A Way Forward for Formal Debt Relief* (2014) <https://www.r3.org.uk/media/documents/policy/policy_papers/personal_insolvency/R3_Personal_Insolvency_Landscape_Jan_2014.pdf>.

[63] In 2015, the UK Financial Conduct Authority found in research on debt management companies, that few individuals had knowledge of the different options, and conceptualised bankruptcy as an extreme and stigmatising option. Advisers often downplayed bankruptcy as an alternative remedy. They often reinforced customers' initial reluctance to consider bankruptcy and played on misconceptions about it to deter them from this alternative. The FCA reported 'many instances where customers were recommended very long-term debt management plans (often many decades...) when debt relief solutions are likely to have been more appropriate but adequate information and advice [were] not provided': Financial Conduct Authority, 'Quality of Debt Management Advice' (Thematic Review TR15/8, June 2015) [4.55] <https://www.fca.org.uk/publication/thematic-reviews/tr15-08.pdf>. In one

This emerging paradigm of the primacy of repayment plans assumes that such an approach is economically and socially beneficial and in Part III, below, I examine existing empirical studies on the effectiveness of existing personal insolvency systems in achieving a fresh start. As a preliminary, one characteristic is the *increasing* length of plans in common law jurisdictions. Thirty years ago, conventional wisdom was that a plan in excess of three years would often fail,[64] but plans are now written for five years or more as in the case of the IVA.[65] It is not clear whether this is economically or socially beneficial.[66] Completion rates of repayment plans raise concerns,[67] and the absence of any repayments by many debtors on plans in countries such as Sweden and Germany suggest the need for a swift discharge for many debtors. Constructing the NINA process as a residual programme does not seem to fit the reality of these systems where substantial numbers of debtors seem to have no repayment capacity. Braucher, surveying studies of repayment alternatives in North America, Australia and Europe in 2009 concluded that existing data, while 'spotty' suggested that these alternatives had high costs in relation to debt repayment and 'significant rates of failure to achieve a discharge'.[68] Almost no knowledge existed on whether repayment plans were effective treatments for over-indebtedness or simply left 'many debtors struggling financially and perhaps in other ways too'.[69] In many countries this question remains unanswered.

III CONTEMPORARY EMPIRICAL RESEARCH ON THE 'FRESH START'

The 'fresh start' is a central objective of personal insolvency law in many countries. The absence of significant assets in most individual bankruptcies undercuts the significance of the traditional bankruptcy objective of equitable distribution of assets among creditors. The World Bank outlines several objectives associated with the fresh start: encouraging entrepreneurialism; increased productivity; promoting financial and social inclusion; reducing health and welfare costs; encouraging responsible lending; and maximising economic activity.[70] The EU Commission identifies 'reduced consumption, labour activity and foregone growth opportunities' with over-indebtedness, arguing that shorter discharge periods will

---

case, a debt adviser failed to correct a debtor's misconception about the effects of bankruptcy and recommended a debt management plan lasting 125 years! Firms often had incentive structures for selling debt solutions.

[64] The Cork Committee concluded in 1982 that the maximum duration of the proposed Debts Arrangement Order should be three years since 'it is clear from the Judicial statistics relating to administration orders that debtors are unlikely to maintain the discipline of instalment payments over periods in excess of three years and we therefore recommend this period as the norm': Insolvency Law Review Committee (UK), (Cork Committee), *Insolvency Law and Practice: Report*, Cmnd 8558 (1982) [313].

[65] See Insolvency Service, *Individual Voluntary Arrangements Outcomes 1990–2015* (27 January 2017) 1 <https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/586485/IVA_Outcomes_2015_-_web.pdf>, noting that over '10% of IVAs registered in 2009 and 5% in 2008 were still ongoing, having started around 7 or 8 years earlier'. In Canada, a recent study of consumer proposals indicated an average length of 4.4 years. This represents an increase from the norm of three years in the 1990s and early 2000s. See Vyacheslav Mikhed and Barry Scholnick, 'Consumer Proposals in Canada after the 2009 Legislative Amendments to the BIA' (Research Paper, Office of Superintendent of Bankruptcy, Canada, 2015) 43 <http://www.ic.gc.ca/eic/site/bsf-osb.nsf/eng/request.html?Open&id=90541C27F538E96485257F7F0060F37C&p=1>.

[66] See Jean Braucher, 'A Law-in-Action Approach to Comparative Study of Repayment Forms of Consumer Bankruptcy' in Niemi, Ramsay and Whitford, above n 10, 333. Braucher suggested three criteria for evaluating repayment systems: creditor repayment, debt relief, and treatment of debt problems.

[67] Insolvency Service data in England and Wales indicate a failure rate of 30–40 per cent for IVAs: Insolvency Service, above n 65. Studies in the US have pointed to high failure rates for Chapter 13 plans. The study by Mikhed and Scholnick, above n 65, indicates a failure rate of 23 per cent in Canada.

[68] Braucher, above n 66, 353.

[69] Ibid.

[70] Other benefits include proper account valuation, reducing wasteful collection costs, concentrating losses on more efficient and effective loss distributors. See World Bank, above n 52, [400] for summary.

permit consumers to re-enter the 'cycle of consumption'.[71] Given these objectives, the task of research must be to determine whether existing systems achieve them. At the outset, it must be stated that this is a challenging research question. Bankrupts are a difficult group to study, and longitudinal data requires following individuals over a reasonable period of time. Moreover, in order to draw firm conclusions about the effect of personal insolvency law, one should ideally have a control group of similarly situated individuals who have not experienced insolvency.

The US tradition of the liberal 'fresh start' is an obvious site for testing the effectiveness of the fresh start. Several US studies question the efficacy of the existing fresh start under both Chapter 7 and Chapter 13. Porter and Thorne found that one year after bankruptcy filing, 25 per cent of Chapter 7 bankrupts were struggling to pay routine bills and 33 per cent had a similar financial situation to that when they filed bankruptcy.[72] They noted that the Brookings Institution had reached a similar conclusion in their study of bankrupts in the mid-1960s. A key factor differentiating those in continuing financial difficulties from other bankrupts was the absence of an adequate and steady income.[73] A bankruptcy discharge did not solve this problem, because employers might not hire an individual who had filed for bankruptcy notwithstanding the prohibition in bankruptcy law on discrimination against bankrupts. Thus, although bankruptcy seemed to provide a fresh start for the majority of bankrupts, Porter and Thorne concluded that for others it was a 'temporary refuge' from continuing income problems.[74]

Other studies suggest that bankrupts may continue to suffer financially for a substantial period after bankruptcy. Zagorsky and Lupicka concluded on the basis of a comparative study of filers and non-filers that for filers it 'took many years to restore financial well-being'.[75] Han and Li concluded that bankrupts have less access to unsecured credit such as credit cards after bankruptcy and were more likely than other consumers to use expensive credit sources. Although this high cost did reduce over time, filers were still more prone to face financial hardship ten years after filing.[76] They concluded that 'for many bankrupt households, debt discharge alone failed to provide a long-run improvement in their financial health'.[77] More recent research suggests that the seven and 10-year bankruptcy 'flags' on a credit file had a

[71] European Commission, above n 2, 4.
[72] Katherine Porter and Deborah Thorne, 'The Failure of Bankruptcy's Fresh Start' (2006) 92 *Cornell Law Review* 67, 'We found that just one year post bankruptcy, one in four debtors was struggling to pay routine bills, and one in three debtors reported an overall financial situation similar to, or worse than, when that debtor filed bankruptcy. Our analysis of these data demonstrates that steady and sufficient income is the key to improved post-bankruptcy financial health. Factors that cause household income to decline, such as unemployment and underemployment, illness or injury, and old age, undermine the chances of financial recovery. These data reveal the limitations of bankruptcy as a social safety net and highlight the fragile economic situations of American families. We conclude that bankruptcy is an incomplete tool to rehabilitate those in financial distress.'
[73] *United States Bankruptcy Code*, Protection Against Discriminatory Treatment, 11 USC § 525.
[74] Ibid 70.
[75] See Lois R Lupica and Jay L Zagorsky, 'A Study of Consumers' Post-discharge Finances: Struggle, Stasis or Fresh Start?' (2008) 16 *American Bankruptcy Institute Law Review* 283.
[76] See Song Han and Geng Li, 'Household Borrowing after Personal Bankruptcy' (2011) 43 *Journal of Money, Credit and Banking* 491; Song Han and Wenli Li, 'Fresh Start or Head Start? The Effects of Filing for Personal Bankruptcy on Work Effort' (2007) 31 *Journal of Financial Services Research* 123; Ethan Cohen-Cole, Burcu Duygan-Bump and Judit Montoriol-Garriga, 'Who Gets Credit after Bankruptcy and Why? An Information Channel' (2013) 37 *Journal of Banking and Finance* 5101 (limited debt availability immediately after bankruptcy, but increased availability after 18 months).
[77] Han and Li (2011), above n 76, 514.

substantial impact on credit availability, with increases in credit scores and credit balances after the flags were lifted.[78]

It is often assumed that debtors do not obtain credit after bankruptcy because of the limits of available credit supply. Porter questions this conventional wisdom, citing studies which demonstrate that a significant credit market exists, targeting recently discharged bankrupts. She concludes that many debtors who have experienced bankruptcy do not borrow on credit cards because of the painful experience of bankruptcy.[79] This undermines the fresh start objective of facilitating re-entry to the credit market.

Empirical studies of Chapter 13, which permits an individual to cure arrears on a home mortgage and repay a portion of debts over three to five years have questioned its benefits. Studies document low completion rates (on average about one third of filers obtain a discharge) and a failure by many individuals to save their homes, which is often a reason for filing for Chapter 13.[80] One recent study, using a logistic regression analysis of national data from the 2007 Consumer Bankruptcy project, concludes that the majority of individuals do not complete plans under Chapter 13, that Chapter 13 does not act as a home-saving device, and generally delays rather than prevents foreclosure. Chapter 13, the authors conclude is 'profoundly inefficient'.[81]

These socio-legal studies contrast with an econometric study by Dobbie and Song,[82] which followed the trajectory of individuals in Chapter 13 from 1992 to 2005 in terms of subsequent earnings, mortality rates, and home foreclosure. Using a randomised methodology,[83] which allowed for the existence of a control group, the authors found that over the first five post-filing years those at the margin who were granted Chapter 13 bankruptcy protection were significantly better off financially in terms of income,[84] and had a significantly lower mortality rate and home foreclosure rate than those denied bankruptcy protection. The difference between the groups is represented by the significant deterioration in those who did not obtain bankruptcy protection rather than gains by those granted protection. Those who filed successfully for Chapter 13 have similar pre- and post-filing earnings. Therefore, bankruptcy

[78] See, Will Dobbie et al, 'Bad Credit, No Problem? Credit and Labour Market Consequences of Bad Credit Reports' (Staff Report, Federal Reserve Bank of New York, 2016) <https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr795.pdf?la=en>.

[79] See Katherine Porter, 'Life After Debt: Understanding the Credit Restraint of Bankruptcy Debtors' (2010) 18 *American Bankruptcy Institute Law Review* 1.

[80] See eg, Sullivan, Warren and Westbrook, above n 7, 217; Scott F Norberg and Andrew Velkey, 'Debtor Discharge and Creditor Repayment in Chapter 13', (2006) 39 *Creighton Law Review* 473, 476; William C Whitford, 'The Ideal of Individualized Justice: Consumer Bankruptcy as Consumer Protection, and Consumer Protection in Consumer Bankruptcy', (1994) 68 *American Bankruptcy Law Journal* 397, 411; studies cited in Braucher, above n 66, 335–6; and Katherine Porter, 'The Pretend Solution: An Empirical Study of Debtor Outcomes' (2011) 90 *Texas Law Review* 103. But see Henry E Hildebrand III 'A Response to a Pretend Solution (2011) 90 *Texas Law Review* 1, criticising the methodology which limited interviews to individuals who had failed in Chapter 13. Porter indicates that, for 70 per cent of filers saving the home is the principal reason for choosing Chapter 13.

[81] See Sara S Greene, Parina Patel and Katherine Porter, 'Cracking the Code: An Empirical Analysis of Consumer Bankruptcy Outcomes (Legal Research Paper no 2016-46, University of California Irvine, 2016) 1.

[82] Will Dobbie and Jae Song, 'Debt Relief and Debtor Outcomes: Measuring the Effects of Consumer Bankruptcy Protection' (2015) 105 *American Economic Review* 1272.

[83] Bankruptcy filers are randomly assigned to judges who vary in their rates of granting bankruptcy protection. They were therefore able to investigate individuals at the margin who might randomly be confirmed or rejected. After discarding data relating to bankruptcy offices with a single judge and certain other factors which prevented random assignment, the authors' data represented 26 per cent of Ch 13 filings during this period.

[84] Marginal recipient of Ch 13 earning $5 562 more than marginal dismissed filer.

appeared to mitigate the effects of a financial downturn for an individual preceding bankruptcy.[85] The study also suggests that bankruptcy protection might increase incentives to continue to work, through its protection against wage garnishment.[86] Economic stability might be promoted,[87] because individuals do not have incentives to go underground, or move state to avoid wage garnishment, and are protected against immediate home foreclosure. The authors conclude that Chapter 13 bankruptcy protection provides significant benefits for debtors.[88]

The contrast between the findings of this study and previous socio-legal studies is striking. Thus, although many individuals do not receive a discharge in Chapter 13, according to Dobbie and Song they have a better post-bankruptcy experience than those not granted protection. These US findings on Chapter 13 and Chapter 7 suggest that some debtors do benefit from these chapters, but for at least a minority of debtors the costs of bankruptcy may be high and it may not be addressing continuing problems of inadequate or insecure income.[89] Sullivan, Warren and Westbrook also suggest that the stigma of bankruptcy may have increased over time as greater media publicity is given to filings and the importance of maintaining a good credit score. A potential bankrupt may now fear the cost to her or his credit reputation, in a similar manner to the historical fear of disapproval by one's neighbours and community.[90]

European studies of the longitudinal effects of personal insolvency relief are limited. No recent systematic studies exist in England and Wales, a jurisdiction which liberalised the bankruptcy discharge in 2002 by reducing the period from three years to one year. The English Insolvency Service evaluated the impact of this reform, concluding in 2007 that although a swift discharge did have immediate emotional benefits, bankrupts still faced difficulties in re-entering the financial market because there were no changes in lending and credit reference policies.[91] The concept of stigma was associated by bankrupts with problems obtaining a bank account, being unable to repay creditors, and the effects on their credit rating.[92]

The few empirical studies of continental European repayment plans are troubling. A qualitative longitudinal analysis of individuals on debt restructuring plans in Finland indicates that individuals continued to live at a low subsistence level one year after the payment plan had ended.[93] A pilot study of individuals who had used the Swedish debt restructuring system

[85] '[B]ankruptcy protection mitigates the long-term consequences of financial shocks that might otherwise harm debtors but does not confer any benefits in the absence of a financial shock': Dobbie and Song, above n 81, 1292.
[86] The authors tested this by analysing the effects in states with different wage garnishment laws.
[87] Tested through analysis of probability of individual working in the same industry, and on probability of worker in baseline county.
[88] Dobbie and Song, above n 82, 1274.
[89] Hacker, above n 11.
[90] See Teresa A Sullivan, Elizabeth Warren and Jay Westbrook, 'Less Stigma or More Financial Distress: An Empirical Analysis of the Extraordinary Increase in Bankruptcy Filings (2006) 59 *Stanford Law Review* 213, 242; Elizabeth Warren and Amelia Warren Tyagi develop the theme that stigma may have increased. See 'The Myth of the Immoral Debtor' in Elizabeth Warren and Amelia Tyagi, *The Two Income Trap: Why Middle-Class Parents are Going Broke* (Basic Books, 2003).
[91] See Insolvency Service, *Enterprise Act 2002—the Personal Insolvency Provisions: Final Evaluation Report* (2007) [30]: 'Rehabilitation of bankrupts is being stifled by a lack of change in lender and credit reference agency policies, which, despite earlier discharge, will continue to deny bankrupts access to various types of financial products.'
[92] Insolvency Service, *Attitudes to Bankruptcy Revisited* (2006).
[93] 'In Finland, of those debtors who have implemented a payment plan, over 40% described their subsistence as poor when asked 1 year after the payment plan had ended.' See Tuula Linna, 'Consumer Insolvency: The Linkage between the Fresh Start, Collective Proceedings and the Access to Debt Adjustment' (2015) 38 *Journal of Consumer Policy* 357, 372.

during the period 2003 to 2008[94] found that 34 per cent did not think it had given them a fresh start,[95] although a majority responded that debt relief had provided a solution to their financial problems. Finally, recent Australian research questions whether bankruptcy provides significant benefits for disadvantaged and low income, individuals since it fails to address the structural causes of financial hardship. Ali, O'Brien and Ramsay conclude that, while bankruptcy provides many benefits, they are unevenly distributed with 'access to adequate income' playing a critical role in rehabilitation.[96]

The promotion of entrepreneurialism is part of the personal insolvency paradigm but studying the effects of bankruptcy law on entrepreneurialism throws up the difficulty of identifying 'entrepreneurs'. Entrepreneurialism is associated with innovation but studies often use self-employment as a proxy. Self-employment is a category which may be over-inclusive as a proxy for innovation, ranging from individuals who are 'very self-sufficient to extremely vulnerable'.[97] It may include individuals who were formerly employed and are in precarious positions with low incomes and few social protections. A widely cited econometric study does indicate a correlation over time between the liberality of the bankruptcy discharge, and levels of self-employment.[98] However, the study does not comment on the quality or innovative nature of the self-employment which is encouraged. Another study suggests no connection between insolvency and innovative entrepreneurship.[99] The English Insolvency Service found no connection between the liberalised discharge procedures in 2002 and business start-ups (used as a proxy for entrepreneurialism).[100] Moreover, while a more forgiving bankruptcy law may permit more marginal high-risk business activity it may also result in higher credit costs for all entrepreneurs,[101] in terms of interest rates and collateral requirements. In the US, more homeowners in states with high homestead exemptions are likely to own a business, but may pay higher interest rates for credit.

US bankruptcy law is the inspiration for European policy makers wishing to promote entrepreneurialism through bankruptcy. 'Fail fast, fail cheap and move on' is a mantra

[94] The Swedish restructuring system requires a five-year period of rehabilitation irrespective of ability to make any payment.

[95] See generally Richard Ahlstrom, S Edstrom and M Savemarkt, *Is Debt Relief Rehabilitative? An Evaluation of Debt Relieved Persons' Health, Life Quality and Personal Finances Three Years After Conducted Debt Relief* (The Swedish Consumer Agency, 2014).

[96] See Paul Ali, Lucinda O'Brien and Ian Ramsay, 'Bankruptcy and Debtor Rehabilitation: An Australian Empirical Study' (2017) 40 *Melbourne University Law Review* 688, 725; Paul Ali, Lucinda O'Brien and Ian Ramsay, 'Bankruptcy, Social Security and Long Term Poverty: Results from a Survey of Financial Counsellors and Consumer Solicitors' (2016) 44 *Australian Business Law Review* 144.

[97] Mies Westerveld, 'The "New" Self-Employed: An Issue for Social Policy' (2012) 14(3) *European Journal of Social Security* 15, 19, referring to the analysis by Martine D'Amours and Stephane Crespo, 'The Dimensions of Heterogeneity Among Own Account Self-Employed: Elements for a Typology' (2009) 59 *Industrial Relations* 459. See Guy Standing, *The Precariat: The New Dangerous Class* (Bloomsbury, 2011).

[98] See John Armour and Douglas J Cumming, 'Bankruptcy and Entrepreneurship' (2008) 10 *American Law and Economics Review* 303.

[99] David M Primo and Wm Scott Green, 'Bankruptcy Law and Entrepreneurship' (2011) *Entrepreneurship Research Journal* 1(2) <https://search-proquest-com.ezp01.library.qut.edu.au/docview/1435441928?accountid=13380>. This study used two measures: self-employment and different levels of venture capital within a state. The latter was intended to capture the 'innovative' nature of entrepreneurialism.

[100] See Insolvency Service, above n 91, 41–2 citing statistical analysis conducted by Department of Business, Innovation and Skills.

[101] See Aparna Mathur, 'Beyond Bankruptcy: Does the US Bankruptcy Code Provide a Fresh Start for Entrepreneurs?' (2013) 37 *Journal of Banking and Finance* 4198. Business owners who have declared bankruptcy are charged higher rates and are more likely to be denied a loan. Owners of previously bankrupt firms are less likely to own credit cards.

associated with Silicon Valley but socio-legal study of bankrupt entrepreneurs in the US does not always provide an optimistic picture of individuals 'bouncing back' in business.[102] Lawless notes the mythology in the US of the founders of Google who financed their business initially through 'all of our credit cards and our friends' credit cards and our parents credit cards'.[103] Bankruptcy law may aspire to facilitate this type of high-risk, high-reward business but Lawless cites Shane's text *The Illusions of Entrepreneurship*[104] which notes that most small businesses fail; only a few are established in high tech industries; and they contribute only a modest number of jobs. A more forgiving bankruptcy law for self-employed individuals is certainly justifiable for similar reasons to those applicable to consumers, but the evidence is not overwhelming on its promotion of entrepreneurialism.

A *Research on NINA Programmes*

Little systematic research exists on the success of schemes designed specifically to provide a swift fresh start for those with few assets or income. In England and Wales, women represent the majority of users of the Debt Relief Order ('DRO'). Many are sole parents and unemployed. They owe debts to central and local state creditors and public utilities, as well as private creditors.[105] Reductions in income and increases in expense dominate the reasons for filing a DRO (Table 3).

Table 3: England and Wales: Causes of Debt Relief Order 2015 (Multiple Causes)

Business failure		0.74
Illness accident		22.9
Increase in household expense		11.9
Living beyond means		15.5
Loss of employment		11.5
Relationship breakdown		14.8
Significant Reduction in household income		33.3
Other		6.5
Unknown		0.9

Source: Insolvency Service.

[102] See Robert Lawless, 'Striking Out on Their Own: The Self-Employed in Bankruptcy' in Porter, above n 11, ch 6.
[103] Ibid.
[104] Scott A Shane, *The Illusions of Entrepreneurship* (Yale University Press, 2008).
[105] An early survey by the Insolvency Service noted that the profile of debtors accessing the DRO system was primarily 'low income, predominantly unemployed individuals with an average of six creditors; over 53 per cent of debt was owed to banks, building societies and credit card companies': Insolvency Service, *DROs Initial Evaluation Report 2010* (2010). More informal data since the recession suggest that public creditors may now be more significant: see eg Anne Pardo et al, *Unsecured and Insecure* (Citizens Advice, 2015).

A government review in 2014–15 did gather information from approved intermediaries and others on its operation. The consensus was that the 'current system is working well'.[106] Clients of intermediaries indicated that the DRO had improved their mental and physical health. The Order also had a positive impact on 50 per cent of debtors' relationships with their families.[107] However, little evidence exists as to the economic and financial impact of the order. Sixty-one percent of debtors in a non-random online survey indicated that they had not wished to access credit after the DRO, with one commenting that the experience of the DRO has 'taught them a lesson about borrowing in the future'.[108] An earlier pilot study of bankruptcy had also found that a significant portion of bankrupts communicated a reluctance to borrow in the future,[109] and Porter identified the same theme in her 2010 US study.[110] The DRO could not only be performing a 'responsibilising' or disciplining function, but also undermining the objective of consumers re-entering the credit market. Further preliminary non-random research on social media suggests that individuals are often concerned about the effect of a DRO on their credit rating, with some regretting the effects it may have on their ability to obtain credit.[111] Evaluation of the similar 'No Asset' procedure in New Zealand concluded that the benefits of the procedure, while significant, might be short term, addressing immediate debt problems but not more general budgeting skills among the debtors interviewed [112].

These special means-tested procedures may increase access through reduced costs but their relatively stringent access controls suggest a continuing fear among policy makers about moral hazard and opportunism in insolvency. The Insolvency Service also has an interest in minimising its costs in administering NINA insolvencies. It devotes modest resources to the DRO and covers its costs through the user fee, with advice agencies (the approved intermediaries) bearing the majority of the costs of screening individuals.[113]

---

[106] See Department of Business, Innovation and Skills, *Insolvency Proceedings: Debt Relief Orders and the Bankruptcy Petition Limit—Call for Evidence; Analysis of Responses* (2015). 'The responses to both the call for evidence and the survey of users showed that debt relief orders are thought to be working well and have provided an important additional route for debt relief for vulnerable people, with benefits for mental health and family relationships as well as allowing a fresh financial start': United Kingdom, *Parliamentary Debates*, House of Commons, 15 January 2015, c30-31WS (Jo Swinson).

[107] Insolvency Service, above n 105, 14. The Insolvency Service conducted a non-random survey, and 72 per cent of respondents had been through the DRO process.

[108] Ibid 18.

[109] John Tribe et al, 'Bankruptcy Courts Survey' (on file with author) 57: 'a sizeable proportion of individuals who are no longer willing to borrow…. If rehabilitation is a key objective of our personal insolvency law…then this response is troubling'.

[110] Porter, above n 79.

[111] These comments are based on analysis of Netmums (UK) threads (www.netmums.com): 'Anyone done a debt relief order?' (142 posts): 'Debt Relief Order please help' (12 posts); 'Debt Relief Order' (15 posts). DROs remain on a debtor's credit file for six years.

[112] See Ministry of Economic Development, *Evaluation of the No-Asset Procedure: Final Report* (2011) 3–4. One article suggests reforming the NAP in New Zealand to require mandatory participation by debtors in counselling. See Trish Keeper, 'New Zealand's No Asset Procedure: A Fresh Start at No Cost?' (2014) (3) *QUT Law Review* 79.

[113] See Insolvency Service *Annual Report and Accounts 2015–16*, House of Commons Paper No HC 482, (13 July 2016) 85, which indicates a surplus of £415 000 in 2015–16. The major advice agency, Step Change, argued in its submission to the review of the DRO in 2014 that 'the current £10 payment to competent authorities for each DRO is nowhere close to the actual cost of advising on and processing a DRO application. This funding situation is not sustainable in the long term…'. It indicates that the 'cost of completing a DRO application is £190': Step Change Debt Charity, Submission to the Insolvency Service Consultation Paper: *Insolvency Proceedings: Debt Relief Orders and the Bankruptcy Petition Limit*, 2014, 12. The English model contrasts with New Zealand where the absence of screening agencies results in a high percentage of rejected applications by the state Insolvency Trustee Service (over 25 per cent). See Ministry of Economic Development, above n 112, 47 which indicates that

Although not a study of bankrupts, a longitudinal qualitative study of low income individuals in England who had obtained debt advice in 2007 and 2011 provides intriguing results.[114] This group would often meet the requirements for a DRO. At the end of the project in 2015 just over a third described themselves as 'debt free',[115] half described themselves as 'managing' their debt, and a small number saw little possibility of moving out of debt. Those who were debt free did so either through bankruptcy, inheritance or increased income with a very small proportion doing so through saving and cutting back. Seven participants became debt free through bankruptcy; four remained debt free at the end. The authors concluded that bankruptcy represented 'a breathing space' for some but for others was simply a 'temporary respite in a longer story of indebtedness'.[116] Bankruptcy was a temporary change in a long term experience of problems where income does not meet outgoings.[117] The authors conclude that debt advice and financial literacy were of some value, but greater priority should be given to addressing structural problems of low wages, limited social security, and health issues. According to the authors, 'wilful non-payment and financial mismanagement are, in fact, minor concerns' for those on low incomes.[118] They also suggested that insufficient attention was currently given to understanding the trajectory of debt careers rather than merely providing a static picture of over-indebtedness and its causes.

These preliminary findings suggest several reasons for further study of the NINA debtor. First, the DRO and similar procedures focus on a generally low-income group which may provide a challenge for the fresh start objective, since debtors may be suffering from continuing income problems. Studies in the UK indicate three different types of poverty: individuals who have a one-off transient experience of poverty; those experiencing recurring poverty and those in persistent poverty.[119] The poor are 'not a homogenous and essentially static population'.[120] A DRO may therefore be effective for some groups, but is possibly unnecessary for those with a transient experience of poverty. Second, the majority of users of the English process are female and often sole parents. Social reproduction[121] in contemporary capitalism, remains women's work. If wages stagnate and social supports are reduced, social reproduction may depend on high cost credit. Study of the DRO provides a window onto this phenomenon, which could be linked to study of similarly situated households who have not used a DRO. Third, it provides

---

the primary reasons for the high levels of rejection are incomplete applications, debts higher than the statutory ceiling and objections by creditors.

[114] Gaby Atfield, Robert Lindley and Michael Orton, 'Living with Debt After Advice: A Longitudinal Study of People on Low Incomes' (Friends Provident, 2016) 22: Fifty-nine participants were recruited in 2007 from not-for-profit advisers Citizens Advice, National Debtline and three community-based advice providers. Fifty-three were recruited in 2011 from individuals with mortgage arrears, some of whom had sought advice.

[115] Ibid 9: the authors indicate that their definition of 'debt free' must be qualified: 'Some participants described themselves as debt-free when they clearly were not entirely without debt, having overdrafts, credit cards and mortgages. Some also owed money to family members, but they had no debts for which they were being pursued by creditors'.

[116] Ibid 31.

[117] Ibid 9.

[118] Ibid 66.

[119] Noel Smith and Sue Middleton, *A Review of Poverty Dynamics Research in the UK* (Joseph Rowntree, 2007) 3.

[120] Ibid.

[121] Defined broadly as 'a key set of social capacities: those available for birthing and raising children, caring for friends and family members, maintaining households and broader communities': Nancy Fraser, 'Contradictions of Capital and Care (2016) 100 *New Left Review* 99.

an opportunity to study the intersection of private law regulation of debt, and housing and welfare policy and administration.[122]

B *Summary*

The following points arise from analysis of the empirical studies in this section. First, bankruptcy does seem to provide benefits for some individuals but not others. This might seem a trite observation but further research to identify relevant groups who may benefit would be useful. Further longitudinal studies are necessary of the trajectory of individuals into over-indebtedness, the role of bankruptcy as an intervention in the process, and the subsequent experience of the debtor. Typologies of the debtor career may emerge from such studies. The Money Advice Service in the UK for example has attempted to outline different categories of the over-indebted, including 'struggling students, benefits dependent families, worried working families, stretched families, low wage families and optimistic young workers'.[123] Debt relief might have different consequences for these groups. Debt advice agencies may already explicitly or implicitly tailor advice based on these typologies, but further research on the debt career of these distinct groups and the effects of bankruptcy on the career should be undertaken. Second, the extent of the benefit of the fresh start may depend on the practices of market actors such as banks[124] and credit reference agencies. It is the rules of credit reporting systems, used by creditors, insurance companies, employers and landlords, rather than the law, which may determine the availability of services for individuals who have filed for bankruptcy.[125] The English attempt to use the Bankruptcy Restriction Order signal as a warning for the market by separating culpable from innocent bankrupts seems to have had little effect on credit reporting systems.[126] Third, bankruptcy as presently structured, may be a limited remedy for certain groups who suffer from continuing instability of employment, long term poverty or unemployment. It may represent a temporary relief but may need to be integrated with better social protections.[127] It is not a substitute for such protections. Existing measures to alter bankrupts' behaviour through counselling are unlikely to be effective in addressing the problems faced by this group.[128] The studies pose the research question of how personal insolvency law, a private law form of consumption insurance, fits with social insurance and welfare provision, which may differ between countries. Fourth, Howard, in an analysis of ideas associated with the fresh start, poses the question whether bankruptcy is expected to serve too

[122] For example, individuals using a DRO may still be evicted from social housing. See *Places for People Homes Ltd v Sharples; A2 Dominion Homes Ltd v Goddfrey* [2011] EWCA Civ 813 (holding that a DRO order did not act as a stay on a social landlord evicting a tenant).

[123] See Money Advice Service, *Indebted Lives: The Complexities of Life in Debt* (2014).

[124] Which may close a bank account of a bankrupt in England and Wales.

[125] See the interesting discussion of the role of these systems in influencing the effectiveness of a fresh start in Howell and Mason, above n 10. The World Bank *Report on the Treatment of the Insolvency of Natural Persons*, above n 52, noted the potential for these systems to discriminate and the relative absence of research on this topic.

[126] Institutional creditors have their own systems for assessing credit so that legal provisions requiring bankrupts to disclose their status if borrowing over £500 are something of a dead letter.

[127] Atfield, Lindley and Orton, above n 114, 66, argue on the basis of their research that 'we need to think very differently about debt. Policy debates are stuck in ruts and do not fit with the lived reality of debt as revealed in this research. Wilful non- payment and financial mismanagement are minor concerns. Policy makers should pay much more attention to "upstream" measures that prevent chronic debt problems arising in the first place, such as low wages, social security, health.'

[128] A meta-analysis of studies of financial education concluded that financial education may have a role in improving behaviours where individuals have 'the ability or slack to exert greater control'. It could improve savings behaviour but 'did less well in preventing loan defaults': Margaret Miller et al, 'Can You Help Someone Become Financially Capable? A Meta-analysis of the Literature' (Background Paper, World Bank, 2014, on file with author).

many masters.[129] We might want to be more modest in our expectations of the fresh start. We should also recognise the challenges in measuring the relationships between the fresh start and achieving a variety of social and economic objectives. Finally, the gap between the promise and the reality of the fresh start as a safety net suggests the value of considering alternative, more radical analyses of personal insolvency law in contemporary capitalism. These might open up new approaches and research questions for personal insolvency law research.

IV THE RADICAL CRITIQUE AND THE STUDY OF PERSONAL INSOLVENCY

The rise in the significance of personal insolvency law is linked with the transformations in capitalism since the 1970s. These have resulted in a rise in inequality,[130] stagnation of wages in several countries, and the growth in household debt. The decline of the 'male breadwinner' model of the household and the rise of the two-income household creates a hostage to fortune should one partner lost a job. Neoliberal policies reduced the power of labour and welfare entitlements and embraced consumerism and entrepreneurialism. This period of high globalisation since the 1980s has been one where the lower middle classes of the rich countries have been the largest losers,[131] and studies suggest that this group is most likely to face issues of over-indebtedness and insolvency.

Theorising about credit and debt increased exponentially after the Great Recession, often as part of analyses of contemporary capitalism and neoliberalism.[132] Several writers have highlighted the role of household debt in maintaining consumer demand in the face of stagnating wages, but also in contributing to unsustainable housing bubbles.[133] Crouch describes this phenomenon as 'privatized Keynesianism',[134] which reconciles labour flexibility with the maintenance of consumer demand. Streeck, adopting crisis theories of capitalism developed by the Frankfurt School in the late 1960s, argues that capitalism faced a legitimation crisis, as capitalist states were increasingly unable to steer the economy effectively and make good on increased social expectations. One strategy to address this problem was the promotion of private consumption, financed by 'lavish credit to private households', thereby 'buying time for the existing social and economic order'.[135] Discourse theorists influenced by Foucault have highlighted how individuals are increasingly encouraged to behave like responsible credit users who 'learn to exploit credit markets appropriately'. Lazzarato argues in *The Making of the Indebted Man*[136] that in contemporary society with fewer traditional 'sites of discipline', such

[129] Howard above n 26, 1069.
[130] See Engelbert Stockhammer, 'Rising Inequality as a Cause of the Present Crisis' (2015) 39 *Cambridge Journal of Economics* 935; Ramsay, above n 16, ch 1.
[131] See Branko Milanovic, *Global Inequality: A New Approach for the Age of Globalization* (Harvard University Press, 2016) 20. Milanovic notes also the large rise in inequality where 'within-nation inequalities in the rich world have increased during the past twenty-five to thirty years'.
[132] For a review of studies see Basak Kus, 'Sociology of Debt States, Credit Markets and Indebted Citizens' (2015) 9(3) *Sociology Compass* 212.
[133] 'Cynical as it may seem, easy credit has been used as a palliative through history by governments that are unable to address the deeper anxieties of the middle class directly': Raghuram Rajan, *Fault Lines: How Hidden Fractures Still Threaten the World Economy* (Princeton University Press, 2010) 8–9.
[134] See Colin Crouch's discussion of 'Privatised Keynesianism' in Colin Crouch, 'Privatised Keynesianism: An Unacknowledged Policy Regime (2009) 11 *British Journal of Political and International Relations* 382.
[135] Wolfgang Streeck, *Buying Time: The Delayed Crisis of Democratic Capitalism* (Verso, 2013) 4. See also discussion in David Harvey, *A Brief History of Neoliberalism* (Oxford University Press, 2005).
[136] Maurizio Lazzarato, *The Making of the Indebted Man: An Essay on the Neo-Liberal Condition* (MIT Press, 2012).

as the factory, a society of control now exists,[137] where the creditor-debtor relationship has become more central to contemporary capitalism than the capital–labor relationship. The power to control and constrain debtors 'does not come from outside, as in disciplinary societies, but from debtors themselves'.[138] This shaping of individual subjectivity may be through government promotion of financial literacy, or technologies of credit scoring, with credit bureaux performing a sorting and disciplining role.[139] Individuals are encouraged to check their credit score and improve their credit rating. They must learn to live with debt.[140] Consumers are enlisted as regulatory subjects to make credit markets competitive (for example, through switching behaviour) and by policing 'internalities' such as impulsiveness or myopia, which might result in over-indebtedness. This is the world of the responsible borrower.[141]

The idea of debt as a disciplining force is not new. Calder argued that the rise of instalment debt in the US, which required individuals to adjust to the discipline of monthly payments, extended the discipline of the Fordist factory system to private consumption.[142] He also documents the efforts of elite opinion makers to normalise and legitimise consumer debt, for example changing its description from 'consumptive' to consumer debt in the 1930s. This conscious creation of a debt culture was supported both by labour and business interests in the US.[143]

Marxist analyses link both material conditions and ideological factors to paint a picture of exploitative credit, where financial institutions have increasingly turned to value-extraction from consumers as a source of profit,[144] legitimated by liberal credit narratives. Soederberg argues that capital exploits low income workers through the credit system, a form of secondary exploitation which fails to address the continuing problem of falling profits, low productivity and stagnant wages. The law structures and legitimates this exploitation through what she terms the *Debtfare State* as one component of the neoliberal state. A neo-liberal discourse of the 'democratisation of credit', 'financial inclusion', and 'consumer protection' legitimates this exploitation. The democratisation of credit to poorer individuals substitutes for secure jobs; 'financial inclusion' masks the often poor credit terms which many workers obtain; and consumer protection relies on 'individualized market based protection rather than the welfare

[137] See Gilles Deleuze, 'Postscript on the Societies of Control' (1992) 59 *October* 3. This idea of 'governmentality' where individuals experience discipline and shaping at many sites — the workplace, school — is a characteristic of neo-liberal 'governing at a distance'.

[138] Lazzarato, above n 136, 69.

[139] See Marion Fourcade and Kieran Healy, 'Classification Situations: Life Chances in the Neoliberal Era (2013) 38 *Accounting, Organizations and Society* 559.

[140] Lazzarato, above n 136, 112: 'Learning how to "live with debt" has now been made part of certain American school curricula'. See also Iain Ramsay, 'Consumer Credit Society and Consumer Bankruptcy: Reflections on Credit Cards and Bankruptcy in an Informational Economy' in Niemi, Ramsay and Whitford, above n 21, 38.

[141] Lazzarato, above n 136, 104. Individuals 'develop a way of life, discipline, attitudes and conduct appropriate to the "indebted man" [sic] who should learn to exploit credit markets appropriately'.

[142] See eg Lendol Calder, *Financing the American Dream: A Cultural History of Consumer Credit* (Princeton University Press, 2009). Calder drew on Jean Baudrillard: J Baudrillard, 'The Consumer Society', *Selected Writings* (Stanford University Press, 2001) 81. This point was also made by David Caplovitz in the 1970s: D Caplovitz, 'The Social Benefits and Costs of Consumer Credit' in RM Goode (ed), *Consumer Credit* (Leyden, 1978).

[143] This shift in the ideology of debt was part of a more general shift to consumerism in the US which was promoted by Ordoliberal writers such as Walter Lippman to reduce class conflict between capital and labour: James Q Whitman, 'Consumerism versus Producerism: A Study in Comparative Law' (2007) 117 *Yale Law Journal* 340, 361.

[144] Paulo L Dos Santos, 'On the Content of Banking in Contemporary Capitalism' (2009) 17 *Historical Materialism* 180.

state'.[145] Bankruptcy processes address the problems of higher level of default in this system through increased disciplining measures such as mandatory counselling, means testing, more repayment alternatives, and processes which delay the opportunity to declare bankruptcy. According to Soederberg, the US's *Bankruptcy Abuse Prevention and Consumer Protection Act 2005* ('BAPCPA') represents the raw power of capital to reduce the scope of bankruptcy's fresh start.[146] Bankruptcy also legitimates the system by individualising failure and responsibility, neutralising collective responses to debt. The increased focus on repayment alternatives to straight bankruptcy reduces losses, forces responsibility onto consumers and suggests that straight debt forgiveness is a suppressed political alternative in contemporary society. Soederberg does not provide any reform proposals beyond those of guaranteeing a living wage and public provision for basic social needs.[147] This radical critique is not fundamentally different from contemporary critiques of the US system by progressive scholars such as Katherine Porter, Jacob Hacker[148] or Jay Westbrook. Progressives recognise the need to change income support and healthcare systems, but they probably assume, unlike Soederberg, that bankruptcy is a potentially useful institution which can be reformed to address the limits of the current system.

Soederberg's critique overgeneralises and lacks attention to empirical and historical facts. For example, it is difficult to adopt her characterisation of the US Bankruptcy Reform Act 1978 as 'burdensome' to debtors.[149] However, the radical approach may be useful for framing future research. It underlines the importance of discourse and narratives in shaping both social and individual understanding of debt, default and insolvency, and provides a potential grid for analysing existing findings. I outlined earlier the important role of insolvency statistics in shaping official narratives of failure. Further studies might explore the relationship of professional discourses of failure to individual debtors' narratives and what debtors learn from the process, relating these findings to studies of individuals' relationship to law and experience of the legal system.[150] Such a study could provide an opportunity to understand the extent to which debtors 'buy in' to neoliberal norms, identifying their problems in personal mismanagement rather than broader structural causes.[151] Addressing this question may be best

[145] Susanne Soederberg, *Debtfare States and the Poverty Industry: Money, Discipline and the Surplus Population* (Routledge, 2014). Paul Mason in his popular book *PostCapitalism: A Guide to Our Future* (Allen Lane, 2015) 20, remarks pithily that 'we are no longer slaves only to the machine, to the 9–5 routine, we've become slaves to interest payments. We no longer just generate profits for our bosses through our work, but also profits for financial middlemen through our borrowing. A single mum on benefits, forced into the world of payday loans and buying household goods on credit, can be generating a much higher profit rate for capital than an auto industry worker with a steady job'.

[146] Soederberg, above n 145, 86–90; and see Linda Coco, 'Debtor's Prison in the NeoLiberal State: "Debtfare" and the Cultural Logics of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005' (2012) 49 *California Western Law Review* 1. See also the special issue of *Critical Sociology* (2014) for a series of articles on the increasingly coercive nature of debtor–creditor relations. About 100 individuals are imprisoned in England and Wales annually for non-payment of council tax. Bankruptcy is used by councils as a means of enforcing council tax.

[147] Soederberg, above n 145, 244.

[148] 'Bankruptcy can be a backstop for the worst financial collapses but was never intended as a replacement for a well-designed and robust safety net... Bankruptcy relief for approximately 1.5 million middle class families each year is ultimately an enormously wasteful, inefficient and incapable means of providing economic security to those who need it': Hacker, above n 11.

[149] Soederberg, above n 145, 87.

[150] See eg Patricia Ewick and Susan S Silbey, *The Commonplace of Law: Stories of Everyday Life* (University of Chicago Press, 1998).

[151] Although this may be problematic since the norm that everyone should pay their debts is not simply found in neoliberalism. See Liam Stanley, '"We're Reaping What We Sowed": Everyday Crisis Narratives and Acquiescence to the Age of Austerity', (2014) 19 *New Political Economy* 895.

achieved through rich qualitative research. Although much has been written at a high theoretical level about the shaping of individual subjectivity in neoliberalism, empirical investigation of the success of such shaping is limited.[152] Law and society scholarship suggests that individuals are not passive recipients of law but may resist or reinterpret laws. Understanding how different individuals approach the insolvency process and its aftermath might increase our knowledge of how individuals think about the legal process and the role of factors such as class and gender in these constructions.

V CONCLUSION

This article sketched an emerging paradigm of personal insolvency with partial repayment alternatives as a preferred policy instrument, combined with residual immediate relief for the deserving poor. The paper documented concerns about the economic and social benefits of repayment alternatives, and the possible limits of insolvency law in addressing the problems of NINA debtors, while pointing to the need for further research. The growth of longitudinal research on the extent to which individuals receive a fresh start suggests that, while bankruptcy may benefit some groups, for others it is merely a way-station in a continuing battle with problems of debt and unstable income. Moreover, the connection between a liberal discharge procedure and the promotion of entrepreneurialism, a dominant international driver of reforms, deserves further examination.

The mixed findings of existing research on the effectiveness of the fresh start suggest the need for more evidence-based policy and greater focus on the role of credit reference systems in determining the success of the fresh start. The current wave of empirical research raises questions whether bankruptcy is a progressive institution and what its role should be within social welfare systems, whether it dampens pressures for social welfare reform, or acts as a useful signal of the need for reform. The radical critique of bankruptcy as a legitimating and disciplinary institution in contemporary capitalism merits a scholarly response. It also has the methodological message that qualitative analysis of the discourse of bankruptcy and the experience of bankrupts may increase knowledge of the extent to which bankruptcy is a progressive or disciplinary institution. The introduction of special procedures in several countries to provide debt relief for low income individuals provides the opportunity to test the possibilities and limits of the fresh start precisely for those who may fall into the category of a 'surplus population' — marginalised and low-income workers.

[152] See John Clarke et al, *Creating Consumers: Creating Citizen Consumers* (Sage, 2007) 21.

QUT Law Review ISSN: Online-2201-7275
Volume 17, Issue 1, pp. 40–56 DOI: 10.5204/qutlr.v17i1.712

THE RETREAT OF AMERICAN BANKRUPTCY LAW

JAY LAWRENCE WESTBROOK*

In 2005 the United States adopted provisions constraining the bankruptcy 'fresh start' for the first time in its history. This paper describes the experience under the 2005 amendments over the decade since their enactment, including the data reported by empirical studies of their effects. It suggests a reappraisal of the goals of consumer bankruptcy law in the 21st century, including the simplification and reduction of costs that would arise from abandoning the idea that bankruptcy law should be used as a collection device for professional creditors in consumer cases. It discusses various possible approaches for a new reform while emphasising the importance of the continuing role of lawyers and courts in the consumer bankruptcy process.

> *The payment of debts is necessary for social order. The non-payment is quite equally necessary for social order. For centuries humanity has oscillated, serenely unaware, between these two contradictory necessities.*[1]

From 1898 until 2005, the fresh start was available to any American who needed it and was willing to pay the considerable reputational and psychological cost of filing for bankruptcy, as well as a filing fee and a lawyer's fee. The year 2005 saw the retreat of American law from its exceptional commitment to the fresh start, even as a number of other countries were moving cautiously in the US direction. Now that we have a decade of experience and data about the effect of the 2005 amendments, it is time for us to use that experience to cast a new light on the goals and costs of consumer bankruptcy in the 21st century. My central conclusions are these:

1. Given that the great majority of bankrupt consumer debtors cannot pay their debts in whole or material part, the central role of bankruptcy is ensuring the fresh start. In the modern world, the fresh start includes an opportunity for debtors to keep property subject to a security interest or mortgage, including their homes and a means of transportation, while respecting the rights of secured creditors.
2. It is past time for us to recognise that in the 21st century, bankruptcy should focus on the fresh start and should not be used as a collection device for professional unsecured creditors (eg issuers of credit cards) in consumer cases. Those creditors calculate the risk of non-payment on an actuarial basis that contemplates and welcomes substantial defaults as part of a profit-maximising business model. By lending to a mass of consumers on that basis, they have only a limited claim to protection from the discharge: primarily the right to be protected from obvious manipulation.

*JD (Texas), Benno C Schmidt Chair of Business Law, The University of Texas School of Law. I appreciate the helpful comments of Angela Littwin and the research assistance of Thomas Dannehy and Harris Wells, both Texas '17. This article is based on a keynote address to a personal bankruptcy conference: A Fresh Look at Fresh Start: The Human Dimension to Bankruptcy, Centre for Commercial and Property Law Research, QUT, Brisbane, September 2016, and is written as of that date.

[1] Simone Weil, 'On Bankruptcy', in *Selected Essays: 1934-1943*, 145, 149 (Richard Rees trans, Oxford University Press, 1962).

3. Most restrictions on the use of bankruptcy arise from a fear of abuse. Although that fear is often illusory or exaggerated, bankruptcy law should include an effective check on obvious debtor abuse at the lowest possible additional cost in non-abusive cases, which are the great majority.
4. Despite the routine nature of many aspects of consumer bankruptcy, it should continue to be administered through a judicial system.

These conclusions are restricted to consumer bankruptcies and to the treatment of claims by companies in the business of extending credit, that is, professional creditors.[2] The problems of small-business bankruptcies overlap with consumer cases, but small-business bankruptcies involve issues materially different from those presented in the great mass of bankruptcies filed by persons who owe primarily consumer debt. They are not discussed here. Similarly, the issues that arise with non-professional creditors (eg neighbours or co-signers) are so distinct I only touch upon them in this paper. In the discussion that follows, I will begin with a review of the American experience in the last 10 years, the decade in which access to the fresh start has been significantly constrained. The key points are:

1. Although the 2005 changes were adopted on the premise they would increase unsecured creditor returns in bankruptcy, the data strongly suggest that they failed to produce any significant increase in bankruptcy distributions. Instead, the benefit to unsecured professional creditors arose from a mass of paperwork justified as preventing supposed abuse. This 'busywork' has substantially increased lawyer's fees and costs with the effect of keeping a substantial number of debtors out of bankruptcy or delaying their entry. That effect has undoubtedly provided a bonanza for professional creditors.
2. It is highly likely that the debtors discouraged from filing were in as much need of bankruptcy relief as those who filed.
3. A central objective of the sorting process was to increase the share of cases filed in Chapter 13, our debt payout proceeding. It failed in that way too, with the fraction of bankruptcy filings made in Chapter 13 settling into the same range as before — about one-third.[3]

Based on that experience, I will argue we should change in some fundamental respects the way we think about consumer bankruptcy relief in modern society. The most basic change is that we should stop thinking of bankruptcy as a method of wringing payment from financially distressed debtors. Most countries have extensive non-bankruptcy provisions designed to enforce payment of debts. Some even have laws that permit harassment of debtors by debt collectors in ways that might not be permitted for other purposes. The central point of

[2] Professional creditors might be defined in terms of national or at least multi-state issuance of consumer credit by members of a creditor group such as Visa, or a national payday lender. However, the best approach might be to identify the category by inclusion in the creditor coverage of the *Credit Card Accountability Responsibility and Disclosure Act of 2009*, PL No 111-24 ('Card Act') or other consumer debt protection statutes.

[3] See Administration Office of the US Courts, *2014 Report of Statistics Required by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* (2014), 33, table 3 ('BAPCPA Report') (indicating that Chapter 13 cases made up 34 per cent of the total number of bankruptcy cases terminated in a 12-month window). See generally Scott F Norberg and Andrew J Velkey, 'Debtor Discharge and Creditor Repayment in Chapter 13', (2006) 39 *Creighton Law Review* 473, 476, 479 (finding a discharge rate of only 33 per cent among Chapter 13 debtors who filed in seven districts in 1994); Jean Braucher, 'A Law-in-Action Approach to Comparative Study of Repayment Forms of Consumer Bankruptcy' (Arizona Legal Studies Discussion Paper No 08-09, August 2009), finding, based on different methods of comparative evaluation of repayment forms of consumer debt proceedings, repayment options in North America, Europe, and Australia have high costs in relation to unsecured debt repayment and high rates of failure to achieve a discharge).

bankruptcy law is to suspend or terminate those provisions as to a debtor who invokes its protection. The ancient idea that bankruptcy (insolvency) was at bottom a collection device for creditors has considerable vitality in a business setting, but not in a modern consumer credit and bankruptcy system.

From a debtor's perspective, the discharge is the heart of the matter, albeit with a few narrowly focused exceptions. Yet it is also in the interest of debtors to retain some encumbered assets, especially homes and automobiles, necessary to a fresh start. Security interests and mortgages serve a function in the marketplace and are generally recognised in bankruptcy law everywhere. Procedures to permit payment of secured debts and retention of collateral are essential to the fresh start.[4] It is often said that debtors have another interest that should be protected by bankruptcy law: the opportunity to pay their debts voluntarily under a debt arrangement (in the United States, Chapter 13). The failure rate for such payment plans under the *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* ('BAPCPA') (at least half) remains deplorable. For the average debtor, the primary use of Chapter 13 is not to permit voluntary payments (which can be truly voluntary without any binding plan), but to permit the debtor to retain property subject to a security interest. If a new bankruptcy reform could include procedures that make retention practical in a liquidation, the primary remaining purposes of Chapter 13 would be to pay attorneys' fees in instalments and to use bankruptcy as a collection mechanism.[5]

I will suggest some possible approaches to a modified consumer bankruptcy system based on a decade of experience under BAPCPA and a few normative premises. The central theme of my suggestions will be a de-emphasis on collection of unsecured consumer debt owed to professional creditors.

I THE *BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT* (BAPCPA)

BAPCPA has been the subject of many articles.[6] I will offer only a brief summary and analysis. Proposed pro-creditor changes in the Bankruptcy Code ('the Code')[7] were introduced in the late 1990s in reaction to the report of the National Bankruptcy Review Commission,[8] which

[4] The two largest questions would be whether the price the debtor must pay for retention of collateral should be regulated by bankruptcy law and, if so, what should be the components of that price and what procedures should govern the process?

[5] Debtors occasionally have other goals that can be addressed on a case-by-case basis. See below, text accompanying n 84.

[6] See eg, Nicola Howell and Rosalind F Mason, 'Reinforcing Stigma or Delivering a Fresh Start: Bankruptcy and Future Engagement in the Workforce' (2015) 38 *University of New South Wales Law Journal* 1529; Angela K Littwin, 'Adapting to BAPCPA' (2016) 90 *American Bankruptcy Law Journal* 183; Sara Greene, Parina Patel and Katherine Porter, 'Cracking the Code: An Empirical Analysis of Consumer Bankruptcy Outcomes (2017) 101 *Minnesota Law Review* 1031; Teresa A Sullivan, Elizabeth Warren and Jay Lawrence Westbrook, 'Less Stigma or More Financial Distress: An Empirical Analysis of the Extraordinary Increase in Bankruptcy Filings' (2006) 59 *Stanford Law Review* 213, 253–54; Lois R Lupica, *The Consumer Bankruptcy Fee Study: Final Report* (American Bankruptcy Institute, 2012) 11–13 < http://digitalcommons.mainelaw.maine.edu/ faculty-publications/32>; Stefania Albanesi and Jaromir Nosal, 'Insolvency after the 2005 Bankruptcy Reform' (Staff Report No 725, Federal Reserve Bank of New York, April, 2015); Michelle J White, 'Abuse or Protection? Economics of Bankruptcy Reform Under BAPCPA' (2007) *University of Illinois Law Review* 275; Ronald J Mann and Katherine Porter, 'Saving Up for Bankruptcy' (2010) 98 *Georgia Law Journal* 289, 292; Robert M Lawless et al, 'Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors' (2008) 82 *American Bankruptcy Law Journal* 349. Given the rich literature in Australia and elsewhere describing the structure and operation of the United States Bankruptcy Code, I assume some familiarity with the US system.

[7] The United States Bankruptcy Code comprises the whole of Title 11 of the United States Code, 11 USC § 101 ff.

[8] National Bankruptcy Review Commission, *Bankruptcy: The Next Twenty Years* (1997).

had proposed mostly pro-debtor changes.[9] The credit industry pointed to the fact that consumer bankruptcy filings had steadily increased year to year and argued that bankruptcy was too easy, despite empirical work showing that most debtors were just as overwhelmed by unpayable debts as they had been in prior decades.[10] They claimed that many debtors were filing for bankruptcy when they could have paid their debts.[11] After years of struggle — during which a strong version of the industry's proposals was actually passed by Congress, only to be vetoed by President Clinton — the industry succeeded in making BAPCPA into law in 2005. It contained many of the provisions the creditors had proposed.

The most debated substantive change was the institution of the means test which, for the first time, blocked access to Chapter 7 liquidation bankruptcy and a prompt discharge. The idea was to identify the debtors who could pay part or all of their debts and to block them from Chapter 7. If debtors' income and debts fell within the means test formula, they would be forced to choose a Chapter 13 payment plan or not to file bankruptcy at all. The test also created a novel distinction among Chapter 13 debtors, requiring more affluent debtors, as measured by its formula, to undertake longer payouts.[12] (Five years is the standard period.) The elaborate formula reflected the industry's conviction that bankruptcy experts, especially specialised bankruptcy judges, were too generous to debtors, a conviction that led to very detailed provisions to measure what percentage of 'disposable' income debtors had to pay.[13] Unfortunately, a further consequence of the industry's suspicion of the bankruptcy bench and bar[14] was that the new provisions were drafted by non-experts who drafted non-expertly,[15] leading to years of litigation.[16]

Other substantive provisions on the consumer side included, inter alia, increasing the period the debtor would be excluded from another Chapter 7 discharge, expanding the exceptions to

---

[9] See Lawrence Ponoroff, 'Bankruptcy Preferences: Recalcitrant Passengers Aboard the Flight from Creditor Equality' (2016) 90 *American Bankruptcy Law Journal* 329, summarising the history of these pro-debtor changes.

[10] Sullivan, Warren and Westbrook, above n 6, 253–4. That study relied primarily on the ratio of debt-to-income as a measure of ability to pay. See below n 48 and related text, discussing the debt-to-income issue further.

[11] See Judge Edith H Jones and Todd J Zywicki, 'It's Time for Means-Testing' (1999) *Brigham Young University Law Review* 177, 186–7, claiming that the implementation of means testing would have caused many debtors, who had the ability, to repay their unsecured creditors. A study financed by the credit industry in the 1980s had claimed that too many consumers were considering 'enriching themselves [through bankruptcy] as often as the law allows': Credit Research Center, Krannert Graduate School of Management, *Consumer Bankruptcy Study: Volume II* (Purdue University, 1982) 103.

[12] See eg, Eugene R Wedoff, 'Major Consumer Bankruptcy Effects of the 2005 Reform Legislation' (2005) 38 *Uniform Commercial Code Law Journal* 87–118; Henry J Sommer, 'Trying to Make Sense Out of Nonsense: Representing Consumers Under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005' (2005) 79 *American Bankruptcy Law Journal* 191; Christian E Weller, Bernard J Morzuch and Amanda Logan, 'Estimating the Effect of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 on the Bankruptcy Rate' (2010) 84 *American Bankruptcy Law Journal* 327 (2010). In bare summary, the formula largely excluded from application of the new rules those debtors with an income below the median income for the state of their residence. Above median debtors were subject to a complicated set of rules for determining their 'disposable income', from which they were to pay something to their unsecured creditors. Secured creditors' entitlements were also strengthened and their priority access to future income enhanced.

[13] Wedoff, above n 12; Sommer, above n 12; Littwin, above n 6.

[14] Most technical laws, like bankruptcy and tax, are the subject of a technical amendments Bill a year or two after adoption. That sort of Bill is designed to make no substantive change, but to correct errors. The credit industry was so suspicious of those with bankruptcy expertise that it blocked the usual technical amendments legislation for years, fearing that some weakening of the 2005 changes might occur. The technical statute for the 2005 amendments was finally adopted in 2010: *Bankruptcy Technical Corrections Act of 2010*, Pub L No 111-327, 22 December 2010, 124 Stat 3557.

[15] The most infamous example of bad drafting is the 'hanging paragraph': Sommer, above n 12, 191–2.

[16] Lupica, above n 6, 114–15; Lawless et al, above n 6, 351–2.

discharge for luxury purchases prior to bankruptcy, and reducing the property a debtor would be allowed to exempt and retain.

However, the bulk of the legislation was made up of procedural changes. Most of them involved adding substantially to the pile of paperwork that debtors and their lawyers were required to complete and file with the court. The means test formula itself required an elaborate form filled with complicated calculations. But the most novel and troubling provisions of the procedural amendments imposed many new duties on the consumer's lawyer, including specified disclosures, mandated record keeping, and the making of a 'reasonable inspection' to assure the debtor's filings were correct. To that extent, the lawyer was made personally responsible for the accuracy of a debtor's filings.[17] Two other changes directly increased the time and money necessary to obtain a discharge: requiring credit counselling before the petition could be filed and completion of a 'financial management' course prior to discharge.[18]

In an insightful article, my colleague Angela Littwin has shown that many of the dire predictions concerning the operation of the new provisions have failed to materialise.[19] In part this result arose from the un-sophisticated drafting of the non-experts, but the main reason was the adaptability of the lawyers and judges, which made the provisions in practice far less onerous than they had appeared (and perhaps were meant to be). Two specific factors that mitigated the burden were the rapid appearance of software that largely automated the paperwork and the common sense of the Executive Office of the United States Trustee in interpreting and applying the new provisions.[20]

In particular, the means test has not made a major substantive difference in bankruptcy proceedings, although it is important in a small percentage of cases involving debtors with higher incomes.[21] This result is unsurprising, given that a number of empirical studies prior to the adoption of BAPCPA showed that relatively few of the debtors who had filed under the prior law would have been barred from Chapter 7 had the means test been in place.[22] On the other hand, the calculations still had to be made and the forms filed. That meant the data for the forms had to be gathered from distressed and unsophisticated debtors[23] to be entered into the algorithms for the means test calculation, along with the completion of much other paperwork.

II THE EFFECTS OF BAPCPA

In the end, the substantive changes had little effect while the procedural ones led to the best possible result for the credit industry: fewer distressed debtors filing for bankruptcy.[24] Mann

[17] Littwin, above n 6, 185; Wedoff, above n 12, 13; Sommer, above n 12, 206; 11 USCA § 707(b)(4) (West).
[18] 11 USCA §§ 109(h)(1), 727(a)(11) (West).
[19] Littwin, above n 6.
[20] For example, the Office made it possible to satisfy the credit counselling requirement by completing a brief on-line course. The Executive Office of the United States Trustee is a branch of the executive in the Justice Department. There is a United States Trustee responsible for each federal judicial district, although some cover more than one district. It performs many of the administrative duties required by the system as well as providing advice to the bankruptcy judges, including scrutiny of attorneys' fees and proposed plans.
[21] Albanesi and Nosal, above n 6, 2.
[22] See eg, Sullivan, Warren and Westbrook, above n 6, 239; Marianne Culhane and Michaela White, 'Taking the New Consumer Bankruptcy Model for a Test Drive: Means-Testing Real Chapter 7 Debtors' (1999) 7 *American Bankruptcy Institute Law Review* 27, 31.
[23] Lupica, above n 6, 31–2.
[24] Albanesi and Nosal, above n 6, 36; Ed Flynn, 'BAPCPA: The Mystery of the 5 Million Missing Cases' (2014) 33 *American Bankruptcy Institute Law Journal* 32, 32.

and Porter argue persuasively that the increased costs of all the busywork mandated by the amendments had the effect of raising the cost of bankruptcy substantially and that this cost increase has delayed or discouraged filings.[25] In particular, the accommodations lawyers and judges had to make to permit the system to function properly were themselves a major, and unavoidable, cause of the increase in costs.

The American Bankruptcy Institute[26] funded a study by Lupica to investigate the effects of BAPCPA on the fees consumer bankrupts had to pay to lawyers.[27] The study took a national sample of consumer cases and analysed them in great detail.[28] For example, it found that fees in no-asset Chapter 7 cases under BAPCPA (90 per cent of consumer Chapter 7 cases[29]) had increased an average (mean) of 48 per cent from their pre-amendments level.[30] So in cases in which the debtor had no assets available for unsecured creditors, the debtor would have to pay the lawyer almost 50 per cent more than before, to file the most routine of bankruptcy cases. Chapter 7 cases with some assets for distribution and Chapter 13 cases also showed dramatic increases in attorneys' fees and other costs.[31] The General Accounting Office did a study with a differently configured sample and reported increases of approximately 50 per cent in attorneys' fees in both Chapter 7 and Chapter 13 cases.[32] It also reported estimates of more than US$100 million in taxpayers' money for start-up costs for the new provisions, plus some additional amounts of increased costs going forward.[33]

Consumer bankruptcy filings have been materially lower since 2005 even after controlling for various economic factors that may have had that effect.[34] It would hardly be surprising if fee increases of the magnitude just described were an important cause of that decline. In fact, many of those who study the bankruptcy statistics believe that the cost of the busywork and the related dramatic increase in overall costs has suppressed consumer filings.[35] One knowledgeable government official who often publishes statistical studies of bankruptcy estimated that BAPCPA fended off 5 million petitions that would have been filed in the years 2005–2013.[36]

---

[25] Mann and Porter, above n 6, 292.

[26] The ABI is a membership organisation that includes judges, lawyers, academics, and others interested in the bankruptcy process: American Bankruptcy Institute, *About Us* <http://www.abi.org/about-us>.

[27] Lupica, above n 6.

[28] Indeed, the report is a valuable source of empirical data on many aspects of the subject beyond fees, although that is its central focus: Lupica, above n 6, 6–8.

[29] Lupica, above n 6, 49.

[30] Ibid 51.

[31] Ibid 36–48, 51. The amounts of increase (and a few regional decreases) varied considerably from one district to another, but the overall effect was a substantial increase.

[32] Professor Braucher anticipated a key problem, administrative costs: 'administrative costs may well exceed disbursements to unsecured creditors': Braucher, above n 3, 335. The US Trustee's Office and the Federal Judiciary estimated the total start-up cost of BACPA would be US$120 782 000: United States Government Accountability Office, *Bankruptcy Reform: Dollar Costs Associated with the Bankruptcy Abuse and Consumer Protection Act of 2005* (2008) 14, 16.

[33] US Government Accountability Office, above n 32, 3–4.

[34] See eg, Lawless et al, above n 6. This study was the latest from the Consumer Bankruptcy Project which conducted large consumer bankruptcy studies of cases filed in 1981, 1991, 2001, and 2007. I was a co-principal investigator for the first two of these studies.

[35] Flynn, above n 24, 32. Other economic factors, including a substantial pay-down of debt by consumers overall, have likely contributed to the substantial fall in consumer filings. For a study of that factor, see generally Robert Lawless, 'The Relationship Between Nonbusiness Bankruptcy Filings and Various Measures of Consumer Debt' (University of Illinois Law and Economics Research Paper Series, 2001).

[36] Flynn, above n 24, 32. Another estimate by leading empiricists was a 'missing' 800 000 filings in 2007 alone. That is, they estimated that 2007 filings were perhaps 800 000 fewer than experience under pre-BAPCPA would have suggested: Lawless et al, above n 6, 350.

Among the things that the amendments' sponsors wanted to achieve was a long-term increase in Chapter 13 filings. Increasing the percentage of debtors committed to a payment plan in Chapter 13 was a major stated purpose of BAPCPA, but that goal rested on the demonstrably false premise that many debtors in the past had chosen Chapter 7 despite being able to pay. The percentage of Chapter 13 cases did indeed rise in the first years after the statute was adopted, but by 2014 it returned to its historic niche as the filing place for about one-third of the debtors, mostly homeowners.[37]

Not only have Chapter 13 filings failed to rise as a proportion of total filings, but there is no evidence the Chapter 13 debtors are achieving more repayment. Over the twenty-five years under the Code prior to BAPCPA about one-third of cases filed in that chapter resulted in completed plans.[38] I am disappointed to say that the Land of Bankruptcy Empiricism has not yet completed a study that provides very current data post-BAPCPA, although some top-notch researchers are compiling data that should give us answers by 2018 or so. For now, the government data are not helpful, because they report completions and dismissals each year without tying the completions to the year of filing.[39] The few data we have suggest that completions may have risen to 36 per cent, but that information was gathered early in the life of BAPCPA and such a small difference is probably not reliable as a trend.[40] In my view, a reasonable assumption would be that the proportion of Chapter 13 filings is likely close to the range that prevailed prior to BAPCPA, about one-third. Even in those cases the information so far suggests that the credit industry changes did not appear to have produced more payment in Chapter 13 bankruptcy than under the prior legal regime.[41]

The effect of a failed case varies.[42] Some debtors may have benefited to some extent from the respite from collection efforts before the filing was dismissed, giving them the breathing space that they needed. But too many of the Chapter 13 filers continued to suffer reverses, often the same troubles that led them to bankruptcy in the first place, and their cases were dismissed for non-payment. The failure of their cases left them with the same debt as before, minus whatever payments they were able to make before their cases failed, minus substantial bankruptcy costs, and often minus their homes.[43] Since about one-third of debtors filed for Chapter 13[44] and around 66 per cent of those Chapter 13 filers failed to complete a plan and get a discharge,[45] the debtors who actually completed a plan and received a discharge represent just 10–13 per

[37] Teresa A Sullivan, Elizabeth Warren and Jay Lawrence Westbrook, *As We Forgive Our Debtors: Bankruptcy and Consumer Credit in America* (Oxford University Press, 1989), 266; Teresa A Sullivan, Elizabeth Warren and Jay Lawrence Westbrook, *The Fragile Middle Class: Americans in Debt* (Yale University Press, 2000); Lupica, above n 6, 33; Greene, Patel and Porter, above n 6, 1043. The percentage of asset and no asset cases in Chapter 7 remained substantially the same before and after the 2005 amendments: Lupica, above n 6, 49.

[38] See Sullivan, Warren and Westbrook, *As We Forgive*, above n 37, 216; Norberg and Velkey, above n 3.

[39] So, in Year 4 there might be 50 completions and 50 dismissals while Year 5 might see 50 completions and 100 dismissals. But we don't know when the cases in either category were filed, since dismissals happen throughout the Chapter 13 process. It could be that the Year 4 dismissals were from Years 2 and 3, while the Year 5 dismissals were from Year 1. It would be incorrect to claim a 50 per cent completion rate in Year 4, falling to a 33 per cent rate in Year 5. We would have to look at the dismissals and assign them to the years they were filed to make a true comparison about failure rates.

[40] The best data we have are from a study of 2007 cases, so it is hard to know if they represent the long-term under BAPCPA. See Greene, Patel and Porter, above n 6, table 1. The ABI data showed around 40 per cent completion, but those data were very early: Lupica, above n 6, 32–3.

[41] The percentage of claims paid in the ABI Study cases actually dropped just a bit: Lupica, above n 6, 67.

[42] Katherine M Porter, 'The Pretend Solution: An Empirical Study of Bankruptcy Outcomes' (2011) 90 *Texas Law Review* 103, 151–3.

[43] Ibid 111, stating that some of these cases would be 'converted' to Chapter 7, but most would be dismissed.

[44] BAPCPA Report, above n 3, 33, table 3.

[45] Ibid 45.

cent of the total number of consumer cases filed in bankruptcy courts.[46] Overall, unsecured creditors received no increase in percentage distributions under the amendments than they received prior to BAPCPA.[47] The actual repayment rate declined a bit after BAPCPA was adopted, although the difference was slight. Thus, virtually any benefit for creditors generated by BAPCPA has been derived from the increase in the cost of bankruptcy that barred or discouraged debtors from seeking bankruptcy protection.

III THE CREDITOR PAYOFF FROM DEBTOR EXCLUSION

If those debtors who did not file for either form of bankruptcy were the 'can pay' debtors who were more affluent or less indebted than others, the resulting increase in creditor recoveries would be exactly what Congress intended: more recovery from people who could pay. If, however, these are people in the same distress as those who did file, then it seems apparent from the rates of payment of those who filed Chapter 13 that many non-filers were equally unable to pay their debts outside of bankruptcy.

As explained above, even before BAPCPA was introduced extensive empirical studies, starting with 1981 filers and extending to the early years of this century, showed that there were vanishingly few 'can pay' debtors in bankruptcy. Thus, the burden of showing that the excluded debtors were 'can pay' candidates must fall on the proponents of the changes. In fact, there is no evidence that the excluded debtors were more able to pay than those who have filed under BAPCPA. Given the fact that those same empirical studies showed that the debt-to-income ratios of bankruptcy debtors had got steadily worse from 1981 through 2007 (the first year of BAPCPA),[48] it would be illogical to assume without evidence that those excluded could have paid any material part of their debts. The constancy of the increase in the debt–income ratio from 1981 through two years of experience under BAPCPA strongly implies that those excluded from bankruptcy are likely to be at least as distressed as those who filed, because the primary reason for their exclusion — the cost of filing bankruptcy — is only marginally connected to their debt-to-income position. If anything, those excluded by costs would seem likely to be more indebted regarding their incomes than those who found the money to file.[49]
It is important to understand why the exclusion of highly indebted consumers from bankruptcy would be so valuable to professional creditors, given that these debtors cannot pay off any substantial part of their debts. By a careful analysis of the credit card business model, Mann has shown that the profits of credit card companies in particular arise in large part from debtors who linger long in default, paying something but not enough, as interest and multiple fees increase their debts and debt collectors are free to pressure and harass.[50] He dubbed that state

[46] The sample of pre-BAPCPA cases included in the American Bankruptcy Institute Study had a 50 per cent completion rate, a rate that dropped in subsequent years. Lupica, above n 6, 32–3.
[47] Ibid 7, 67–8; Braucher, above n 3, 336. Apparently, payment results in Germany have been similarly disappointing: Braucher, 347; and this is true in other European countries as well: see note 151, Jason J Kilborn, 'The Hidden Life of Consumer Bankruptcy Reform: Danger Signs for The US Law from Unexpected Parallels in the Netherlands' (2006) 39 *Vanderbilt Journal of Transnational Law* 77, 102.
[48] Sullivan, Warren and Westbrook, *As We Forgive*, above n 37, 74; Sullivan, Warren and Westbrook, *Fragile Middle Class*, above n 37, 70–2, 130; Sullivan, Warren and Westbrook, above n 6, 239; Lawless et al, above n 6, 353. The ratio in 2001 was debt 2.5 times annual income: Lawless et al, 377. Because the great majority of consumer debtors have few assets subject to creditors' claims — most are exempt or encumbered — net worth is not very important on the consumer side. Nonetheless, it is striking that debtors' inflation-adjusted negative net worth doubled from 1981 to 2007: Lawless et al, 369–70.
[49] Albanesi and Nosal, above n 6, 21.
[50] The same business model is central to the business models of many issuers of small, short-term loans ('payday lenders'). Ronald J Mann, 'Bankruptcy Reform and the "Sweat Box" of Credit Card Debt' (2007) *University of Illinois Law Review* 375, 385–6. The article opens a fascinating window on the financial world of credit card

of debtor existence the 'sweat box'. He asserts, based on the financial evidence, that 'lenders are not just indifferent to default, they actually rely upon it in part to turn on the sweatbox's heat switch for their most lucrative constituency'.[51] As Freeman has commented, 'the ideal credit card user maintains only enough financial institution stability to avoid bankruptcy proceedings'.[52] Her article is more recent than Mann's and pulls together very helpfully a number of sources. She argues: 'Although most economists and legal scholars view the 'credit card problem' of excessive consumer debt as one of market failure, it is in fact a story of overwhelming market success', citing Owen Bar Gill, among others.[53] Perhaps the most powerful support for these conclusions comes from the General Accounting Office, one of the most dispassionate of our government entities, which estimates that 80 per cent of the industry's profits now come from interest payments and consumer fees rather than merchant-paid fees.[54] John Pottow has provided a helpful analysis of the causes and resulting externalities of these credit practices.[55]

By keeping more debtors in the box and outside of bankruptcy, BAPCPA has undoubtedly earned for the credit card companies more than the cost of their expensive lobbying campaigns for BAPCPA, even if not a dollar more was paid to them within bankruptcy proceedings.[56] To illustrate this point, if one million excluded debtors (a highly conservative number)[57] managed to pay an additional US$200 each, there would be a US$200 million return to the credit industry.[58] Therefore a lack of greater payment in bankruptcy (those 'can pay' debtors being elusive) pales in comparison with the windfall the industry has received by making bankruptcy much more expensive and therefore less available.[59]

companies. See also Dalié Jiménez, 'Dirty Debt Sold Dirt Cheap' (2015) 52 *Harvard Journal on Legislation* 41, discussing issues related to the collection of consumer debt, especially credit-card debt, barred by the statute of limitations—yet another window into that industry.

[51] Mann, above n 50, 379.

[52] Andrea Freeman, 'Payback: A Structural Analysis of the Credit Card Problem' (2013) 55 *Arizona Law Review* 151, 162.

[53] Oren Bar-Gill, 'Seduction by Plastic' (2004) 98 *Northwestern University Law Review* 1373, 1373–4.

[54] See Freeman, above n 52, 154, citing US Government Accountability Office, *Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers: Report to the Ranking Minority Member*, Permanent Subcommittee on Investigations, Committee on Homeland Security and Governmental Affairs, US Senate, GAO-06-929, September 2006, 67 <http://gao.gov/new.items/d06929.pdf>. James White, an eminent commercial scholar not famous for pro-consumer stances, has suggested that exclusion of debtors of all sorts from bankruptcy was likely to be a reason for BAPCPA: James J White, 'Abuse Prevention 2005' (2006) 71 *Montana Law Review* 863. Yet another confirmation is found in a recent comparison of earnings and profits of credit card companies before and after the Card Act: Sumit Agarwal et al, 'Regulating Consumer Financial Products: Evidence from Credit Cards' (NBER Working Paper No w19484) 37-44, <https://ssrn.com/abstract=2332556> (stunning graphs show earnings and profits strongly skewed to debtors with lower credit ratings). Note that I use 'exclusion' to include those who delay filing and thus are excluded for a period of time during which they make additional payments.

[55] John Pottow, 'Private Liability for Reckless Consumer Lending' (2007) *University of Illinois Law Review* 405, 418.

[56] For one interesting calculation, based on the available evidence, see Mann, above n 50, 375–6. One early estimate by an economist was US$4 billion a year: Robert H Scott III, 'Bankruptcy Abuse Prevention and Consumer Protection Act of 2005: How the Credit Card Industry's Perseverance Paid Off' (2007) 41 *Journal of Economic Issues* 943, 945: the author estimated that the industry contributed almost $25 million to politicians from 1999–2005.

[57] Recall the estimates of 5 million excluded petitions from 2005–2013 and 800 000 in 2007 alone: Flynn, above n 24, 81; Lawless et al, above n 6, 376.

[58] We do not have a metric for the coincident human misery.

[59] See Lawless et al, above n 6, 379–80.

The professional creditors have developed algorithms that are highly predictive as to certain cohorts of debtors, many of whom have weak credit ratings. A roughly predictable number of them will be unable to pay their debts. While the write-off of those debts is part of the business model, if the debtors can be pushed for a few more payments before they fail or give up, the resulting profit is over and above the amount the models would otherwise predict. Thus, there is no paradox between these debtors being 'unable to pay' and a substantial increase of profit from excluding them from bankruptcy.[60]

BAPCPA's procedural changes were justified primarily to identify debtors who could pay some substantial part of their debts. The evidence to date strongly suggests the changes have not achieved that result. The primary benefit to creditors came from exclusion of persons unlikely to be able to pay off their debts, paying sporadically in the sweat box. There has been a large aggregate gain for the industry at the same time that the additional payments from each debtor were relatively small.

IV THE PROPER FUNCTIONS OF CONSUMER BANKRUPTCY LAW WITH REGARD TO PROFESSIONAL CREDITORS

To summarise:

1. The benefits to professional creditors from BAPCPA do not lie in greater payments in bankruptcy, but rather in excluding many debtors from bankruptcy protection.
2. The debtors who are kept out of bankruptcy by the costs of complying with BAPCPA are as financially distressed as those who filed.
3. Those excluded debtors are unlikely to pay off their debts outside of bankruptcy because they are in much the same financial distress as those who are unable to pay in bankruptcy.
4. It follows that the primary benefit to professional creditors lies in the sweat box.

These propositions tee up a normative question: does society accept that obtaining some payments to creditors through the sweat box justifies denying bankruptcy relief to those who will never be able to pay any substantial portion of their debts? Congress was not asked that question. The question that was presented was whether debtors who could pay their debts should be barred from bankruptcy or discouraged from using it. Once experience has confirmed what empirical research predicted—that the excluded debtors would at best make some further payments in a context of ever-increasing debt—I believe the answer to the question should change. To introduce devices that exclude millions of debtors from the fresh start they need, merely to extract a few additional payments from heavily burdened debtors, seems to me to be morally repugnant, economically unproductive, and socially damaging.

For many years prior to 2005, the unsecured credit industry accepted losses from marginal debtors because the majority of marginal (often called 'sub-prime') debtors generated profits greater than those losses. The losses were built into a successful business model. The 2005 moral and economic trade-off to exclude needy debtors from bankruptcy to marginally reduce those losses and increase those profits seems a bad social and economic exchange. It follows for me that consumer bankruptcy should not be used to collect debts for professional creditors. Its function should be to provide the fresh start. Some would argue that debtors would be

[60] See Lauren E Willis, 'Against Financial-Literacy Education' (2008) 94 *Iowa Law Review* 197, 265–6, discussing the 'fee-harvesting credit card' which, by targeting consumers who were likely to incur fees, enabled creditors to reap profits and write-off debts that were largely the credit-card 'issuer's own fees'.

deprived of additional credit that might help them avoid bankruptcy. I would respond that avoiding bankruptcy when a debtor needs it is precisely the problem for many debtors and for a society that wants debtors restored to full economic function.[61]

However, there remains the problem of possible abuse of the bankruptcy process. Many of us could agree that blatant and widespread manipulation of bankruptcy by debtors who could comfortably repay their debts would be a bad result. Not only would it be morally troubling, it might lead to a contraction of unsecured credit and an increase in its price. Thus there would be a social value in preventing that abuse of a system designed to rescue people from serious over-indebtedness. If there is evidence of such abuse, the question becomes what is the best approach to fend off such a result.

Some years ago, as the notion of consumer bankruptcy was beginning to take hold in Western Europe,[62] I had occasion to write an article about the effects on bankruptcy law of the ever-present fear of abuse of such a system.[63] I argued that the American experience of almost a century under liberal-consumer bankruptcy laws seemed to show that the fear was greatly exaggerated, but nonetheless lawmakers overcorrected for it, leaving debtors with inadequate and often unworkable procedures. Reflecting on the experiences in the United States and elsewhere since that time,[64] I have come to see that part of the exaggeration of the risk of abuse came from confusing the risk of abuse with the use of bankruptcy as a collection device. Even though there is no evidence that widespread abuse is likely, citizens are often concerned by the simple logic of discharge: people would naturally run up debts and then gaily discharge them if there were no price to pay for doing that.[65] Insistence that debtors pay what they reasonably can pay could serve as a bar to abuse even though that approach has little value in producing meaningful payments of unsecured debt. The two uses of bankruptcy—collecting payment and deterring abuse—are rarely separated in discourse, but they are conceptually and perhaps practically distinct. As we have seen, the first goal is unachievable. The claim underlying the second goal is that the threat of collection in bankruptcy is the best defence against serious abuse.

For 107 years US bankruptcy law, largely[66] relied on social controls to avoid bankruptcy abuse, in particular, the stigma of bankruptcy. Even in the United States, a nation populated by many

---

[61] See Michelle J White, 'Why Don't More Households File for Bankruptcy?' (1998) 14 *Journal of Law, Economics and Organization* 205, 205, suggesting that more 'households would benefit financially from bankruptcy than actually file'; Sullivan, Warren and Westbrook, above n 6, 214–15, suggesting that increases in bankruptcy filings were driven by economic need, not due to declining social stigma surrounding bankruptcy; Mann and Porter, above n 6, 338, stating that access to bankruptcy is important in part because 'society loses when people are trapped in financial distress, discouraged from productive economic enterprises and so burdened by debts that they cannot participate in the consumer economy'.

[62] See generally Iain Ramsay, 'Comparative Consumer Bankruptcy' (2007) *University of Illinois Law Review* 241; Iain Ramsay 'US Exceptionalism, Historical Institutionalism, and the Comparative Study of Consumer Bankruptcy Law' (2015) 87 *Temple Law Review* 947; Kilborn, above n 47, 83, n17.

[63] Jay Lawrence Westbrook, 'Local Legal Culture and the Fear of Abuse' (1998) 6 *American Bankruptcy Institute Law Review* 25, 28.

[64] The concern over abuse and the procedures structured in light of those fears are captured in the excellent comparative work of Jason Kilborn: Kilborn, above n 47, 77.

[65] White, above n 61, 205.

[66] Dismissal of cases for 'substantial abuse' was included in the Code in 1984, but the creditors proposing BAPCPA complained that it was underused: Kathleen Murphy and Justin H Dion, '"Means Test" or "Just a Mean Test": An Examination of the Requirement the Converted Chapter 7 Bankruptcy Debtors Comply with Amended Section 707(B)' (2008) 16 *American Bankruptcy Law Review* 413, 432–3.

immigrant debtors from the start, bankruptcy carried a substantial stigma.[67] The claim that was made in the BAPCPA debates was that the stigma had greatly declined, so that filing bankruptcy was socially perceived as just a clever legal manoeuvre. Whatever might be said about that factor in the business context,[68] Mason and others have demonstrated its implausibility in consumer cases.[69] Mason pointed to the continuing effect of bankruptcy on reputation:

> A seminal British law reform report on insolvency in the 1980s, the Cork Report, referred to one result of bankruptcy as 'a sense of failure and humiliation ... with [his] family or [his] colleagues at work' which must be aggravated if there is a public examination and press publicity. More recently a World Bank report in 2014 on insolvency and natural persons cited surveys of debtors in many well-established insolvency systems that revealed 'pervasive and profound feelings of guilt, shame, and stigma'. Bankruptcy stigma also has an economic aspect – affecting a bankrupt as an economic player, whether in seeking employment, credit ([eg] to operate a business as a sole trader) or positions of responsibility.[70]

In the United States, my co-authors and I have shown in previous work that the data concerning the financial situation of bankrupt debtors 'hint that, despite loud claims to the contrary, the stigma of bankruptcy may actually be increasing.'[71] In fact, in over more than a century, the generous US system produced no widespread abuse.

Closely related to the unsupported argument that stigma has declined is the concern about moral hazard: might debtors run up unpayable debts knowing that bankruptcy is readily available? There is no evidence for this claim either, but more importantly it has a certain inherent difficulty rarely discussed. Just the same concern is presented by every social measure designed to protect us from bad or risky choices. Rescue teams in the national parks might encourage climbers to try more dangerous routes up the mountain. Fire insurance might encourage carelessness in the kitchen. These sorts of claims usually have three characteristics: they make no distinction between misfortune and assumption of the risk; they assume that society is better off when its members are discouraged from taking risks, and they may represent excuses for failing to aid others although each of us sometimes makes poor choices. My conclusion is that there is no sustainable argument for erecting barriers to consumer bankruptcy because of a fear of abuse. Nonetheless, in the concluding section of this paper, I will include that concern among the factors that should be considered in any future reform.[72]

---

[67] Ramsay, 'Comparative Consumer,'above n 62, 256; Paul Ali, Lucinda O'Brien and Ian Ramsay, 'Short a Few Quid': Bankruptcy Stigma in Contemporary Australia' (2015) 38 *University of New South Wales Law Journal* 1575, 1575.

[68] *See* Robert O'Harrow Jr, 'Trump's Bad Bet: How Too Much Debt Drove His Biggest Casino Aground', *Washington Post*, 18 January 2016 <https://www.washingtonpost.com/investigations/trumps-bad-bet-how-too-much-debt-drove-his-biggest-casino-aground/2016/01/18/f67cedc2-9ac8-11e5-8917-653b65c809eb_story.html>, discussing how Trump believed 'that he was shrewd for using "the laws of the country to my benefit"'; Bryan Hood, '4 Times Donald Trump's Companies Declared Bankruptcy', *Vanity Fair*, 29 June 2015 <http://www.vanityfair.com/news/2015/06/donald-trump-companies-bankruptcy-atlantic-city>.

[69] See eg, Howell and Mason, above n 6, 1529–30; Sullivan, Warren and Westbrook, above n 6, 214–15.

[70] Howell and Mason, above n 6, 1530–31 (footnotes omitted).

[71] Sullivan, Warren and Westbrook, above n 6, 214–15.

[72] Braucher, above n 3, 342, citing Jacob Ziegel, 'What Can the United States Learn from the Canadian Means Testing System?' (2007) *University of Illinois Law Review* 195, 206.

V THE FRESH START

Once we have put to one side using consumer bankruptcy as a collection device, we can focus more specifically on what bankruptcy law must do to ensure a fresh start. After reviewing the literature and the bankruptcy files of many debtors, it seems to me that debtors have three basic goals:

1. Both discharge of unsecured debt and retention of possessions generally seen as indispensable to starting over;
2. A mechanism for paying attorneys' fees and costs;
3. Miscellaneous fresh start relief (eg, protection of co-signers and truly voluntary repayment).

The most important component of the fresh start is the discharge. However, further relief is necessary in light of the existence of security interests in nearly all jurisdictions: procedures that permit debtors to retain certain property necessary to the debtor's basic needs and the ability to find work. Part of the retention of necessary property is met by exemption policy, which is beyond the scope of this paper. However, in Chapter 7 the retention of property necessary to a fresh start, including exempt property, is often precluded by outstanding liens.[73] In Chapter 7, encumbered property can be retained by agreement with the secured creditor, but such 'reaffirmations' are often onerous.[74] Debtors routinely file in Chapter 13 for the primary reason of keeping liened property,[75] but at the price of paying a formula amount of mostly unrelated unsecured debt over three to five years—a 'stale start' which is almost always onerous and often leads to repeated defaults.[76] The retention of necessary property should not be hostage to payment of debts to unsecured professional creditors. The property that falls into the essential category will vary around the world. For us, most often a car is necessary to keep a job or to pursue employment, and in many cases, there is not a better alternative for shelter than paying to keep an existing home.[77] In the United States, both cars and homes will routinely be subject to a security interest and a mortgage respectively; in effect, the grant of the lien is a waiver of any exemption of that property vis-à-vis the secured creditor. Chapter 13 is regularly understood as the solution to these problems.

[73] See generally Lawless et al, above n 6, 366–7, noting that families in bankruptcy often have assets, such as homes and vehicles, encumbered by secured loans.

[74] The lender is not required to agree to reaffirmation and often uses the debtor's need for the collateral to require addition of interest, late fees, and attorneys' fees, among other terms. Elizabeth Warren, Jay Lawrence Westbrook, Katherine Porter and John Pottow, *The Law of Debtors and Creditors: Text, Cases and Problems* (Aspen Press, 7th ed, 2014) 187–91.

[75] Ibid 215; repayments in Chapter 13 have several advantages, especially the opportunity to repay the debt in instalments. In some cases, it is possible for the debtor to 'strip' the security interest on personal property to reflect its current value.

[76] See Porter, above n 42.

[77] There are exceptions. A car may be a luxury for those who live in New York City and a home may be the 'cause' of the bankruptcy. Sullivan, Warren and Westbrook *The Fragile Middle Class*, above n 37, 143, 227. Blanket liens on household goods are not so much of a concern for us, because obtaining non-purchase-money liens on household goods is for the most part unlawful in the United States by a rule of the Federal Trade Commission: 16 CFR § 444.1. In addition, such liens are ordinarily subject to avoidance in a consumer bankruptcy: 11 USCA § 522 (West). On the other hand, vendors' liens are not avoidable and may encumber essential property like refrigerators.

Another important reason that debtors choose Chapter 13 is to pay attorneys' fees.[78] The Supreme Court has barred the use of estate property[79] in Chapter 7 to pay a debtor's lawyer.[80] The ordinary result is that debtors must pay the lawyer's fee in advance. Thus, we have the title of an important article, *Saving Up for Bankruptcy*.[81] For debtors who cannot arrange to pay in advance,[82] the instalment payment advantage in Chapter 13 is an important attraction.[83]

Finally, there is a miscellany of reasons for extended payment in bankruptcy. For example, a debtor may want to protect a mother who co-signed the note and may well be liable for the whole of it if the debtor discharges it. Chapter 13 provides an answer for this also in the form of the co-debtor stay.[84]

There has always been a concern to have a procedure enabling debtors to pay their debts voluntarily. The obvious response is that a debtor can always do that post-discharge on a truly voluntary basis. Yet there may be a few cases where debtors want to pay in full or large part, but are under great pressure from debt collectors and feel they need a mechanism to forestall creditors pending payment. It is not clear how often this problem arises, but it seems an important question to some observers. Again, Chapter 13 is presented as the solution.

VI THE POSSIBLE SHAPE OF REFORM

A *Reform Within the Existing System*

Katherine Porter has done a careful and persuasive study that was virtually unique in actually examining the outcomes of Chapter 13 cases in detail and is therefore enormously helpful.[85] In another ground-breaking investigation of Chapter 13 procedures, Porter, Patel, and Greene[86] have given us an important insight into who uses Chapter 13, as well as the chances for success for various types of users.[87] Their focus has been on the debtors, not the creditors, and their suggestions for possible reforms, subject to further research, are aimed at improving the existing system. The reforms they consider are important but less sweeping than those suggested in this article. They could be forgiven for thinking that I am politically naïve in proposing that collection should be reduced or eliminated as a goal in consumer bankruptcy. They might be correct in that, but it is my view that identification of the best answer is important in any movement for reform, even if our society ultimately settles for something less. Thus, with respect and admiration, I want to go further.

[78] See Porter, above n 42, 118–19.
[79] Estate property in the United States is all the debtor's property that is not claimed as exempt: 11 USCA § 541 (West).
[80] *Lamie v US Treasury*, 540 US 526, 538 (2004).
[81] See Mann and Porter, above n 6.
[82] See Warren et al, above n 74, 297.
[83] Keith M Lundin and William H Brown, *Chapter 13 Bankruptcy* (4th ed) Ch13online.com, § 38.3, <http://www.ch13online.com>, discussing the option to pay the filing fees in instalments, generally, early in the case.
[84] 11 USCA § 1301 (West).
[85] See Porter, above n 42.
[86] Greene, Patel and Porter, above n 6. They also provide a host of useful references to other empirical studies.
[87] Ibid 17, for example, they find a larger failure rate among black users.

B *The Simple Version of Reform*

To the extent policy makers are prepared to consider relief for debtors beyond reform of the existing system, I offer some suggestions framed for this discussion to fit the US system, but perhaps suggestive as applied to other bankruptcy regimes as well. In the US context, it seems to me that a simple extension of the Chapter 7 discharge injunction along the lines suggested below could accommodate the debtors' key goals. On that basis, Chapter 13 would be largely unnecessary given a de-emphasis on collection on behalf of unsecured professional creditors.

Except for the discharge, the most important item of fresh start relief in Chapter 7 is the retention of encumbered property. An extended discharge stay against lien enforcement would bar seizure and sale of that property during the case and would continue as long as the debtor was making whatever payments were required. The stay would give debtors a chance to cure arrears and pay off these debts. The discharge of all other debts would often make it possible. There are some things to be debated in adopting such a procedure in Chapter 7. In particular, would payments go directly to secured creditors or would trustees be involved in administration (probably yes); would the amount to be paid be the remainder of the original debt or the value of collateral at the time of bankruptcy; what procedures would be used to lift the stay and permit seizure; and how would this relief relate to exemption policy?[88] Each of those would involve important details and occasion spirited discussion, but all of these points could be resolved, it seems to me, without great technical difficulty. Chapter 13 could be 'seen off' in favour of the necessary additional provisions in Chapter 7, with the caveats noted below.

Similarly, fees and costs could be paid in instalments over some period of time set by statute, with the same sort of questions about procedures as with secured debt. If the debtor opted to pay over time, the discharge could be delayed until payment was complete, with the stay barring enforcement of pre-petition debts as with secured debt. This arrangement would solve the problem of saving up for bankruptcy as discussed above.

For those cases where the central motif is the payment of debts voluntarily or to protect co-signers, there would be tricky questions about the proper metric to determine when use of the stay is appropriate for those purposes and over what period of time. Given that these cases may be relatively rare, I am not sure that creation of some elaborate procedure is appropriate. It might be enough to issue a stay where the court finds the results fair all round and to nullify it on the same basis, creating a common law of the treatment of rare cases.

Finally, a reformer should address the problem of manifest abuse, if only to address the theoretical (or sound-bite) concerns of opponents of reform. A standard of manifest abuse would likely be acceptable, but if a more specific approach is wanted it might be adoption of an additional exception to discharge in liquidation: a) if clear and convincing evidence showed that the debtor had incurred debts with a present intention of non-payment; or b) if the debtor is solvent to pay creditors substantially in full, without regard to the value of exempt property,[89] under either the bankruptcy standard (balance sheet, at fair value) or the equity standard (ability to pay debts when due). Both standards have been applied with a fair measure of certainty for many decades. Some interesting questions would arise in the drafting, but nothing insurmountable.

[88] For example, in our bankruptcy system the opportunity to redeem encumbered property by paying the full outstanding debt in one payment is limited to exempt property: 11 USCA § 722 (West).
[89] Exempt here includes property otherwise not available to creditors, such as future bequests.

Most of the paperwork imposed by BAPCPA was unnecessary in the first place, and the adoption of a simple system would render it almost completely superfluous. The same is true of most of the extra obligations imposed on consumer attorneys. Coupled with payment of fees in instalments, a rollback of both the paperwork and the extra duties would likely reduce the cost of bankruptcy.

C *Narrower Reform*

1 *Smaller Creditors*

Some would object to the proposal I offer above because of concern for small, local creditors, especially individual lenders and suppliers of goods and services. The case against using bankruptcy as a mechanism for collecting consumer debt is not nearly so applicable to them. Creditors holding these sorts of debts may be found in too many consumer bankruptcies to be called rare. If careful study finds that to be true, provision could be made for paying them under existing Chapter 13 rules, including a modified version of the means test. Applying that test to debts that would generally be much smaller, and occur less often, would perpetuate the existing complexity and associated expense in those rules; and those rules might have somewhat more bite in some cases because debtors might be more able to pay the non-professional debts. However, a rule that eliminated the means test in any case not including such debts would likely dispense with the means test paperwork in most consumer cases. The removal of the means test would also make it likely consumers with such debts could and would settle them outside of bankruptcy altogether.

2 *Limiting Collection on Behalf of Professional Creditors*

Given the immense profits of the consumer credit industry, it seems unlikely to me that de-emphasising recovery for professional lenders would reduce any extensions of credit that a sensible policy maker would regret discouraging. But complete discharge of most professionally issued consumer debt may draw too much resistance. In that case, a more limited approach would nonetheless greatly improve the current system.[90] There are many possibilities. One would be to limit recovery by professional creditors to a certain dollar amount or a certain percentage of 'current monthly income' as defined by the Bankruptcy Code.[91] Or certain consumer debt issued by professional creditors could be disallowed for distribution. For example, the Code could disallow claims for credit extended after a serious default in payment to that creditor, pending a subsequent full reinstatement of the account. Another approach would be to disallow claims from creditors who set hopelessly unrealistic minimum payment levels that nearly guarantee their debtors would never be able to repay their balances fully.[92] At the least, those sorts of rules would reduce the amount of debt seeking repayment in Chapter 13. In addition, they might modestly deter irresponsible issuance of credit, narrowing the dimensions of the sweat box. However, it is also possible that bankruptcy losses are so relatively small compared to the benefits of marginal lending that professional lenders would make no adjustments in their models.

[90] Pottow, above n 55, 435–6, offered an intriguing proposal that creditors be liable for reckless lending as defined.
[91] 11 USCA § 101(10A) (West).
[92] See Mann, above n 50, 387, discussing credit card minimum payment levels that will result in a debtor taking decades to pay off the debt.

D *The Role of Lawyers*

A number of people over many years have observed that the great majority of consumer bankruptcies seem relatively simple. Given the absence of weighty legal issues in those cases, the natural thought is to relegate them to administrative resolution to save taxpayers, debtors, and creditors time and money.[93] Yet, Angela Littwin has argued persuasively that the presence of lawyers and judges who devote a significant part of their time to consumer bankruptcy has saved it from the ills associated with administrative procedures.[94] To summarise her case, she likens consumer bankruptcy to various social 'safety net' programs.[95] She discusses 'bureaucratic disentitlement,' a process that enables opponents of a social program to claim abuse by some users as an excuse for adopting procedural reforms that make the process substantially less available and less helpful to its intended beneficiaries.[96] She believes that the entrenchment of judges and lawyers in the consumer bankruptcy system,[97] together with the overlap in the United States between that system and business bankruptcy, which engages many affluent and influential lawyers, has helped to prevent bureaucratic disentitlement from being nearly as successful in bankruptcy as it has been in other social programs. This point obviously relates to the other article she has published about the success (and cost) of the bankruptcy bench and bar in adapting to the antidebtor provisions of BAPCPA. Thus she suggests that the natural reaction to the barrier of costs created by BAPCPA —assignment of most cases to an administrative agency—might be disadvantageous, because of the vulnerability of such a system to bureaucratic disentitlement.[98]

In addition to that very cogent point, the role of lawyers in consumer bankruptcy should continue because bankruptcy law is one of the most technically difficult and complex areas of the law. Although it would be a great improvement to simplify it,[99] its economic importance and its moral ambiguity combine to cause lawmakers to fill it with exceptions and qualifications,[100] a tendency exploited by various pressure groups. The suggestions I've made above would significantly simplify US law, but much complexity would remain. As long as consumer bankruptcy looks more like a Victorian desk and less like a Herman Miller table, it will be a task for lawyers and judges.

---

[93] See eg, David T Stanley and Marjorie Girth, *Bankruptcy: Problem, Process, Reform* (Brookings Institution, 1971) 44–5.

[94] See Angela K Littwin, 'The Affordability Paradox: How Consumer Bankruptcy's Greatest Weakness May Account for its Surprising Success' (2011) 52 *William and Mary Law Review* 1933, 2009–22. I do her article an injustice in the brief summary that follows, so I commend it to everyone who recognises the importance of the institutional side of consumer bankruptcy.

[95] Ibid 1938, 1944–6. Littwin seems at times to consider that this view is the correct one, one of our few points of disagreement on this subject.

[96] Ibid.

[97] Ramsay, 'Comparative Consumer', above n 62, 266, citing David A Skeel, *Debt's Dominion: A History of Bankruptcy Law in America* (Princeton University Press, 2001).

[98] Littwin, above n 94, 1940–41. Seeing the system institutionally, Littwin argues that 'when struggling, bankrupt consumers hand over much-needed funds to their lawyers, they are paying for more than representation in their individual cases. They are paying for the fact that much of the administrative work necessary to process their bankruptcies will be completed by people they have hired, rather than by government officials operating under the [political] pressures of bureaucratic disentitlement' (footnote omitted).

[99] See Jean Braucher, 'A Fresh Start for Personal Bankruptcy Reform: The Need for a Fresh Start and a Single Portal' (2006) 55 *American University Law Review* 1295.

[100] The drafting sessions must be filled with comments like this: 'But what if the debtor won the lottery soon after discharge? Well, let's say within 18 months of the discharge and ...'.

QUT Law Review
Volume 17, Issue 1, pp. 57–73

ISSN: Online-2201-7275
DOI: 10.5204/qutlr.v17i1.706

THE STORY BEHIND BANKRUPTCY: WHEN BUSINESS GETS PERSONAL

JENNIFER VAN KESTEREN, JAN ADRIAANSE,
JEAN-PIERRE VAN DER REST*

The number of bankruptcies in a specific period, and levels of debt, are well documented but little is known about the consequences of bankruptcies beyond the numbers. In this study, Dutch entrepreneurs who went through debt rescheduling after personal bankruptcy, were interviewed in order to gain an understanding of the private, personal and social implications of bankruptcy. Recently, systematic investigations of the implications of bankruptcy have been published. However, research has not yet taken the phenomenological experience of the bankrupt entrepreneur into account. Insights into these experiences are of critical importance for obtaining a comprehensive understanding of the impact of the bankruptcy process, and for engaging in a meaningful reform of bankruptcy law. During the interviews in this study, the entrepreneurs reflected on the early days of their business venture, the moment of first detecting the prospect of business failure, their personal experiences during business failure, and the aftermath of bankruptcy and debt rescheduling. The findings indicate that a bankruptcy experience can be compared to losing a loved one: a psychological process similar to mourning. The findings show that a lack of empathy, respect and transparency by formal institutional representatives such as judges, trustees and administrators is seen by the entrepreneurs as 'emotional punishment', and can be considered as a major source of their grief. Because of this grief, the bankruptcy and debt rescheduling experience can be extremely stressful causing severe psychological and physical distress. Implications for theory and practice are discussed.

I INTRODUCTION

In a study of 137 bankruptcies, Couwenberg and De Jong present evidence on the efficiency of the resolution of small and medium-sized firms in financial distress.[1] In the Dutch liquidation-based bankruptcy system, they found that, on average, total payouts to all creditors are 37 per cent of the total debt outstanding before bankruptcy. Other studies of defaulting firms in a liquidation procedure show similar results.[2] Although empirical work on the efficiency of reorganisation procedures report higher recovery rates, ranging from 43 per cent

* Jennifer Kesteren, BSc (Psych) (Leiden University), Researcher, Leiden Law School. Professor Jan Adriaanse, BBA (Nyenrode Business Universiteit), LLM, PhD (Leiden University), Professor of Turnaround Management and Head of Department of Business Studies, Leiden Law School. Professor Jean-Pierre van der Rest, BBA (Zuyd University), MA (Econ) (Durham University), PhD (Oxford Brookes University), Professor of Business Administration and Deputy Head of Department of Business Studies, Leiden Law School, Leiden University, The Netherlands.

[1] Oscar Couwenberg and Abe de Jong, 'Costs and Recovery Rates in the Dutch Liquidation-based Bankruptcy System' (2008) 26 *European Journal of Law and Economics* 105.

[2] See eg Karin S Thorburn, 'Bankruptcy Auctions: Costs, Debt Recovery, and Firm Survival' (2000) 58 *Journal of Financial Economics* 337; Julian R Franks, Kjell G Nyborg and Walter N Torous, 'A Comparison of US, UK, and German Insolvency Codes' (1996) 25 *Financial Management* 86; and Arturo Bris, Ivo Welch and Ning Zhu, 'The Costs of Bankruptcy: Chapter 7 Liquidation Versus Chapter 11 Reorganization' (2006) 59 *Journal of Finance* 1253.

in Finland[3] to 73 per cent in the United States,[4] it can be concluded that bankruptcies have considerable financial impact on creditors and on the economy as a whole. The prediction of business failure has, therefore, received wide research attention, for example in finance and accounting.[5] As Aziz and Humayon argue, 'the early detection of financial distress and the use of corrective measures (such as changes in corporate governance) are preferable to protection under bankruptcy law'.[6] Indeed, a parallel stream of business research can be observed focusing on corrective measures and prevention, such as studies on early warning signals, turnaround management, or other forms of informal reorganisation.[7]

While business failure has occurred throughout history, the recent economic climate has proven to be a driving force for the reform of insolvency regimes around the world. For example, through public consultations and intense legislative efforts, the European Commission has recommended a new approach to business failure and insolvency across the Union, which aims to rescue viable enterprises in financial difficulties, and to give honest bankrupt entrepreneurs a second chance.[8] Also, to encourage innovation, the Australian federal government has proposed improvements to its insolvency law, such as reducing the current default period for personal bankruptcy as a means of encouraging entrepreneurial development and reducing the stigma associated with personal bankruptcy.[9]

Peng, Yamakawa and Lee show that debtor-friendly bankruptcy laws have a pronounced effect on the development of entrepreneurship.[10] With ample attention for the consequences of bankruptcy law for innovation, entrepreneurship and economic growth from a societal perspective, there is, however, little focus, in research and policymaking, on the psychological, physical and social-psychological consequences of bankruptcy law, with one notable exception. Lee, Peng and Barney postulated that, 'in a society with a high level of stigma associated with bankruptcy, there will be less impact of an entrepreneur-friendly bankruptcy law on entrepreneurship development'.[11]

Therefore, in this article we aim to gain an understanding of the private, individual and social implications of bankruptcy by exploring how an entrepreneur experiences the bankruptcy and debt rescheduling process. Insights into these experiences are of critical importance for a comprehensive understanding of the impact of bankruptcy procedures, and for engaging in a

---

[3] Stefan Sundgren, 'Does a Reorganization Law Improve the Efficiency of the Insolvency Law? The Finnish Experience' (1998) 6 *European Journal of Law and Economics* 177.

[4] Elizabeth Tashijan, Ronald C Lease and John J McConnell, 'Prepacks: An Empirical Analysis of Prepackaged Bankruptcies' (1996) 40 *Journal of Financial Economics* 135.

[5] Nico Dewaelheyns, Sofie De Prijcker and Karen Van Den Heuvel, 'Predicting Business Failure' in Jan A A Adriaanse and Jean-Pierre I van der Rest (eds), *Turnaround Management and Bankruptcy* (Routledge, 2017) 66.

[6] M Adnan Aziz and Humayon A Dar, 'Predicting Corporate Bankruptcy: Where We Stand?' 2006 6 *Corporate Governance* 29.

[7] See eg Jan A A Adriaanse and Hans J Kuijl, 'Resolving Financial Distress: Informal Reorganization in The Netherlands as a Beacon for Policy Makers in the CIS and CEE/SEE Regions?' (2006) 31(2) *Review of Central and East European Law* 135.

[8] European Commission, *Commission Recommendation on a New Approach to Business Failure and Insolvency*, C (2014) 1500 final (12 March 2014) <http://ec.europa.eu/justice/civil/files/c_2014_1500_en.pdf>.

[9] National Innovation and Science Agenda (Aust), *Improving Bankruptcy and Insolvency Laws: Proposals paper* (The Treasury, 2016) <https://www.treasury.gov.au/ConsultationsandReviews/Consultations/2016/Improving-bankruptcy-and-insolvency-laws>.

[10] Mike W Peng, Yasuhiro Yamakawa and Seung-Hyun Lee, 'Bankruptcy Laws and Entrepreneur-friendliness' (2009) 34 *Entrepreneurship Theory and Practice* 517.

[11] Seung-Hyun Lee, Mike W Peng and Jay B Barney, 'Bankruptcy Law and Entrepreneurship Development: A Real Options Perspective' (2007) 32 *Academy of Management Journal* 266.

meaningful reform of bankruptcy law. In this way, the article contributes to the literature by exploring empirically, at the individual level, how adverse consequences of insolvency law can be elevated as a means to foster and promote entrepreneurship.[12] The article is structured as follows: in the next section, the literature is reviewed to establish a framework for data analysis. The methodology is explained and justified in the following section. This is followed by the findings, and the final section provides the main conclusion and discusses implications for theory and practice.

II THEORETICAL FRAMEWORK

What makes people successful entrepreneurs has attracted considerable interest in entrepreneurship and psychology.[13] Successful entrepreneurs often are higher in need for achievement, more innovative, have a higher risk-taking propensity and stronger internal locus of control.[14] How entrepreneurs deal with failure has also attracted considerable research attention. Ucbasaran, Shepherd, Lockett and Lyon have synthesised and structured this literature, focusing on the individual response to business failure. They conceptualise life after failure 'as a journey in which making sense of and recovery from failure is a process that unfolds over time'. We have reviewed this journey and have selected it as a framework for the analysis of the qualitative interviews. The journey consists of three stages including 'the aftermath' of failure, sensemaking and learning processes, and 're-emergence'.[15]

The first stage involves three aspects of the 'aftermath': financial, social and psychological. Ucbasaran et al outline a number of findings relevant to our study.[16] First, Arora and Nankumar find that entrepreneurs with significant outside opportunities are likely to be more impatient for success, even if this also implies failing more quickly.[17] Moreover, DeTienne, Shepherd and DeCastro find that environmental munificence, personal investment, significant outside opportunities, prior business success, and perceived collective efficacy of the business, are factors that make entrepreneurs decide to persist despite poor performance.[18] They also find a negative relationship between entrepreneurs' extrinsic motivation and the factors that

[12] See eg, Alan Schwartz, Barry Adler and Ben Polak, 'Regulating Consumer Bankruptcy: A Theoretical Inquiry' (2000) 29 *Journal of Legal Studies* 585.

[13] See Robert Hisrich, Janice Langan-Fox and Sharon Grant, 'Entrepreneurship Research and Practice: A Call to Action for Psychology' (2007) 62 *American Psychologist* 575.

[14] Christopher J Collins, Paul J Hanges and Edwin A Locke, 'The Relationship of Achievement Motivation to Entrepreneurial Behavior: A Meta-analysis' (2004) 17 *Human Performance* 95; W H Stewart and P L Roth, 'Data-quality Affects Meta-analytic Conclusions: A Response to Miner and Raju (2004) Concerning Entrepreneurial Risk Propensity' (2004) 89 *Journal of Applied Psychology* 14; Andreas Rauch and Michael Frese, 'Let's Put the Person Back into Entrepreneurship Research: A Meta-analysis on the Relationship Between Business Owners' Personality Traits, Business Creation, and Success' (2007) 16 *European Journal of Work and Organizational Psychology* 353.

[15] Deniz Ucbasaran et al, 'Life after Business Failure: The Process and Consequences of Business Failure for Entrepreneurs' (2013) 39 *Journal of Management* 166. See also Melissa S Cardon and Rita Gunther McGrath, 'When the Going Gets Tough ... Toward a Psychology of Entrepreneurial Failure and Re-motivation' (Paper presented at the Frontiers of Entrepreneurship Research Conference, Babson College, 1999) <https://fusionmx.babson.edu/entrep/fer/papers99/I/I_B/I_B.html >.

[16] Ucbasaran et al, above n 15.

[17] Ashish Arora and Anand Nandkumar, 'Cash-Out or Flame-Out! Opportunity Cost and Entrepreneurial Strategy: Theory and Evidence from the Information Security Industry' (2011) 57 *Management Science* 1844.

[18] Dawn R DeTienne, Dean A Shepherd and Julio O De Castro, 'The Fallacy of "Only the Strong Survive": The Effects of Extrinsic Motivation on the Persistence Decisions for Under-Performing Firms' (2008) 23 *Journal of Business Venturing* 528.

contribute to this escalated commitment.[19] Second, Cope finds that the inability to repay debt generates feelings of guilt, which can lead to social distancing and withdrawal 'due to an inability to share concerns with others'.[20] Third, Ucbasaran et al argue that 'business failure has parallels with the loss of something (or someone) important'.[21] In addition, failure generates a sense of 'helplessness' and, beyond a certain point, loss of faith. The second stage comprises responses to failure, which Ucbasaran et al classify as learning and sensemaking. First, Shepherd argues that only when entrepreneurs understand why they lost their business, can they start learning how to run a business differently in the future.[22] Cope argues that such learning is unlikely to occur immediately as entrepreneurs need time to recover from the grief associated with the failure. Moreover, Cassar and Graig find that hindsight bias affects this process of critical reflection.[23] Second, Shepherd argues that being drawn too much to grief emotions may adversely affect the sensemaking process. Schwand notes that if these emotions induce the protection of self-esteem, sensemaking may be hindered as well. Finally, the third stage relates to the long-term outcomes of failure: recovery, cognition, and future behaviour. First, there is a positive relationship between the processing of grief and the speed of recovery. Cope concludes that this relationship is mediated by three interrelated phases: (a) entrepreneurs psychologically distance themselves so as to heal from the failure; (b) critical reflection to make sense; (c) reflective action in order to move on. Second, Hayward et al find that entrepreneurs' widespread overconfidence in their capabilities makes them also more equipped to recover from the grief over a lost business.[24] Third, while there is literature that relates business failure to the intention to restart subsequent business, Ucbasaran et al argue that there is no research actually testing this relationship. Instead, Ucbasaran, Westhead and Wright find that failed entrepreneurs identify new business opportunities, but are not capable of exploiting opportunities that are more innovative.[25]

III METHOD

A *Research Design*

The exploratory nature of the research topic required a qualitative research design, as intricate details about the phenomenological experiences of bankrupt entrepreneurs were to be explored, such as feelings, thought processes, and emotions. These would have been more difficult to obtain using a quantitative design.[26] In addition, the qualitative design was valuable when gaining an understanding of the personal context within which the bankrupt entrepreneurs acted.[27] Semi-structured open-ended interviews were held with 11 Dutch entrepreneurs: nine

[19] Escalation of commitment refers to a tendency to escalate commitment to a previous course of action even when this is unwise, see for example, Dustin J Sleesman et al, 'Cleaning Up the Big Muddy: A Meta-Analytic Review of the Determinants of Escalation of Commitment' (2012) 55 *Academy of Management Journal* 541.
[20] Jason Cope, 'Entrepreneurial Learning from Failure: An Interpretative Phenomenological Analysis' (2011) 26 *Journal of Business Venturing* 611.
[21] Ucbasaran et al, above n 15.
[22] See Dean A Shepherd, 'Learning from Business Failure: Propositions of Grief Recovery for the Self-employed' (2003) 28 *Academy of Management Review* 318.
[23] Gavin Cassar and Justin Craig, 'An Investigation of Hindsight Bias in Nascent Venture Activity' (2009) 23(2) *Journal of Business Venturing* 149.
[24] Mathew L A Hayward et al, 'Beyond Hubris: How Highly Confident Entrepreneurs Rebound to Venture Again' (2010) 25 *Journal of Business Venturing* 569.
[25] Deniz Ucbasaran, Paul Westhead and Mike Wright, 'The Extent and Nature of Opportunity Identification by Experienced Entrepreneurs' (2009) 24 *Journal of Business Venturing* 99.
[26] See Juliet Corbin and Anselm Strauss (eds), *Basics of Qualitative Research: Techniques and Procedures for Developing Grounded Theory* (SAGE, 1998).
[27] See Joseph A Maxwell (ed), *Qualitative Research Design: An Interactive Approach* (SAGE, 1996).

with a sole proprietorship, who had been declared personally bankrupt because of business insolvency; and two with a limited company, who had experienced corporate bankruptcy.[28] All entrepreneurs had subsequently considered, filed for or gone through debt rescheduling. Face-to-face interviews were conducted to find out how the entrepreneurs coped with the bankruptcy experience. Informed consent, confidentiality, and rules of conduct were discussed prior to each interview. All interviews were recorded and transcribed (edited verbatim) with consent. The interviewees were encouraged to be completely open about their experiences in their own way. The interviewer returned the interview to its anticipated course (ie, research protocol) when necessary, 'but not so rigid as to preclude his or her obtaining some unexpected information'.[29] Given the sensitive nature of the interview topic, as it intruded into the private sphere and delved into the deeply personal experience of the entrepreneur,[30] it was anticipated that some interviewees could express particularly strong emotions during the interviews (eg, intense crying). The interviewer, therefore, prepared herself when it came to emotional labour,[31] which involved handling her emotions while 'managing the outward displays of emotions according to the situation'.[32] The interviews were conducted in the final quarter of 2015 and each lasted approximately two hours.

B *Sample*

Data collection was facilitated by one of the largest debt counselling firms in the Netherlands. The firm agreed to provide access to its clients providing that confidentiality and anonymity were guaranteed. Access was particularly useful as it was anticipated that it would be relatively difficult to find entrepreneurs (mostly with a proprietorship) whose businesses were bankrupt and who had subsequently filed for or gone through personal bankruptcy (debt rescheduling). Clients were invited by e-mail to voluntarily agree to participate in the study.

Table 1: Overview of Bankruptcy Cases

Case	Sector	Legal Form	Size	Years in Business	Bankruptcy Declared After	Warning Signs	Year of Bankruptcy
A	Café/diner	Sole proprietorship	16	28	Decrease in turnover and introduction of smoking ban (debt accumulation)	2010	2014
B	Day-care	Sole proprietorship	23	23	Turnover decreased significantly due to the financial crisis (debt accumulation)	2008	2014
C	Cable Installation	Sole proprietorship	11	7	A major client could not pay the labour	2010	2011

[28] At the design stage, focusing on debt rescheduling, the appropriateness of lumping together insolvent sole proprietors with owners of insolvent limited companies was considered. Given how little guidance is available in the literature, and the exploratory nature of the study, we proceeded. A post hoc examination of the findings revealed no indications of meaningful differences (see also Table 3, cases D and H).

[29] John M Johnson and Timothy Rowland, 'The Interpersonal Dynamics of In-depth Interviewing' in Jaber F Gubrium et al (eds), *The SAGE Handbook of Interview Research* (SAGE, 2012) 107.

[30] See Claire M Renzetti and Raymond M Lee (eds), *Researching Sensitive Topics* (SAGE, 1993).

[31] Emotional labour refers to the management of feelings to create a facial and bodily display needed to fulfill the emotional requirements of a job. See Arlie Russell Hochschild (ed), *The Managed Heart: Commercialization of Human Feelings* (University of California Press, 1983).

[32] Annika Lillrank, 'Managing the Interviewer Self' in Jaber F Gubrium et al (eds), *The SAGE Handbook of Interview Research* (SAGE, 2012) 287.

Case	Sector	Legal Form	Size	Years in Business	Bankruptcy Declared After	Warning Signs	Year of Bankruptcy
					performed (debt accumulation)		
D	Landscaping	Private company*	9	3	Employee absence due to illness causing financial problems (debt accumulation)	2014	2015
E	Desktop publishing	Sole proprietorship	20	21	Market changed (digitisation) and interests of the owner changed (debt accumulation)	2010	2012
F	Electric installation	Sole proprietorship	6	5	Turnover significantly reduced due to the financial crisis (debt accumulation)	2010	2012
G	Day-care	Sole proprietorship	3**	10	A creditor did not agree to the suggested payment plan (debt accumulation).	2011	2015
H	Construction	Private company*	40	6	Banks could or would not finance growth (debt accumulation)	—	2009
I	Taxi	Sole proprietorship	18	5	Turnover significantly reduced due to the financial crisis and the lack of bad weather in the harvest months (debt accumulation)	2009	2014
J	Restaurant	General partnership	n/a	10	Disappointing revenue after re-opening as city imposed 9 month compulsory closure due to construction of underground subway (debt accumulation).	2011	2013
K	Retail	Sole proprietorship	7	11	Turnover significantly reduced due to the financial crisis and moving to a larger location without enough equity (debt accumulation)	2009	2012

* = filed for debt rescheduling after corporate bankruptcy. Size = number of employees. ** = number of locations.

Using a purposive heterogeneous sampling technique, 11 clients were selected from those who responded to the e-mail invitation. Cases vary in markets served, size, age, cause and date of bankruptcy (see Table 1). The logic and power of purposive sampling lay in selecting information-rich cases for in-depth study.[33] The heterogeneous approach was used to enable identification of the key themes that could be observed.[34]

[33] See Michael Quinn Patton (ed), *Qualitative Research and Evaluation Methods* (SAGE, 2014).
[34] See Mark Saunders, Philip Lewis and Adrian Thornhill (eds) *Research Methods for Business Students* (Pearson Education, 2013).

As the number of interviewees in similar studies[35] ranged between six and eight, following Francis et al, eight interviews were initially planned and three more interviews were conducted to achieve data saturation.[36] Interviewees were predominantly male, aged between 35 and 69 years, with secondary or vocational education and no prior businesses experience, and whose personal bankruptcy had been converted into a debt rescheduling scheme for natural persons (see Table 2).[37]

Table 2: Interviewee Sample

Case	Age	Gender	Civil Status	Education	Entrepreneurial Experience	Personal Bankruptcy*	Work Status
A	57	Male	Divorced	Higher Education	None, first business	Since 12 months	Jobless
B	64	Female	Married	Higher Education	None, first business	Since 8 months	Self-employed
C	69	Male	Married	Vocational Education	Since 1971, one prior bankruptcy	Completed	Retired
D	Mid-30s	Male	Married	Vocational Education	None, first business	Not applicable	Self-employed
E	54	Female	Cohabiting	Higher Education	None, first business	Since 31 months	Self-employed
F	61	Male	Married	—	Since 1992, one prior bankruptcy	Since 18 months	Sickness Benefit
G	64	Male	Married	—	None, first business	Since 3 months	Jobless
H	Early -40s	Male	Divorced	—	Yes, sold multiple businesses before	Inadmissible	Self-employed
I	60	Male	Married	Secondary Education	None, first business	Since 6 months	Self-employed
J	45	Male	Single	—	None, first business	Since 9 months	Employed
K	45	Male	Married	Secondary Education	None, first business	Since 16 months	Employed

* Wet Schuldsanering Natuurlijke Personen [Natural Persons Debt Rescheduling Act]: maximum three years.

C *Data Analysis*

To rearrange and analyse the collected data systematically, the interviews were disaggregated into meaningful and related parts in the original Dutch language.[38] These parts or categories were taken from Ucbasaran et al's 'scheme for research on entrepreneurial business failure', including 'aftermath' (financial, social, psychological costs), social psychological processes (learning, sensemaking), and outcomes (recovery, cognitive, behavioural), and guided by the

[35] See eg, Jason Cope, Frank Cave and Sue Eccles, 'Attitudes of Venture Capital Investors to Entrepreneurs with Previous Business Failure' (2004) 6 *Venture Capital: An International Journal of Entrepreneurial Finance* 147; Smita Singh, Patricia Corner and Kathryn Pavlovich, 'Coping with Entrepreneurial Failure' (2007) 13 *Journal of Management and Organization* 331; and Cope, above n 20.

[36] See Jill J Francis et al, 'What is an Adequate Sample Size? Operationalizing Data Saturation for Theory-based Studies' (2010) 25 *Psychology and Health* 1229.

[37] The Dutch Bankruptcy Act provides for the following insolvency procedures: (1) bankruptcy; (2) suspension of payments (in Dutch: Surseance); and (3) debt restructuring for private individuals (in Dutch: Wet Schuldsanering Natuurlijke Personen (WSNP) [Natural Persons Debt Rescheduling Act]). The bankruptcy procedure (1) includes both personal bankruptcy (ie, natural person) and corporate bankruptcy (ie, private legal entity). Personal bankruptcy and WSNP are two separate judicial rulings that cannot coexist (in the Netherlands). As such, 'when a conversion of the personal bankruptcy into natural persons debt rescheduling has occurred, the personal bankruptcy ends': Reinout D Vriesendorp, *Insolventierecht* (Kluwer, 2013) 325 [translated].

[38] See Saunders, Lewis and Thornhill, above n 34.

exploratory purpose of the research.[39] Textual parts of the interview data were subsequently labelled and placed in categories. To enhance the credibility of the findings, investigator triangulation[40] was applied to verify the initial categories and to rectify potential miscategorisation of the interview data. The data analysis was carried out manually as it was felt that by keeping close to the data a certain degree of proficiency could be gained.[41] The report of findings (see below) was completed fully in Dutch, before it was translated by a licensed academic translator and independently cross-validated by the three authors.[42]

IV FINDINGS

A *Bankruptcy Experience*

The bankruptcy experiences of entrepreneurs illustrate that business failure is a phenomenon with profound personal and social consequences. The findings reveal multiple interlinked psychological, physical and social effects. The legal bankruptcy and debt rescheduling procedures, and their key representatives, such as the judge and bankruptcy trustee [*In Dutch: curator*], play a surprising role in the processing of these consequences. To describe and explain this role, the bankruptcy / debt rescheduling experience will first be analysed.

Ex-ante: in the run-up to a bankruptcy, entrepreneurs can lose their motivation; they don't answer their emails, get behind on their administration, and generally just let things go. They are worried about what is going to happen, both for themselves and their families. There is a lot to think about. This results in sleepless nights, making them emotionally unstable, tense and unpredictable, while at the same time, they are unable to rest:

> You don't start up a company to go bankrupt, so you're constantly trying not to go bankrupt [Case A].

Entrepreneurship is no longer any fun. The entrepreneur only works to keep those who want money (staff, suppliers) off his or her back. The entrepreneur's moral obligation to want to pay debts should not be underestimated:

> I really suffered from the fact that I was unable to pay those who had placed their faith in me. I've had many sleepless nights about them, my staff and suppliers. [Case G]

> We had everything properly completed before we filed for bankruptcy, so we weren't in debt to anyone in [name of city]. The [name of bank], the tax authorities and [name of other bank] were all we owed money, but I didn't lose any sleep over them. We made sure we paid off anyone who would have really suffered. [Case I]

There is a continuous search for solutions, time and money. For example, attempts are made to arrive at amicable settlements, money is found from every possible source, savings are made on staff costs, or an external manager is appointed who can turn the situation around. There are even indications regarding an escalation of commitment:

---

[39] See Ucbasaran et al, above n 15.
[40] See Patton, above n 33.
[41] See Eben A Weitzman, 'Software and Qualitative Research' in Norman K Denzin and Yvonna S Lincoln (eds), *The SAGE Handbook of Qualitative Research* (SAGE, 2000) 803.
[42] See Bugusia Temple and Alys Young, 'Qualitative Research and Translation Dilemmas' (2004) 4 *Qualitative Research* 161, for a discussion of the epistemological implications of translation and the methodological consequences of involving a translator in research.

> I'd agreed a plan with [debt counselling firm] in which I would have been able to repay all my creditors within three years, however one didn't agree. That's really hard — you're completely powerless at that moment; you're forced to close down your business while it still had a chance of survival. [Case G]

And, as the entrepreneur's stress levels increase, the staff become increasingly demotivated, resulting in a downward spiral.

In Media Res: when personal bankruptcy is imposed by court order, a wide range of emotions can be observed. For one person, this can be resignation or relief, for another it is a truly bitter pill, and for yet another, bankruptcy can come totally out of the blue. For all the entrepreneurs, however, it can be associated with a deep sense of humiliation:

> What I found most painful was that I had to fight to get into the WSNP [Natural Persons Debt Rescheduling Act]. The judge doubted whether I had acted in good faith and that means your honesty is in question: that really hurts and I really hated that. After bankruptcy, you become a sort of public property. [Case E]

> Well, you know, this type of occurrence is, for those like the judges and lawyers involved, apparently the most natural thing in the world. When I went bankrupt, the lawyer of the pension fund involved was there, and he was completely uninterested, and even though I know that the judge is just doing his job, it could be done differently. Look, in my [name of sector] respect was one of our most important values, and I completely missed that in the courtroom, during the bankruptcy, and from the trustee and everything that went with it. You're just a number and you're considered to be a villain, 'because they all are'. [Case G]
> The worst thing I experienced, apart from the effect on my private life, was that in a public sitting, with students and everyone watching, that the judge declared me to be personally bankrupt. And then, on the same evening, the trustee shows up. You feel totally screwed, and then this turns to anger. [Case H]

It is a phase in which entrepreneurs become emotionally exhausted, and they and their partners suffer from psychological and physical problems:

> My innate kindness completely disappeared, I became a fiend. Every night my wife woke up screaming. Terrible dreams; it wasn't a good period. [Case I]

A frequently mentioned and related problem is that the settlement of the bankruptcy in the eyes of entrepreneurs takes far too long (for example, two and a half years). For a number of entrepreneurs, the demands of the debt rescheduling scheme at that time are also often too much.

Ex-post: a few months after their debt rescheduling ruling, the entrepreneurs settle down in somewhat quieter waters. In addition to frustration, fear and uncertainty about the future, there is an overriding sense of helplessness. There are several ways in which this can be dealt with:

> A great sense of anger, and more than just a little irritation about the trustee and his actions. [Case D]

> Very grateful that the [debt rescheduling scheme] was in place, but it's a financial prison. You do get used to it, because resistance is futile, but it's no fun. [Case E]

> I was really down, because the company was more about ideology than about making a profit. When I heard I'd spend three years in debt restructuring, I thought, oh well, we'll be fine. But the idealism had gone, and that's what was worst. [Case G]

There are situations where the future looks more positive and opportunities arise, for example in those cases where good guidance was provided, such as in the taxi case:

> You just asked me about what it does to a person's self-esteem. Well, at the time I actually got my own life back again, at least that's what it felt like. I now get into the car every morning with just as much pleasure; it's my hobby. [Case H]

B *Effects of the Bankruptcy Experience*

The findings uncover multiple interlinked psychological, physical and social effects (summarised in Table 3). It is striking to see how severe the suffering — which included heart attack, alcohol abuse, suicidal tendencies and divorce — was in each of these cases.

Table 3: Effects of Bankruptcy Experience on Life

Case	Psychological	Physical	Private	Social
A	Diagnosed burn-out. Has been suicidal after bankruptcy	Stress-induced heart attack after bankruptcy	Divorced during final years of the business. Currently no contact with ex-wife and daughter. Ties with siblings have improved	Loss of many friends and contacts
B	Grief, loss of self-esteem, fear of being dependant again, feeling worthless	Exhaustion	Husband and daughter very supportive	Two ex-employees / friends refuse contact, other friendships have remained strong
C	Some anxiety, feeling in control	No change	Wife and children very supportive. No blame	Social network remains supportive
D	Grief, near burn-out, anxiety over incoming mail, depressed, apathetic	Weight loss, sleeplessness	Wife and children very supportive. Feels guilty for the increased tension in household	Social network remains supportive
E	Memory loss, anxiety over incoming mail, loss of self-esteem	Physical discomfort, feeling disassociated from self	Divorced before business strain and bankruptcy. Feeling guilty towards daughters for not being able to financially support them now that there are growing up	Bankruptcy brought her closer together with friends
F	Feeling helpless, frustrated, anger, rumination, feeling lonely	Sleeplessness	High marital strain. Redirecting anger and frustration on wife and vice versa. Good relations with children. Family bonds damaged	Relations with friends superficial. Anxiety to reach out to / be seen by familiar people
G	Grief, depressed feeling, losing ideals		Wife and children very supportive. No blame. Increased family bonds	Strengthening effect on relationships with friends
H	Grief, feelings of disappointment towards family	Weight loss, abscess in foot, stress-induced heart attack after bankruptcy	Divorced during venture failure. Now single parent (two children). Family bonds damaged and lost.	Loss of many friends, but other relationships strengthened.

Case	Psychological	Physical	Private	Social
I	Grief, loss of self-esteem, fear of facing people	Alcohol abuse	High marriage strain. Wife's health decreased significantly. Sleeplessness, depression and psychoses. No family bonds. Relationship with daughter is good.	Loss of friends. Superficial contacts remain
J	Anxiety, frustration		Relationship with girlfriend ended during venture failure. Family is supportive	Loss of some friends, strengthening relationships with others
K	Grief, frustration, feeling insecure, anxiety	Sleeplessness, nausea, exhaustion	Divorced during last years of business	Relationships turned superficial. Feels judged on how he lives after bankruptcy

As a first key theme, and given that the psychological consequences are far-reaching — such as burn-out, anxiety, loss of self-esteem, depression, and not least, grief — the findings indicate that family and friends play an important role in how the bankruptcy experience and the mourning are processed emotionally. In this context, the exploratory findings indicate that the formal legal bankruptcy proceeding can contribute negatively to the psychological and physical distress of business failure, as is explained in the following section.

C *Bankruptcy Procedure*

The findings indicate that entrepreneurs feel insecure and anxious about the legal procedure because they often have no idea what their rights and obligations are: [43]

> The process is opaque and literally and figuratively completely incomprehensible. As an entrepreneur, you no longer seem to have any rights, and you are at the mercy of the whims of the trustee and your lawyer. You have to pay for help, but you're bankrupt: So where do you get the money? [Case D]

Because a personal bankruptcy and a debt rescheduling scheme for entrepreneurs are unknown and complex processes, they are highly dependent on the resources in their immediate vicinity (ie, legal aid or lawyers, bankers, accountants). If they cannot communicate well with these resources, they can easily fall into an 'emotional pit'.

> Everyone wants to feel seen and heard. How you do something is a much greater determinant than what you do. So when people are 'rolling over you' like you're a small, naughty child ... you react to this emotionally. You actually need someone who says, 'I believe in you and I'll do my best to help you when needed'. You have to manoeuvre between what you need to do to take care of yourself, and not kicking the shins of the administrator [in Dutch: bewindvoerder] or trustee. [Case E]

When entrepreneurs gain more insights into their rights and obligations, or as one interviewee put it 'if you have already been bankrupt once', then they seem to know more of what to expect,

[43] A lack of comprehensibility of court hearings (in general) for the general public has been a subject of recent scholarly debate in the Netherlands; eg, see Michiel Glas and Paul Verweijen, 'Op Gelijke Voet: Een Verkenning van de Mogelijkheid van een Heroriëntatie van de Positie van de Officier van Justitie in de Rechtszaal' ['On an Equal Footing: An Exploration of the Possibility of a Reorientation of the Position of the Prosecutor in Court'] (2014) 24(1175) *Nederlands Juristenblad* 1612.

and are no longer driven so much by these feelings of anxiety. The following comments illustrate how good coaching can contribute to this:

> I had guidance from an SME consultant, a friend of ours. This was a particularly pleasant experience. Something as dramatic as this is something you can't deal with alone; not before nor after. It interferes with your sense of security and your self-image. You may have debt rescheduling, but you miss an emotional safety net. [Case B]

> We had a really good trustee to whom we could talk, as well as my accountant. They were a great company and became personally involved. We had discussions about how it was going and about what had happened. They tried to see things from our point of view; they were really nice people. You still have to find the solutions yourself. There's still a lot of bad feeling, but we hope that at the end of the debt rescheduling, the judge will provide safeguards. [Case I]

However, communication is often far from perfect, and there is little or no direct contact. In some cases, entrepreneurs may have to deal with four or five different trustees, and contact often only occurs via email or the secretary.

> Contact with our first trustee was terrible. It was very confrontational and business-like, while I was terribly emotional. I was pretty much treated like a criminal. They really don't look at who you are and what you did to make sure everything would be resolved. However, the second trustee, a woman, was someone I could get along with. [Case B]
> I feel totally screwed by the trustee. He spares nothing and no one, he has absolutely no feelings, he's a hard case and he's really out to get you. Your business is bankrupt, your dream has gone, and the trustee seems only to be interested in sticking a knife in your back. [Case D]

> If I was the trustee, I'd always keep in mind that indeed, some people do try to get away with murder, but others happen to go bankrupt through sheer bad luck, so don't start off with a prejudice. First of all ask, 'how are things, and how's it affecting you'. No, in most cases it seems to be all about getting what you can, because then their billable hours are safe. That's really what happens; they're only interested in making money, and that's clear from the arrogant way they talk down to you. They walk all over you, emotionlessly, they walk through your home and 'suck it empty', only asking you about your kid's savings accounts. That's how far they go — how sad is that? It's all negative energy, the whole system. These people seem to think they're sitting on a throne. [Case H]

A second key theme that emerges from the interview data is that entrepreneurs often have a need to be heard, and they do not understand why the legal process should be as devoid of emotion as it is. It feels like an 'emotional punishment', often because they are unable to let go of their business:

> It was May, and we could have kept the shop open for another six months, because then we could have earned about 3–4 times the amount that the trustee raised. This gives you the feeling that this guy is only working for himself instead of for me or the creditors on the other side. [Case K]

These entrepreneurs need emotional and psychological support. Their bankruptcy experience is comparable to losing a loved one; it is a psychological process similar to mourning. A lack of empathy, respect and transparency by the formal institutional representatives, such as judges, trustees and administrators, is an additional source of their grievance. In their eyes, it is unfair and incomprehensible that the legal system only works for the creditors and not for them. Because of this perceived non-cooperative, emotion-free treatment, the bankruptcy proceeding

can be an extremely stressful grieving process, beside the emotions associated with business failure itself, contributing to the psychological and physical distress.

D *Stigma, Learning, Second Chance Experience and Current Situation*

Those entrepreneurs whose failure has not been made public usually experience less social stigma, even within their own business network. Some find the 'business stigma' the worst thing of all; they expected that their business contacts would treat them with as much compassion as they themselves did when one of their contacts went insolvent. What is really striking is that in the view of the entrepreneurs it is the judicial system itself that brands them with this stigma:

> You're bankrupt, so then you're treated like a criminal. That's especially what I felt when I met the first trustee and the administrator. No one looks at who you are and what you've done; you miss any form of personal recognition. They don't see you for who you are and what you've done, you miss that recognition. Socially, stigma was only experienced from two former employees. [Case B]

Furthermore, the findings indicate that entrepreneurs certainly learn from their bankruptcy experience. Common pitfalls that they identified are managing costs (mainly staff costs), poor cash flow management, excessive external financing, or an over-reliance on a few major customers. In addition, some entrepreneurs have learnt to be aware more quickly of the things they are weak at, and get others involved in time. They also may no longer consider starting a sole proprietorship, instead they will set up a limited company, and will no longer co-sign for the debt of that company. So, many entrepreneurs emerge stronger from their bankruptcy. Moreover, all entrepreneurs indicate that after the debt rescheduling, they really want to continue being an entrepreneur:

> I'm not allowed to start up anything new thanks to the WSNP [Natural Persons Debt Rescheduling Act], but I'm constantly thinking about it. Despite the bankruptcy, my mind-set hasn't changed. It's a bit difficult to explain, but that's what I think about, 24 hours a day. [Case A]

> I'd love to start another business again. Nothing big, but a small company where I can share my experiences, for example in the form of courses and workshops. You don't need to invest that much, there's no need for an office, equipment and/or staff, nothing like that. To do this, you have to send in a request to the magistrate involved, and I did that months ago, but I've heard nothing since. I think that's stupid. You're made to feel incredibly small and terribly mistrusted, and that really gets to me. Your whole life is characterised by other people's distrust and disdain; that's something I have trouble dealing with, because there's no reason for it. [Case G]

While waiting for the completion of their three-year debt rescheduling scheme, the reality is that none of these entrepreneurs have actually started up a business.

V DISCUSSION AND IMPLICATIONS

The interview data reveal two interrelated key themes. First, entrepreneurs who are in a debt rescheduling scheme after being declared bankrupt generally cannot personally let go of their demised business. They have a need to be heard, and cannot understand why the legal process is so devoid of emotion and so hostile to their personal interests. They feel this as 'emotional

punishment', which hinders the way they cope with their loss. The lack of empathy, respect and transparency of the legal system and its representatives is an additional source of grief, contributing negatively to the already existing psychological and physical distress of the business failure. Secondly, support — in the form of family, friends, and business contacts — plays an important role in how a bankruptcy experience, debt rescheduling scheme and the mourning over the lost business are processed emotionally. In this context, it seems counter-productive that the legal system itself is perceived to impose a stigma on these entrepreneurs. Whether this perception results from the legal system imposing the stigma itself, or from entrepreneurs projecting onto this system their own sense of stigma — for example by projecting their own emotions onto the formal actors in the legal system — needs to be examined further.

A *Implications for Theory*

A review of the literature shows that after a bankruptcy, entrepreneurs bear personal financial costs,[44] a breakdown of their personal and professional social network,[45] and negative emotional and psychological effects,[46] which in turn affect how entrepreneurs continue their lives and undertake future tasks. While bankruptcy systems can have a pronounced effect on entrepreneurship in general,[47] including personal financial,[48] health-related,[49] and social costs of failure, such as suicide,[50] little research attention has been paid to the 'entrepreneurial-friendliness' of the bankruptcy procedure and the incurrence of psychological costs. This study found that the manner in which a trustee, judge or administrator treats an entrepreneur in a bankruptcy debt rescheduling scheme, can have severe negative emotional and motivational effects. In this way, the study connects insolvency law to the discussion of the role of emotion in law, particularly empathy.[51] This area of research aims to shed light on the role of empathy in judging.[52] The study thereby contributes to strengthening the ties between law and psychology in three ways. First, it is relevant to the theory of grief and recovery. We note that prior research primarily considers the informal social network in order to explain how entrepreneurs manage grief. For example, Shepherd finds that the emotional intelligence of an entrepreneur and the emotional capabilities of family members help to use a grief recovery

[44] See Cope, above n 20.
[45] See Dean A Shepherd and J Michael Haynie, 'Venture Failure, Stigma, and Impression Management: A Self-verification, Self-determination View' (2011) 5 *Strategic Entrepreneurship Journal* 178.
[46] See Shepherd, above n 22.
[47] See John Armour and Douglas Cumming, 'Bankruptcy Law and Entrepreneurship' (2008) 10 *American Law and Economics Review* 303; or John Armour, 'Personal Insolvency Law and the Demand for Venture Capital' (2004) 5 *European Business Organization Law Review* 87.
[48] See Howard Van Auken, Jeffrey Kaufmann and Pol Herrmann, 'An Empirical Analysis of the Relationship Between Capital Acquisition and Bankruptcy Laws' (2009) 47 *Journal of Small Business Management* 23.
[49] See David U Himmelstein et al, 'Medical Bankruptcy in the United States, 2007: Results of a National Study' (2009) 122 *American Journal of Medicine* 741; and David U Himmelstein, Deborah Thorne and Steffie Woolhandler, 'Medical Bankruptcy in Massachusetts: Has Health Reform Made a Difference?' (2011) 124 *American Journal of Medicine* 224.
[50] Rafael Efrat, 'Bankruptcy Stigma: Plausible Cases for Shifting Norms' (2006) 22 *Emory Bankruptcy Developments Journal* 481.
[51] See eg, T A Maroney, 'Law and Emotion: A Proposed Taxonomy of an Emerging Field' (2006) 30 *Law and Human Behavior* 119; T A Maroney, 'The Persistent Cultural Script of Judicial Dispassion' (2011) 99 *California Law Review* 629; Heather Conway and John Steward (eds), *Emotional Dynamics of Law and Legal Discourse* (Hart Publishing, 2016).
[52] See for example Richard A Posner, *How Judges Think* (Harvard University Press, 2008); Mona Lynch and Craig Haney, 'Mapping the Racial Bias of the White Male Capital Juror: Jury Composition and the "Empathic Divide"' (2011) 45 *Law and Society Review* 69; or Scott E Sundby, 'The Capital Jury and Empathy: The Problem of Worthy and Unworthy Victims' (2003) 88 *Cornell Law Review* 343.

strategy appropriately (ie, loss, restoration, oscillation or transition).[53] The findings in this study suggest that, in a bankruptcy or debt rescheduling context, the role of a formal representative, in particular the trustee and administrator, may affect (ie moderate) the relationship between business failure and psychological symptoms, and thereby affect the speed of recovery. Second, drawing on the psychoanalytic view of coping, Singh et al distinguish between problem focused and emotion focused coping when managing the demands of a business failure.[54] The findings indicate that the formal role of a bankruptcy trustee (or judge), as well as (uncertainties about) the formal bankruptcy procedure, may affect emotional coping, and, subsequently, recovery. Third, the findings suggest that empathy — that is, responding with sensitivity and care to the suffering of an entrepreneur without breaching impartiality — deserves much greater research attention in bankruptcy law, as it may, for example, play a much greater role in the acceptance of a personal bankruptcy ruling, the mourning over the lost business and the subsequent second chance for entrepreneurs than is commonly acknowledged.

B *Implications for Practice*

Discussions about the purpose of bankruptcy procedures have been (re-)opened in recent years, with much attention being paid to the early and cost-effective rescue of business. In an attempt 'to avoid debt enforcement mechanisms that involve detailed and extensive court oversight',[55] preventive insolvency and out-of-court procedures are now considered a key European policy area to limit the economic and social effects of bankruptcy for entrepreneurs. If out-of-court re-organisation is not an option, simple and predictable in-court procedures are recommended. Moreover, it has been argued that 'a system must be put in place that does not exacerbate pressure by creditors to declare an entrepreneur as dishonest'.[56] That is, bankruptcy law should reduce the stigma of bankruptcy and foster a solid and realistic second chance.[57] The European Commission therefore, has recommended specialist judges and specialised training courses for formal representatives adjudicating in or administering the bankruptcy proceedings. Court-appointed trustees, whose salary is dependent on the estate's funds, generally have multiple duties, including tracing fraudulent acts (eg, actio pauliana), for which there are not always enough funds in the estate to cover for the time required. In this context, trustees tend to behave in a formalistic, efficient and distrustful, maybe even sceptical way. As a result, bankrupt entrepreneurs may feel like suspected criminals which exacerbates their problems. In light of a worldwide legal reform towards (more) 'debtor-friendly' procedures (as opposed to 'creditor-friendly' systems) this appears to be contradictory. Although the current wave of bankruptcy reform seems to focus on a second chance (to restart following bankruptcy), or to turn struggling businesses around via workouts, this study suggests that debate is necessary on how to deal with the entrepreneur's emotions throughout the legal procedure. That is, it should be discussed whether trustees, administrators and judges should respond with care and sensitivity

---

[53] See Shepherd, above n 22.
[54] See Singh, Corner and Pavlovich, above n 35.
[55] See Simeon Djankov et al, 'Debt Enforcement around the World' (2008) 116 *Journal of Political Economy* 1105.
[56] European Commission, *Report of the Expert Group: A Second Chance for Entrepreneurs: Prevention of Bankruptcy, Simplification of Bankruptcy Procedures and Support for a Fresh Start* (Enterprise and Industry Directorate General, European Commission, 2011) 10 <http://ec.europa.eu/DocsRoom/documents/10451/attachments/1/translations/en/renditions/native>.
[57] See European Commission, *Proposal for a Directive of the European Parliament and of the Council on Preventive Restructuring Frameworks, Second Chance and Measures to Increase the Efficiency of Restructuring, Insolvency and Discharge Procedures, and Amending Directive 2012/30/EU*, COM (2016) 723 final, 2016/0359 COD <http://ec.europa.eu/information_society/newsroom/image/document/2016-48/proposal_40046.pdf>.

to the suffering of entrepreneurs in a bankruptcy or debt rescheduling procedure, and if so, in what way and to what purpose. In general, it should be discussed whether society as a whole needs to pay attention to the psychological and social impact of distressed entrepreneurs. For example, it is known that debt troubles seriously affect health.[58] Also, which measures can be taken to remove the stigma of failure? Is there a role for trustees, administrators and judges themselves — for example via a soft-law solution such as 'general principles and best practices on how to be sensitive to the sufferers in a bankruptcy' — initiated by their professional bodies, or is there a role for governmental bodies with a focus on social healthcare, or both? As showing empathy is trainable,[59] should there be a training programme or perhaps a professional register (to meet standards for professional conduct)? We argue that a legal discussion on a 'second chance' cannot ignore how the legal process and its key representatives affect the psychological stress of failed entrepreneurs.

VI LIMITATIONS

We draw attention to some limitations of our study. First, purposive sampling means that the interview study cannot be considered to be statistically representative of the total population. This technique was chosen merely to explore the key themes that could be observed, hence, the effects that were found may only be applicable to a specific group of entrepreneurs with a debt rescheduling scheme, namely those who responded to the invitation to participate in the interview study. Second, the study focused on entrepreneurs with sole proprietorships who experienced debt rescheduling after a personal bankruptcy. Therefore, the findings may not correspond to the experiences of entrepreneurs who have gone through a corporate bankruptcy. Moreover, more research is needed to determine whether the findings, given the specific Dutch legal context, including the WSNP, correspond to the experiences of entrepreneurs in other legal systems and countries.[60] Third, the cases described do not entail case studies, but were instead in-depth interviews focusing on the bankruptcy experiences of individual entrepreneurs. Thus, the interview data were not corroborated with other data (eg, records) or methods (eg, observation). However, as a direction for future research the scope of personal bankruptcy and debt rescheduling experiences could be expanded to include the interactions with and social realities of other stakeholders, such as the judge, bankruptcy trustee, administrator, and the governing bodies with a public task related to or dealing with personal bankruptcy. Finally, by focusing on debt rescheduling the study's exploratory findings do not shed light onto how business failure would be different for entrepreneurs who failed (ie, went through personal bankruptcy) but never entered the formal natural persons debt rescheduling

[58] Eg, see Anamaria Savu et al, 'The Intersection of Health and Wealth: Association Between Personal Bankruptcy and Myocardial Infarction Rates in Canada' (2016) 16(31) *BMC Public Health* 1; and Melissa B Jacoby, 'Does Indebtedness Influence Health? A Preliminary Inquiry' (2002) 30 *Journal of Law, Medicine and Ethics* 560.

[59] See eg, Daniel Goleman, *Social Intelligence: The New Science of Human Relationships* (Bantam, 2007).

[60] There are some particular aspects of the Dutch bankruptcy system, such as harsher bankruptcy rules in comparison with for example the UK and US: eg, see Oscar Couwenberg and Abe de Jong, 'It Takes Two to Tango: An Empirical Tale of Distressed Firms and Assisting Banks' (2006) 26 *International Review of Law and Economics* 429. Also, while the entrepreneurial culture in the Netherlands is similar to other countries in Europe, specifically the Central European and North European countries (see Fransisco Liñán and José Fernandez-Serrano, 'National Culture, Entrepreneurship and Economic Development: Different Patterns Across the European Union' (2014) 42 *Small Business Economics* 685), there are some specific aspects of entrepreneurship in the Netherlands, eg, the rate of Dutch entrepreneurial activity is high compared to other developed countries: see Pekka Stenholm, Zoltan Acs and Robert Wuebker, 'Exploring Country-level Institutional Arrangements on the Rate and Type of Entrepreneurial Activity' (2013) 28 *Journal of Business Venturing* 176. Moreover, there are differences between the Netherlands and other countries regarding the stigma of failure attached to entrepreneurs, even though these are not very large; eg, see Sharon Simmons, Johan Wiklund and Jonathan Levie, 'Stigma and Business Failure: Implications for Entrepreneurs' Career Choices' (2014) 42 *Small Business Economics* 485.

procedure. By distinguishing more explicitly between the consequences of the business failure and the formal legal bankruptcy proceedings, it is our hope that future research will examine how the formal legal system itself hinders the way small business entrepreneurs cope with their loss.

QUT Law Review ISSN: Online-2201-7275
Volume 17, Issue 1, pp 74–96 DOI: 10.5204/qutlr.v17i1.711

SOME SUGGESTIONS FROM JAPAN FOR REFORMING AUSTRALIA'S PERSONAL BANKRUPTCY LAW

STACEY STEELE AND CHUN JIN*

This article examines Japan's contemporary personal bankruptcy law reform experience in light of Australia's proposed reforms to the Bankruptcy Act 1966 *(Cth). Japan's personal insolvency legislation was substantially revised at the turn of the 21st century and a new proceeding for individual rehabilitation introduced. These innovations built on practical and procedural solutions pioneered in the courts especially in the late 1990s as the number of personal bankruptcies increased after the bursting of the bubble economy. The article shows that by comparison with Japanese approaches to discharge, investigation and continuing obligations, including requirements for income contributions, the proposed Australian reforms are conservative and not as debtor-friendly as those in Japan. The time between filing and discharge in Japan, for example, is flexible and typically no more than a few months. The Australian reforms merely suggest revising the default bankruptcy period from three years to a fixed one year. In practice, the article suggests that the obstacles of adverse credit histories and enforcement of personal guarantees against entrepreneurs remain problems for an entrepreneur seeking a fresh start in both jurisdictions.*

I INTRODUCTION: REFORMING PERSONAL BANKRUPTCY LAW

This article examines contemporary personal bankruptcy law reform experience in Japan, in light of the suggested reforms to personal bankruptcy law set out in the Australian government's proposals paper, *Improving Bankruptcy and Insolvency Laws*, released on 29 April 2016 ('Proposals Paper').[1] To date, Australian law reformers have not typically looked to Japan for insights or alternatives in the context of insolvency law, but this article argues that proposed Australian reforms could be reconsidered in light of Japanese experience. In particular, the proposal to reduce the default bankruptcy period from three years to one year and a proposal that would require bankrupts to make income contributions for three years, appear to be very conservative when it comes to consumer bankruptcies in light of Japanese developments. The article argues that despite the prevailing stigma attached to becoming

* Stacey Steele, LLB, LLM (Melbourne), Associate Director (Japan), Asian Law Centre, Melbourne Law School, Australia. Chun Jin, LLB (Renmin U of China), LLM, PhD (Kyoto), Associate Professor, Doshisha University Japan, Visiting Research Scholar, Asian Law Centre, Melbourne Law School (2015–2017), Visiting Professor at Renmin University of China (2017–2020). The authors acknowledge the financial support of a Grant for Social Science (2016) (Shakai kagaku josei) from the Nomura Foundation (*Nomura Zaidan*), Japan, and the Melbourne Law School International Collaboration Fund, and thank Mr Michael Murray and Professor Ros Mason, Queensland University of Technology, and other participants at the 'Personal Insolvency Conference', QUT, Brisbane, Australia, 7–9 September 2016 for their comments on earlier versions of this article. The authors also thank Ms Kaori Kano, Principal Research Assistant, Asian Law Centre, and Ms LI Ying, PhD Candidate, Osaka University, for their research assistance. Stacey Steele also thanks Mr Naoya Mori, Japaneasy Language School, for his assistance with Japanese language materials. This article reflects the authors' personal opinions. Statements do not represent the views or policies of employers, past or present, or any other organisation with which the authors are affiliated.

[1] National Innovation and Science Agenda (Aust), *Improving Bankruptcy and Insolvency Laws: Proposals Paper* (The Treasury, 2016) ('Proposals Paper') <https://treasury.gov.au/consultation/national-innovation-and-science-agenda-improving-bankruptcy-and-insolvency-laws/>.

bankrupt in Japan, the Japanese legislation is more encouraging of risk taking than the Australian legislation will be, if the proposed Australian reforms are adopted. The Japanese framework includes a quick procedure for individuals, whilst also making it easier and cheaper for entrepreneurs to file for personal and corporate insolvency at the same time. Moreover, the average time between filing a petition to commence a personal bankruptcy proceeding and a discharge becoming final and binding is about 100 days.[2]

After this introduction, the article begins by setting out the key legislative frameworks for Japanese personal insolvency proceedings.[3] This section focuses on the *Hasan hō* [Bankruptcy Act] (Act No 75, 2004) (Japan) ('*Bankruptcy Act*'), which corresponds generally with Australia's *Bankruptcy Act 1966* (Cth) in the sense that applicants seek a discharge from their debts on completion of the proceeding. This section examines three key features of the Japanese system: the system of simultaneous termination which refers to a proceeding where no trustee is appointed and the court provides an order to terminate the proceeding at the same time as giving an order for commencement; small-scale proceedings supervised by a trustee with a small fee payable to the court to cover the trustee's fixed fee; and the Japanese courts' approach to discharge. In addition, this section also analyses recent survey data about the number and type of bankruptcies collected by the Japan Federation of Bar Associations in relation to personal insolvency in Japan to provide context for readers from Australia.[4] In the third section, the article specifically examines Japan's approach to the issues and questions raised in the Australian Proposals Paper and provides some suggestions based on Japanese experience. Finally, the article argues that Japan's experience suggests that a key obstacle to entrepreneurs receiving a fresh start is the treatment of personal guarantees by financial institutions. This section introduces recent Japanese guidelines for financial institutions dealing with guarantees. The guidelines are designed to address the concern that a business person will be bankrupted due to a guarantee being called if she or he files for formal insolvency proceedings in respect of a related enterprise, and thus she or he would be discouraged from making the corporate filing.[5] This Japanese experience suggests that future Australian reforms need to give consideration to the role that personal guarantees play in the small and medium-sized enterprise ('SME') market for credit in Australia and how they are treated in any insolvency of the SME. The article argues that there may be lessons for Australia from this recent development in Japan.

---

[2] Shōhisha mondai taisaku iinkai [Committee for Addressing Consumer Problems], *2014-nen hasan jiken oyobi kojin saisei jiken kiroku chōsa* [*2014 Survey of Records of Bankruptcy Cases and Individual Rehabilitation Cases*] (Japan Federation of Bar Associations, 2014).
<http://www.nichibenren.or.jp/library/ja/publication/books/data/2014/2014_hasan_kojinsaisei.pdf> 5.

[3] For an overview of Japan's insolvency law system, see Stacey Steele and Jin Chun, CCH, *Japan Business Law Guide* (at 26 November 2015) 19.140. English translations of the relevant insolvency legislation may be found on the Ministry of Justice's Japanese Law Translation website: Ministry of Justice (Japan), *Japanese Law Translation* <www.japaneselawtranslation.go.jp>. On the reliability and translation process for the Ministry of Justice translation project, see Carol Lawson, 'Found in Translation: The "Transparency of Japanese Law Project" in Context' (2007) 24 *Journal of Japanese Law* 187.

[4] See Committee for Addressing Consumer Problems, above n 2.

[5] *Keieisha hoshō ni kansuru gaidorain* [*Guidelines in Relation to a Business Owner's Personal Guarantee*] (2013) <http://www.jcci.or.jp/chusho/kinyu/131205guideline.pdf>. These guidelines became effective from 1 February 2014, and are available on the websites of various institutions and associations including the Japan Chamber of Commerce and Industry (Nihon Shōkō Kaigi Sho), the Japan Federation of Credit Guarantee Corporations (Zenkoku Shinyō Hoshō Kyōkai Rengō Kai), and the Japanese Bankers' Association (Zenkoku Ginkō Kyōkai).

II PERSONAL INSOLVENCY IN JAPAN

A *Overview of Japan's Legal Framework for Personal Insolvency*

Japanese personal insolvency legislation was substantially updated by a suite of reforms which were introduced over the course of about a decade.[6] The drivers for insolvency law reform in Japan were multifaceted. The late 1990s saw an upswing in the number of insolvency proceedings being dealt with in the courts as reflected in the figures shown in Table 1. Japan's economic malaise continued during this period and, at the same time, the Japanese consumer credit industry developed and expanded significantly. The reforms were also aimed at modernising Japan's insolvency law framework. The previous law was based on 19th century European statutes which were introduced to Japan in the early 20th century. The previous *Hasan hō* (Act No 71, 1922) (Japan) ('*Bankruptcy Act 1922*'), for example, was based on the German *Konkursordnung* [Bankruptcy Act] of 1877.[7] The Japanese personal insolvency law framework now includes a rehabilitation procedure, bankruptcy procedure and quasi-formal procedures involving court-led conciliation processes.[8] The courts also led non-legislative reform efforts around this time, such as the introduction of the small-scale proceedings supervised by a trustee for a fixed fee, as discussed further below. The procedure was pioneered by the Tokyo District Court, from the late 1990s.[9] Out-of-court workouts are also still popular in Japan, but difficult to quantify and examine, given that they are not typically public.[10] This section provides an outline of the civil rehabilitation procedure first, but focuses on the bankruptcy procedure, which is the most used legislative procedure with 65 393 filings in 2014.[11]

Table 1: Number of filings for personal bankruptcy (*kojin hasan jiken*) from 1988 to 2001[12]

Year	'88	'89	'90	'91	'93	'94	'95	'96	'97	'98	'99	'00	'01
Filings	9, 433	11, 480	23, 491	43, 394	43, 816	40, 613	43, 649	56, 802	71, 683	105, 468	123, 915	139, 590	160, 741

The *Minji saisei hō* [Civil Rehabilitation Act] (Act No 225, 1999) (Japan) ('*Civil Rehabilitation Act*') was the first legislation to be enacted during the legislative reform process. Civil rehabilitation is available to both individuals and corporations. The Act was amended in April 2001 to include special provisions for rehabilitation of individual debtors with small-scale debts (*shōkibo kojin saisei tetsuzuki* or 'small-scale individual rehabilitation procedure') and

[6] On the process of reform in Japan, see Steele and Chun, above n 3, 19.120–19.130.
[7] *Konkursordnung* [Bankruptcy Act] (Germany) 10 February 1877, RGBl, 1877, 351.
[8] Jin Chun, 'Kojin saimusha no tōsan tetsuzuki [Insolvency Proceedings for Individual Debtors]' in Fujimoto Toshihazu and Nomura Tsuyoshi (eds), *Kiso toreeningu tōsanhō* [*Bankruptcy: Examples and Explanations*], (Nihonhyoronsha, 2013), 235, 236.
[9] As discussed further below, the Tokyo District Court developed this proceeding as an alternative to the simultaneous termination proceeding which was developed in the 1980s by the Tokyo and Osaka District Courts: see Shibata Takeo and Kimura Yuji, 'Tajū saimusha kyūsai no hō to jitsumu: jikōhasan tetsuzuki "dōji haishi" o chūshin ni [Law and Practice in Assisting People with Multiple Debts: Focusing on the Personal Bankruptcy Proceeding Known as Simultaneous Termination]' (2015) 27(2) *Seigaku'in daigaku ronsō* 29, 35, 38.
[10] Specific individual guidelines are also available for application in relation to victims of the Great East Japan Earthquake. See Stacey Steele and Jin Chun, 'Insolvency Law Responses to a National Crisis: Great East Japan Earthquake and Guidelines for Individual Debtor Out-of-Court Workouts' (2012) 17(34) *Journal of Japanese Law* 43.
[11] *Saibansho dētabukku 2016* [*Court Data Book 2016*] (Supreme Court of Japan, 2016) <http://www.courts.go.jp/about/databook/index.html> 44–53.
[12] Ibid.

wage-earning debtors (*kyūyo shotokusha nado saisei tetsuzuki* or 'wage earner etc rehabilitation procedure').[13] These procedures allow individual debtors with a prospect of earning a future income to negotiate an individual rehabilitation plan with creditors if their general debts (excluding debts relating to a loan secured by their principal place of residence) are less than ¥50 000 000.[14]

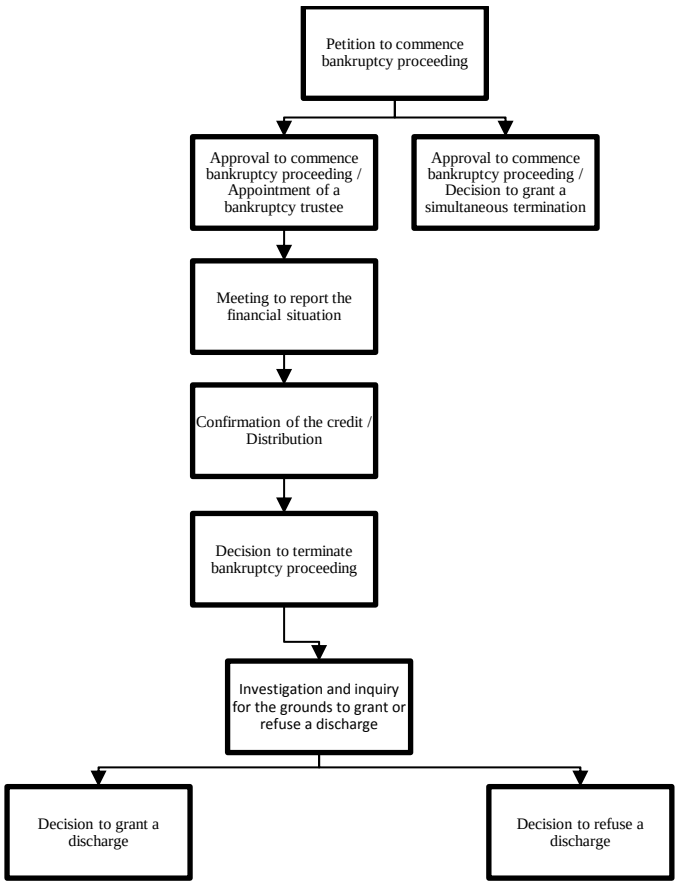
Civil rehabilitation does not prevent a secured creditor from enforcing a secured claim.[15] In the case of enterprise rehabilitation, however, where the collateral for that secured claim is indispensable to the continuation of the debtor's business, the court may order a stay of enforcement on the application of an interested party or of its own motion.[16] Moreover, the civil rehabilitation proceeding introduced an innovative mechanism designed to assist companies with assets which are secured for more than they are worth, known as the security interest extinguishing scheme (*tanpo ken no shōmetsu*).[17] The scheme also allows the debtor or relevant insolvency practitioner to use the threat of applying to court to extinguish a security interest after paying a certified value as leverage in negotiations with secured creditors.[18] However, these provisions relate to enterprise rehabilitation proceedings, and civil rehabilitation initially did not prevent a secured creditor in a proceeding relating to an individual from enforcing a secured claim. Special rules relating to individual rehabilitation debtors with a home loan were introduced in 2001, and these prevent secured creditors from exercising a security interest relating to a home loan and allow a debtor to keep her or his home as part of the proceeding in certain circumstances.[19]

The new *Bankruptcy Act* followed the introduction of the civil rehabilitation procedure and became effective in 2005. There is no distinction drawn between merchants and consumers in the Japanese *Bankruptcy Act*. The applicable jurisdiction is the debtor's local district court. Diagram 1 illustrates the life of a typical bankruptcy procedure in Japan, from filing to discharge. In summary, a bankruptcy procedure commences with a petition being filed. Both debtors and creditors may file a petition, and there is no threshold amount for a creditor's petition.[20] In practice, however, debtors file petitions, although there may be pressure from creditors to file. If the court accepts the petition, a meeting will be held to confirm the debtor's financial position and the claim information. These processes are then followed by an investigation into whether there are any grounds to object to a discharge and, if there are none, a discharge will be granted. Secured creditors do not have to participate in the bankruptcy

[13] *Minji saisei hō* [Civil Rehabilitation Act] (Act No 225, 1999) (Japan). Articles 221–38 of the *Civil Rehabilitation Act* provide for the individual debtor with small scale debt, and arts 239–45 provide for the wage-earning debtor.
[14] Ibid art 221.
[15] Ibid art 53.
[16] Ibid art 30.
[17] Ibid arts 148–53.
[18] See Stacey Steele, 'Too Hot to Handle: Extinguishing Secured Creditors' Interests in Insolvency Under Japan's Civil Rehabilitation Law' (2003) 8(16) *Journal of Japanese Law* 223. Recent empirical research on civil rehabilitation proceedings in Japan suggests that the 'security interest extinguishing scheme' has been applied in 15 out of 313 cases surveyed, and nine out of those 15 cases involved business transfers; it appears that the extinguishing of security interest is applied in relation to the business transfer. The application was approved in 11 cases: Mayumi Kurabe and Ken Yamamoto, 'Saisei tetsuzuki ni okeru betsujoken no shogū [Dealing with Rights of Separate Satisfaction in Rehabilitation Proceeding]' in Kazuhiko Yamamoto and Ken Yamamoto (eds), *Minji saisei hō no jisshōteki kenkyū* (*Empirical Research on the Civil Rehabilitation Act*) (Shōji hōmu, 2014) 215.
[19] *Civil Rehabilitation Act* arts 196–206.
[20] *Bankruptcy Act* art 18(1). On the personal bankruptcy procedure, see generally Steele and Chun, above n 3, 19.220–19.285; Junichi Matsushita, 'Japan's Personal Insolvency Law' (2007) 42 *Texas International Law Journal* 765.

proceeding and may execute on their security.[21]

Diagram 1: personal bankruptcy proceeding flowchart[22]



A key feature of Japan's personal bankruptcy law is the quick and simple *dōji haishi* procedure which is also illustrated in Diagram 1. The procedure provides for a bankruptcy proceeding to be terminated simultaneously with the commencement of the proceeding, without a trustee being appointed.[23] Accordingly, *dōji haishi* is often translated as 'simultaneous termination'. As Diagram 1 shows, the discharge process starts almost immediately in cases where there is an order (*kettei*) to grant a simultaneous termination, despite the legislation otherwise providing for certain time periods for the appointment of a trustee, and registration and investigation of claims.[24] The speedy resolution of the proceeding has merit for debtors. The procedure was introduced into the *Bankruptcy Act 1922*[25] and developed further during the 1980s and 1990s, based on practice in the Tokyo and Osaka District Courts for cases where the debtor had no or insufficient assets to cover the costs of the bankruptcy proceeding.[26]

In response to criticisms that bankrupts were not being investigated properly and were thus able to conceal assets from creditors, the Tokyo District Court adopted a revised procedure

[21] *Bankruptcy Act* arts 65.
[22] This diagram is a translated and adapted version of the diagram appearing in Chun, above n 8, 238.
[23] *Bankruptcy Act* art 216(1).
[24] Ibid arts 31(1), (2).
[25] See Makoto Ito, *Hasanhō minji saisei hō* [*Bankruptcy Act and Civil Rehabilitation Act*], (Yūhigaku, 3rd ed, 2014) 179.
[26] The Tokyo District Court developed *sokujitsu mensetsu* or same-day interviews from 1999 as discussed below. See Takeo and Yuji, above n 9, 35, 37.

known as a small-scale procedure supervised by a trustee (*shōgaku kanzai tetsuzuki*), in the late 1990s. For cases where a pre-petition representative *bengoshi* (attorney) has been appointed, this procedure provides for a comparatively simple and quick process once a petition for commencement has been made, because, for the most part, the investigation of the debtor's assets and creditors' claims, as well as the investigation of whether there are any reasons to refuse a discharge are carried out prior to filing. Accordingly, the court requires a lower payment into court (*yonōkin*) to cover the fees of the court-appointed trustee, because there should not be much work left for that trustee to do.[27] The involvement of a trustee also means that the trustee can perform the investigation into, and report on, any reasons for refusing a discharge, which reduces the court's workload.[28] The small-scale procedure supervised by a trustee (*shōgaku kanzai tetsuzuki*) thus supports the effective functioning of ordinary bankruptcy and discharge proceedings and seeks to balance the interests of debtors and creditors.[29] Scheduled fees for ordinary cases were substantially reduced in line with the reduction in the work required by the court and trustees. Currently, debtors are required to pay approximately ¥10 000 to ¥20 000 into court, an amount known as *yonōkin*, when a debtor files for a *dōji haishi* proceeding in the Tokyo District Court.[30] This amount is designed to cover public notification in the official gazette.[31] The cost of a small-scale procedure supervised by a trustee is typically ¥200 000, which includes the fee payable to the trustee.[32]

Simultaneous termination of the proceeding under a *dōji haishi* procedure does not amount to an order for a discharge, which typically comes a few months after the initial filing for commencement and termination as detailed further below. The investigation in relation to the existence of any grounds to refuse a discharge occurs during the period between termination and discharge. The *Bankruptcy Act* provides that certain claims may not be discharged, for example: certain taxes;[33] damages following a wilful tort; penalties and fines; and debts to a former spouse for child support.[34] Exempted assets include the debtor's household furnishings, household goods, apparel, household appliances, cash of up to ¥990 000 and the debtor's right to receive unpaid salary of up to ¥330 000 per month.[35] Prior to reforms in 2004, the amount of exempt cash was ¥660 000. The increase in the exempt cash amount to ¥990 000 was designed to encourage debtors to file for bankruptcy and demonstrate better support for the maintenance of the debtor's well-being and the goal of giving a debtor a fresh start.[36] In the

[27] See Takashi Sonoo et al (eds), *Shōgaku kanzainin tetsuzuki no riron to jitsumu* [*Small-Scale Procedure Supervised by a Trustee: Theory and Practice*] (Keizai hōrei kenkyūkai, 2001) 33; Ito, above n 25, 180; Kazuhiko Yamamoto, *Tōsan shorihō nyūmon* [*Introduction to Insolvency Workout Law*], (Yūhigaku, 4th ed, 2012) 126.

[28] Trustees are typically *bengoshi* (licensed attorneys) in Japan, but in some Japanese local jurisdictions *shihō shoshi* (judicial scriveners) are appointed. Accountants tend to be engaged by the trustee if necessary.

[29] See Ito, above n 25, 180.

[30] See Yamamoto, above n 27, 58. Tokyo District Court fees as at 2004 are listed by Ginza Seiwa Law Office: *Hasan jiken no tetsuzuki hiyō ichiran* [*Summary of Court Fees from Bankruptcy Cases*] (Ginza Seiwa Law Office, 2004) <www.ginzaseiwa.jp/feature/feature05_01.pdf>. For indigent cases, the *Bankruptcy Act* specifically provides for the complete waiving of costs: see *Bankruptcy Act* art 23.

[31] See Yamamoto, above n 27, 124.

[32] See Ito, above n 25, 180; Yamamoto, above n 27, 125.

[33] Unpaid taxes which have accrued and remain unpaid for a period up to 12 months before the commencement of a bankruptcy proceeding will be treated as administrative claims (*zaidan saiken*, also translated as 'estate claims'): *Bankruptcy Act* art 148(3). The rationale behind this limitation is that it is up to the tax authorities to ensure that they are seeking timely payment of taxes and in any event following up debtors where taxes remain unpaid at least on an annual cycle. Some commentators suggest that the reference to tax claims being unable to be discharged does not include those unpaid taxes treated as administrative claims. See Makoto Ito et al, *Jōkai hasanhō* [*Understanding the Provisions in the Bankruptcy Act*], (Kōbundō, 2nd ed, 2014) 1680.

[34] *Bankruptcy Act* art 253(1).

[35] Ibid art 34. See also Matsushita, above n 20, 766.

[36] *Bankruptcy Act* art 34 (3)(i).

context of a debtor's spending power in Japan, this was a large increase.[37]

Despite an initial increase in filings for personal bankruptcy in Japan around the time of the reforms and new judicial procedures, there was a significant decline in filings after 2011 (see Table 2). Some of the substantial increase in personal bankruptcy filings immediately before the new legislation became effective relates to the bankruptcy procedure's interaction with the civil rehabilitation proceeding which quickly became popular after it took effect in 2000.[38] Further, there was pent-up demand as debtors delayed filing until the new suite of insolvency legislation became effective. A key reason for the later decrease in the number of personal bankruptcies is a Supreme Court of Japan judgement against the money lending industry, which required money lenders to repay interest paid above the amount set under the *Risoku seigen hō* [*Interest Rate Restriction Act*] (Act No 100, 1954) (Japan). Some debtors have since been able to recover any overpayments and may thus avoid bankruptcy.[39] The decline over the last five years may also be attributed to Japan's low interest rate environment, improved economic circumstances and a renewed preference for out-of-court proceedings which do not involve the disadvantages presented by formal bankruptcy discussed further below.

Table 2: Number of filings for personal bankruptcy (*kojin hasan jiken*) from 2002 to 2015[40]

Year	'02	'03	'04	'05	'06	'07	'08	'09	'10	'11	'12	'13	'14	'15
Filings	214, 996	242, 849	211, 860	184, 23	166, 399	148, 524	129, 833	126, 533	121, 150	100, 736	82, 902	72, 287	65, 393	64, 081

B *Personal Bankruptcy Law in Japan in Practice: Survey Data from the Japan Federation of Bar Associations*

The practical contexts of Japanese personal bankruptcy legislation and judicial practice, as well as Japan's changing economic and demographic environment, are evidenced by survey data collected by the Committee for Addressing Consumer Problems (*shōhisha mondai taisaku iinkai*) ('Consumer Committee') of the Japan Federation of Bar Associations ('JFBA'). The Consumer Committee was established in September 1985 by the JFBA in the aftermath of incidents such as the Yoshida shōji case involving institutional defrauding of consumers and an increase in debtors who owed multiple debts to so-called *sara-kin* companies, or loan sharks.[41] The Committee's goal is to assist the JFBA in formulating its opinions and policies by collecting information in relation to problems relating to consumer protection, and conducting surveys and research.[42] Volunteer *bengoshi* (attorneys) conduct a review of official records held by district courts relating to bankruptcy matters and individual rehabilitation matters, and the Consumer Committee collates and publishes the combined results.[43] The survey has been published every few years since 1992.[44] The most recent survey results,

[37] Debtors may also retain household furnishings, household goods, apparel and household appliances: *Minji shikkōhō* [Civil Execution Act] (Act No 4, 1979) (Japan) art 131; *Bankruptcy Act* art 34(3).
[38] Civil rehabilitation proceedings may be transferred to bankruptcy proceedings under certain circumstances.
[39] Yamamoto, above n 27, 121.
[40] *Court Data Book 2016*, above n 11.
[41] Japan Federation of Bar Associations, *Shōhisha, Tajūsaimumondai* [*Consumer, Multiple Debt Problems*] <http://www.nichibenren.or.jp/activity/human/consumer.html>.
[42] Ibid.
[43] Committee for Addressing Consumer Problems, above n 2, 1.
[44] Ibid.

published in June 2014,[45] involved collecting data from 1 June 2013 to 30 November 2013. Twenty bankruptcy cases were chosen randomly from each district court jurisdiction, except where a district court is co-located with a high court, in which case 50 bankruptcy cases were randomly chosen from that district court's records to reflect the greater volume of cases in those busier districts.[46] Similarly, over the same period, 10 matters involving a petition for individual rehabilitation involving a small-scale individual rehabilitation and a wage earner etc rehabilitation were chosen from each district court jurisdiction, except where a district court is co-located with a high court, in which case 25 cases were randomly chosen.[47] The results published in 2014 captured available data from 47 prefectures and 50 district courts and 1240 bankruptcy cases and 708 individual rehabilitation cases (560 small-scale individual rehabilitation cases and 148 wage earner etc rehabilitation cases).[48] Whilst the data set is relatively small as a percentage of overall court filings, the survey's geographical coverage and breadth of information makes it an important source of insolvency data in Japan. Further, despite some variation in coverage over three decades, the data, particularly from 2002 onwards, consistently cover the vast majority of prefectures and administrative areas in Japan. Moreover, the same or very similar questions have been asked as part of the survey since 1997 to maintain consistency and provide opportunity for longitudinal comparisons.[49]

The survey results published in 2014 suggest that bankruptcy in Japan still tends to be a procedure for low income earners in financial difficulties: the average monthly income of a bankrupt at the time of filing was ¥131 612.[50] The majority of petitioners (60.48 per cent) earn less than the benchmark for receiving living assistance and less than ¥150 000 per month.[51] The difference between the financial position of men and women petitioners is stark, with 76.34 per cent of female petitioners earning less than ¥150 000 per month compared to 48.88 per cent of men earning that amount.[52] Petitioners typically had approximately ¥24 143 329 in debts at filing, but approximately half of petitioners (48.22 per cent) had less than ¥5 000 000.[53] Most bankrupts (80.65 per cent) have fewer than nine creditors and on average about 6.76 creditors.[54] These results suggest that debtors are increasingly unable to pay even small debts.[55] Moreover, in almost all cases creditors received no distribution. Since 2005, creditors receive a return of 2–3 per cent according to the data collected by the Consumer Committee.[56]

[45] Ibid (available on the JFBA's website, <http://www.nichibenren.or.jp/library/ja/publication/books/data/2014/2014_hasan_kojinsaisei.pdf>).
[46] Ibid.
[47] Ibid.
[48] Ibid. Each year the survey has varied slightly in terms of jurisdictions covered and number of cases reviewed: 1992 (21 district courts, 530 cases), 1994 (8 district courts, 779 cases), 1997 (43 district courts, 1089 cases), 2000 (47 district courts, 50 cases); and then 2002 (46 prefectures, 48 district courts), 2005 (44 prefectures, 47 district courts), 2008 (47 prefectures, 50 district courts), 2011 (47 prefectures, 50 district courts). Individual rehabilitation matters were included from 2002 after the introduction of individual rehabilitation proceedings by the *Civil Rehabilitation Act* in 2001.
[49] Committee for Addressing Consumer Problems, above n 2.
[50] Ibid 2. This amount is an increase on previous years. Earlier average monthly incomes were: ¥104 639 in 2002; ¥110 061 in 2005; ¥121 288 in 2008; ¥117 576 in 2011.
[51] Committee for Addressing Consumer Problems, above n 2.
[52] Ibid.
[53] Ibid 3.
[54] Ibid.
[55] Ibid.
[56] Ibid 6. Since 2005, the data evidences that creditors receive a return of two or three per cent.

The survey also considers the reasons why people are experiencing financial distress.[57] Lifestyle hardship / low income has consistently been the most commonly cited problem, typically accounting for approximately 60 per cent of cases reviewed since 2002, followed by illness and medical costs (typically accounting for approximately 20 per cent of cases reviewed).[58] After the so-called Lehman Shock in 2008, the number of people citing a reduction in income increased to 16.13 per cent in 2011, and 13.47 per cent in 2014, from approximately 11 per cent in 2005 and 2008. The number of people citing unemployment and change in work circumstances also increased in 2011 and 2014 to 19.77 and 19.84 per cent respectively, from 14.67 per cent in 2008.[59] People are also increasingly citing difficulty in repaying their home loans as a reason for filing for bankruptcy (9.59 per cent in 2008; 12.24 per cent in 2011; 16.05 per cent in 2014).[60] This result may be related to a spike in home purchases before the anticipated increase in consumption tax in Japan, which the Abe government has postponed.

The survey also reflects Japan's ageing society, with the number of bankrupts aged 60 or more years old reaching 18.71 per cent, the highest level for that age group since the survey's inception in 1992.[61] A typical bankrupt in Japan is in her or his forties (27.02 per cent) or fifties (21.05 per cent), but the median age is definitely increasing in line with Japan's ageing population. The increased number of elderly seeking bankruptcy may also be contributing to the increasing number of petitioners who are also welfare recipients (6.97 per cent in 2011, rising to 11.13 per cent in 2014).[62] Elderly people in Japan are also increasingly living by themselves, which could help to explain the rising number of petitioners who live alone (30.40 per cent in 2014 compared to 18.20 per cent in 2008 and 22.45 per cent in 2011).[63] In more recent years, the difference in the number of men and women filing for bankruptcy has also grown, with men increasingly more likely to use the procedure since 2011.[64]

III JAPAN'S APPROACH TO ISSUES RAISED IN THE AUSTRALIAN GOVERNMENT'S PROPOSALS PAPER

A *Issues Raised in the Australian Government's Proposals Paper*

This part of the article examines Japan's legislative and procedural approaches to the key issues raised in the Australian Proposals Paper, and highlights key differences and similarities. Despite Australian reformers typically looking to the United Kingdom or the United States of America for inspiration, this article argues that Japan offers a useful touchstone for Australia when considering the reform of personal bankruptcy law. Despite significantly different legal, economic and social contexts between Australia and Japan, there are also important similarities, and Australia's close relationship with Japan suggests that the countries could learn from each other. Japan is a fellow OECD high income country with a mature economy and

[57] Multiple reasons could be given by one person.
[58] Committee for Addressing Consumer Problems, above n 2, 1.
[59] Ibid. Previously, unemployment was 13 per cent in 2000, 14.14 per cent in 2002 and 18.12 per cent in 2005.
[60] Committee for Addressing Consumer Problems, above n 2.
[61] Ibid 2.
[62] Ibid 3.
[63] Ibid 44. For discussion of the elderly in the Japanese criminal justice system and living circumstances, see Stacey Steele, 'Elderly Offenders in Japan and the Saiban'in Seido (Lay Judge System): Reflections through a Visit to the Tokyo District Court' (2015) 35 *Japanese Studies* 223.
[64] Committee for Addressing Consumer Problems, above n 2, 2.

ageing society.[65] It is one of Australia's key trading partners and a recent signatory to a bilateral free trade agreement with Australia[66] and co-signatory to the Trans-Pacific Partnership.[67] Moreover, Japan has diligently and consistently worked to improve its approach to personal bankruptcy law over the last two decades in light of its economic malaise during the 1990s and 2000s, which has seen a cultural, procedural and operational shift in insolvency law practice.

The Australian government also hopes that its law reform proposals will contribute to a cultural shift in Australia; a shift in favour of entrepreneurship. The Australian Proposals Paper asserts that '[m]ore often than not, entrepreneurs will fail several times before they achieve success' and that Australians should be encouraged 'to embrace risk, learn from mistakes, be ambitious and experiment to find solutions'.[68] The Proposals Paper suggests reducing the default bankruptcy period and restrictions on discharged bankrupts travelling overseas from three years to one year. The government also asked for submissions in relation to the ongoing obligations of bankrupts, suggesting that a bankrupt be required to make income contributions for three years. The analysis below considers how Japan has approached similar issues and offers some suggestions for Australian reformers.

B *Reducing the Default Bankruptcy Period and Objections to Discharge*

The Australian government proposes to reduce the default period for bankruptcy from three years to one year and thus any related restrictions on a bankrupt will also typically be reduced to one year.[69] The Proposals Paper suggests that this reform 'will encourage entrepreneurial endeavour and reduce associated stigma' and 'acknowledges that bankruptcy can be a result of necessary risk-taking or misfortune rather than misdeed'.[70] The timeframes in Japan, however, are even shorter than the one year suggested for Australia in the Proposals Paper. The time between filing and receiving an order for commencement of a proceeding in Japan was typically between 10 and 30 days (43.09 per cent of cases), with a significant number (20.72 per cent of cases) taking between 30 and 45 days to receive a commencement order, the average being 33.6 days.[71] The average time between receiving an order for commencement and a discharge from bankruptcy was 68 days, with 99.23 per cent of cases receiving an order for discharge in less than four months.[72] Accordingly, the average time for a whole proceeding measured as the time between filing a petition and receiving a discharge is typically about 100

---

[65] For high income countries classification, see Organisation for Economic Co-operation and Development, *Country Classification 2016 — As of 26 July 2016* (OECD, 2016) 9 <http://www.oecd.org/trade/xcred/2016-ctryclass-as-of-26-july-2016-rev1.pdf>.

[66] *Agreement Between Australia and Japan for an Economic Partnership*, Australia–Japan, [2015] ATS 2 (entered into force 15 January 2015). For full text of agreement, see Department of Foreign Affairs and Trade (Cth) ('DFAT'), *Japan–Australia Economic Partnership Agreement* <http://dfat.gov.au/trade/agreements/jaepa/official-documents/Pages/official-documents.aspx>; Ministry of Foreign Affairs of Japan ('MOFA'), *Japan–Australia Economic Partnership Agreement* <http://www.mofa.go.jp/policy/economy/fta/australia.html>.

[67] *Trans-Pacific Partnership Agreement Between the Government of Australia and the Governments of: Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States of America and Vietnam*, signed 4 February 2016 [2016] ATNIF 2 (not yet in force). For full text see DFAT, *TPP Text and Associated Documents* <http://dfat.gov.au/trade/agreements/tpp/official-documents/Pages/official-documents.aspx>; MOFA, *Signing of the Trans-Pacific Partnership (TPP) Agreement* <www.mofa.go.jp/press/release/press4e_001013.html>.

[68] Proposals Paper, above n 1, 3.

[69] *Bankruptcy Act 1966* (Cth) s 149.

[70] Proposals Paper, above n 1, 5.

[71] Committee for Addressing Consumer Problems, above n 2, 4–5.

[72] Ibid 5.

days.[73] Whilst these data do not capture the work performed by the debtor and the pre-petition representative prior to filing, the survey results highlight the short timeframe required for the formal proceeding and the flexibility afforded to the court and parties in Japan where the legislation does not provide for a fixed period of bankruptcy.

To mitigate concerns about potential abuse of the bankruptcy process based on the shorter period of one year running from the time the bankrupt filed a statement of affairs to discharge, the Australian government proposes that a trustee retain the right to object to a discharge.[74] The trustee will also retain the right to extend the period of bankruptcy up to eight years.[75] The Proposals Paper notes that, 'courts currently do not have a direct role in extending the period of bankruptcy'.[76] A bankrupt, creditor or other affected person may, however, appeal to the court in relation to an act, omission or decision of a trustee.[77] The government has asked for submissions from the public 'on whether the criteria for lodging an objection and the standard of evidence to support an objection should be changed to facilitate a trustee's ability to object to discharge' in light of the shorter default bankruptcy period which it suggests may make it difficult to gather 'sufficient evidence to support lodgement of an objection'.[78]

The corresponding approach to discharge under the Japanese *Bankruptcy Act* places an emphasis on the debtor's behaviour, and gives the courts great discretion when it comes to granting a discharge. A Japanese court may refuse a debtor's request for a discharge if the debtor has concealed assets to defraud creditors, made false statements suggesting solvency when borrowing money, or failed to perform any duties required under the law or to cooperate with the trustee or the court. A discharge may also be denied if a debtor has been granted a discharge in a previous bankruptcy or individual rehabilitation case within certain time periods.[79] But even in those circumstances the court has discretion to grant a discharge.[80] All but five of the 1240 cases in the JFBA survey involved a petition for discharge and it is not clear from the JFBA's data why those five cases did not include such a petition. Of the 1235 cases that requested a discharge, the court granted a discharge in 96.44 per cent of cases.[81] There was only one case of a discharge being refused, with the other cases being withdrawn before a decision was made.[82]

To the extent that a trustee is appointed in Japan, the court expects the trustee to investigate whether there are any grounds for refusing to discharge the debtor.[83] A trustee will collect documentation which supports or refutes grounds for refusing a discharge. Such documentation may include information provided by the bankrupt, and a trustee may interview the bankrupt's family and other related persons and creditors, and demand that they provide documentation.

---

[73] Ibid.
[74] Proposals Paper, above n 1, 6. For the grounds for an objection, see *Bankruptcy Act 1966* (Cth) s 149D.
[75] Ibid.
[76] Ibid.
[77] *Bankruptcy Act 1966* (Cth) s 178.
[78] Proposals Paper, above n 1, 6.
[79] Matsushita, above n 20, 767.
[80] *Bankruptcy Act* art 252(2).
[81] Committee for Addressing Consumer Problems, above n 2, 5.
[82] Ibid. The number of cases withdrawn also continues to increase, albeit from a low base. Results from earlier surveys are as follows: 0.65 per cent in 2000, 1.24 per cent in 2002, 0.70 per cent, 1.64 per cent in 2008, 2.19 per cent in 2011 and 2.82 per cent in 2014. Whilst not clear from the survey, this result may suggest that cases are increasingly being withdrawn by petitioners and their pre-petition representative legal counsel where the court indicates that it will not grant a simultaneous termination.
[83] *Bankruptcy Act* art 250(2).

The trustee may report on these investigations in writing or orally to the court.[84] In *dōji haishi* cases where no trustee is appointed, the court performs the investigation and may rely on work performed by a pre-petition representative.[85] Court clerks (*shokikan*) perform an important role in the investigation process, and will check that all documentation is in order and may ask for further information from the debtor and pre-petition representative. The debtor is required to cooperate with the court or trustee's investigation prior to any discharge and failure to do so is grounds for refusing a discharge.[86]

A trustee or creditor has two opportunities to challenge a debtor's petition for discharge. First, the trustee or creditor may provide an opinion to the court on whether a discharge should be granted.[87] Second, if a court grants a discharge, the trustee or creditor may appeal the court's decision.[88] There are no specific grounds for an appeal in the legislation. The types of circumstances that may give rise to an appeal would typically include those circumstances in which a court may have chosen not to grant a discharge had the court known of certain information. In practice, the trustee's report on whether grounds to refuse a discharge exist largely influences a creditor's decision whether to file an appeal or not.[89] Given the short timeframes involved in Japanese cases, the creditors must work quickly if they intend to lodge an objection or appeal. In fact, there are few cases of creditors objecting to a petition for discharge: 3–4 per cent annually over the last 15 years.[90]

The trust that the court and creditors place in the pre-petition *bengoshi* (attorney) representing the debtor and court-appointed trustees is key to the court's reliance on the information provided by the debtor and the decision to grant a simultaneous termination and discharge with minimum investigation or objections.[91] Recently, in many cases where a *bengoshi* has been engaged as a pre-petition representative, the practice has been to grant commencement of the bankruptcy proceeding and simultaneous termination of the proceeding on the same day as the petition is filed. This process is known as *sokujitsu mensetsu* or same-day interview.[92] The JFBA's survey results suggest that this procedure is used in the majority of cases filed in the Tokyo District Court, with the period between filing and commencement in those cases reportedly being one day and, in any event, commencement otherwise typically occurs within 10 days of filing.[93] Nationally, very few petitioners are self-represented (2.66 per cent in 2014), with most (84.11 per cent) using a *bengoshi* and a small proportion (13.06 percent) using a judicial scrivener (*shihō shoshi*).[94] Self-representation has decreased dramatically since 2000 when it was as high as 30.51 per cent of petitioners; the decline was particularly noticeable between 2005 (29.09 per cent of petitioners unrepresented) and 2008 (11.15 per cent of petitioners unrepresented).[95] The increase in representation reflects the courts' preference for

[84] Ibid art 250(1).
[85] Ito et al, above n 33, 1637.
[86] *Bankruptcy Act* art 252(1)(viii).
[87] Ibid art 251(1).
[88] Ibid art 252(5).
[89] Ito et al, above n 33, 1637.
[90] Committee for Addressing Consumer Problems, above n 2, 5.
[91] On the relationships between insolvency practitioners and courts in Japan, see Stacey Steele, 'Appointing and Remunerating Insolvency Practitioners in Japan: The Roles of Japanese Courts' (2017) 26 *International Insolvency Review* 82.
[92] Jin, above n 8, 238.
[93] Committee for Addressing Consumer Problems, above n 2, 33.
[94] Ibid 4. Similarly, *bengoshi* have been used consistently by petitioners in approximately 80 per cent of cases since 2008, with approximately 20 per cent of petitioners using a *shihō shoshi*. The number of self-represented petitioners in individual rehabilitation proceedings has been negligible since 2008: at 9.
[95] Committee for Addressing Consumer Problems, above n 2, 4.

represented petitioners, including its reduction of the filing fees for people using a representative.

So-called abuse of the system of *dōji haishi* is discouraged by the legislation, which provides that a debtor may not receive a further discharge within seven years, although that is a reduction from the 10-year period under the previous legislation.[96] This forward-looking approach should be contrasted with the Australian proposal to extend the fixed bankruptcy period in certain circumstances. In Japan, debtors are initially given the benefit of the doubt. Even in Japan, however, concerns were raised by creditors about the ease with which bankrupts could obtain a discharge. As the number of bankruptcy cases increased, creditors were concerned about the lack of review by a trustee who typically investigates if there were any acts of avoidance or other reason to dismiss the application for discharge.[97] Historically, approximately 90 per cent of personal bankruptcy cases were accepted as *dōji haishi*. Courts began to use the procedure known as a small-scale trustee procedure (*shōgaku kanzai tetsuzuki*) discussed above, instead of simultaneous termination, depending on certain criteria. The Tokyo District Court, for example, typically appoints a trustee if the debtor has more than ¥200 000 in cash, other than exempted assets, as there may be an opportunity to discover more assets through an investigation by a trustee. The Osaka District Court typically allows a *dōji haishi* case if the total amount of assets including cash, other assets such as savings and insurance, is less than ¥990 000, which is the amount of exempted cash provided for by law.

Dōji haishi cases still make up a significant number of personal bankruptcy cases in Japan, although the precise number depends on the relevant district court, and use of the procedure has decreased over time.[98] In the period from 2000 to 2005, more than 90 per cent of cases were dealt with under this procedure. Since 2011, according to the JFBA survey, this has dropped to about three quarters of cases nationally. The decrease in number may be explained by the introduction of the small-scale proceeding, where a trustee is appointed by the court, and an increase in the number of practitioners working in this area of law who are seeking to be appointed as pre-petition representatives.[99] A trustee was appointed by the court in about 20 percent of all cases in 2014.[100] The decreasing number of *dōji haishi* cases correlates to a slight increase in cases which are withdrawn over the same period. In particular, there was an increase in withdrawals, from 1.57 per cent in 2008 to 2.11 per cent 2011, which coincides with the period when *dōji haishi* cases dropped from 87.70 per cent (2008) to 76.82 per cent (2011).[101] This result supports the conclusion that creditors are not inclined to object, due to the scrutiny of debtors by the court, and pre-petition representatives and trustees who are typically *bengoshi*.[102]

---

[96] *Bankruptcy Act* art 252(1)–(10).

[97] Tetsuo Sato, 'Hasan kanzainin no hōshū ni kansuru shiten to ronten [Point of View and Point of Discussion in Relation to Remuneration for Bankruptcy Trustees]' in *Kanami shinichi taishoku kinen ronshū* [*Collection in Memory of the Retirement of Shinichi Kanami*] (Ritsumeikan daigaku hōgakukai, 2017) (forthcoming).

[98] A recent report suggests that *dōji haishi* proceedings in the Tokyo District Court which has championed small-scale proceedings supervised by a trustee account for about 50 per cent of proceedings: Yamamoto, above n 27, 126.

[99] Steele, above n 91.

[100] Committee for Addressing Consumer Problems, above n 2, 5.

[101] Ibid.

[102] Note that the Republic of Korea adopted a *dōji haishi*-type procedure, beginning with courts in Seoul, after considering Japanese practice and bankruptcy petitions increased dramatically. Unlike Japan, however, pre-petition representatives are judicial scriveners, not *bengoshi*. Although debtors in Korea were found to have attempted to hide assets in only one per cent of all cases, Korean creditors expressed deep reservations about this one per cent case. In response, the courts in Korea also now typically appoint a trustee in almost all cases based on a fixed fee. See JFBA, Shōhisha mondai taisaku iinkai [Committee for Addressing Consumer

Table 3: Number of cases ending in simultaneous termination from 2000 to 2014[103]

Year	2000	2002	2005	2008	2011	2014
Simultaneous termination	93.56%	95.04%	93.03%	87.70%	76.82%	73.55%

C *Obligations in Relation to Income Contributions in Japan*

Although the Australian Proposals Paper suggests reducing the period for discharge, it also asks for submissions on which 'obligations on a bankrupt should continue even after a bankrupt is discharged'.[104] The provisions relating to income contributions are particularly worth considering in light of the Japanese provisions relating to this issue, which are more debtor friendly than the proposals. Currently, a bankrupt in Australia may continue to earn income during the period of bankruptcy,[105] but if the bankrupt's after-tax income exceeds a certain amount, then the bankrupt must pay half of that excess income to the trustee.[106] The trustee may then distribute that income to creditors. This rule currently applies for the duration of the default bankruptcy period, but the Proposals Paper recommends that bankrupts be required to pay income contributions for three years, which is equivalent to the current default period. Moreover, under the government's proposals, income contributions will continue to be payable if the period of bankruptcy is extended to five or eight years.[107]

After a bankruptcy proceeding commences in Japan, a bankrupt is required to provide explanations of matters relating to the bankruptcy proceeding upon request of the trustee, creditors' committee or creditors.[108] The debtor must provide information, including about her or his salary and living expenses.[109] If the bankrupt fails to provide the information or refuses to cooperate, this behaviour could form a reason for the court's refusal to grant a discharge as discussed above, and be a criminal offence.[110] A bankrupt's mail will also be redirected to the trustee after the commencement of a bankruptcy proceeding until the completion of the proceeding.[111] Once a discharge becomes final and binding, however, these obligations cease.[112] This legislative stance reflects the intention of the Japanese reformers to offer bankrupts a 'fresh start' and means that the obligations typically apply for only a few months.[113]

Problems], *Kankoku no hasan seido oyobi hoshōseido ni kansuru hōkokusho* [*Report in Relation to the Korean Bankruptcy System and Guarantee System*] (2014) <http://www.nichibenren.or.jp/library/ja/committee/list/data/2013kankoku_tyousa_report.pdf> 11. The report suggests that although the trustee's remuneration was fixed, the work required of a bankruptcy was not reduced, and trustees are finding it difficult to meet their responsibilities in light of the fixed fee.

[103] Committee for Addressing Consumer Problems, above n 102.

[104] Proposals Paper, above n 1, 7.

[105] Subject to certain licensing and industry restrictions.

[106] Ibid. See also *Bankruptcy Act 1966* (Cth) s 139K.

[107] Proposals Paper, above n 1, 7.

[108] *Bankruptcy Act* art 40.

[109] *Hasan Kisoku* [Bankruptcy Regulations] (Regulations No 14, 2004) (Japan) r 14(3).

[110] *Bankruptcy Act* arts 268(1)–(2).

[111] Ibid art 81.

[112] Ibid art 255(1).

[113] However, as discussed above, certain claims are not able to be discharged even with court consent: *Bankruptcy Act* art 253(1). There was debate about whether claims relating to unpaid taxes should be discharged to give a debtor a fresh start, but this suggestion was not adopted in the legislation, for reasons including on the basis that the government's income stream needed to be protected. In practice, however, tax claims which are treated as

Similar to the current debate in Australia, the treatment of income contributions was a contentious issue in Japanese reform debates. Under the final and current version of the legislation, any and all assets that the bankrupt holds at the time of commencement of a bankruptcy proceeding (irrespective of whether or not it exists in Japan) constitute the bankruptcy estate.[114] A bankrupt's income does not, however, form part of the bankruptcy estate and the bankrupt is free to use moneys received as income. A draft of the new *Bankruptcy Act* published for comment in June 2000 proposed three alternatives on the issue of the treatment of a debtor's income. First, a debtor would be able to choose freely between a bankruptcy proceeding or simplified rehabilitation proceeding. A second alternative provided that the debtor would be discharged from a bankruptcy proceeding only after attempting to repay her or his debts in a rehabilitation proceeding, if her or his expected disposable income exceeded a certain amount. A third alternative suggested that a debtor would be discharged from a bankruptcy proceeding only once she or he repaid debts from income up to a certain amount (a 'minimum payment rate standard' or 'disposable income standard' would apply), as if the debtor had chosen a simplified rehabilitation proceeding , where the expected disposable income of the debtor exceeded a certain amount.[115] The second and third alternatives were mooted because creditors, particularly consumer finance and credit card companies, usually look to a debtor's future income rather than a debtor's current assets.[116] The Insolvency Law Reform Committee eventually chose the first alternative, as reflected in the existing legislative mix, mainly because both the second and third alternatives would have been difficult to implement. Calculating an expected disposable income amount for a debtor with a perceived ability to repay more in all personal bankruptcy cases would have been time-consuming and not cost-effective.[117]

Prior to reforms to the *Bankruptcy Act* in 2004, unsecured creditors used procedures such as compulsory execution (*kyōsei shikkō*), provisional attachment (*kari sashiosae*) and provisional disposition (*kari shobun*) to collect debts, which included executing against a debtor's income.[118] Under the old legislation, a declaration of bankruptcy or filing for simultaneous termination did not prevent creditors from using these types of proceedings prior to a discharge order being confirmed. Accordingly, some creditors were able to obtain payment until discharge. The debtor's dilemma in these circumstances was another driver for the Tokyo District Court's introduction in the late 1990s of the small-scale proceeding, where a trustee is appointed for a fixed fee. The problem was also dealt with explicitly in the final and current version of the *Bankruptcy Act*. Article 249(1) of the *Bankruptcy Act* now stays and prohibits the types of compulsory execution proceedings used prior to 2004, where a debtor files for a discharge and a termination order such as a simultaneous termination order is made. Further, any stayed proceedings will become ineffective after the discharge is confirmed by the court.[119] Continued criticism of the approach which excludes income contributions was also one of the drivers for the scheme in the individual civil rehabilitation procedure, which provides for a debtor to agree to pay a portion of her or his salary for the benefit of creditors over a three to five year period.[120] In practice, however, over 80 per cent of individual insolvencies proceed as personal bankruptcy cases in Japan, and less than 20 per cent of insolvencies proceed as

administrative claims (*zaidan saiken*) are discharged, and accordingly any amount of undischarged tax claim is quite small: see Ito et al, above n 33.

[114] *Bankruptcy Act* art 34(1).

[115] Matsushita, above n 20, 769.

[116] Ibid 770.

[117] Ibid.

[118] Yamamoto, above n 27, 132.

[119] *Bankruptcy Act* art 249(2).

[120] *Civil Rehabilitation Act* arts 129–245.

individual civil rehabilitation cases, which means that these provisions are not commonly used.[121] Therefore, even today, there are still calls to introduce a new scheme in the bankruptcy procedure that requires a debtor to pay a certain amount of future income, when a debtor is expected to receive regular income over a certain amount determined by legislation.[122] Those future amounts will be paid in respect of a certain amount of debt which would not be discharged as a result of the bankruptcy proceeding. This proposal does not, however, include a suggestion that the time period and amount be set with reference to two or three years of future income; rather, the decision would be left to the court, based on its own investigation or an investigation by a trustee into a debtor's living circumstances and expectation of future income, after which the trustee provides an opinion to the court.[123] The majority of commentators in Japan today, however, still support the current formulation in the legislation, which reflects the fundamental importance of the integrity of the discharge system and allows a bankrupt to continue to use her or his income freely, and get a financial fresh start.[124]

Some critics argue that the exclusion of income contributions means that debtors who can expect a high and regular future income will choose a bankruptcy proceeding and discharge, over a rehabilitation proceeding. However, the results from the JFBA survey suggest that people with future financial potential typically use the individual rehabilitation proceedings under the Civil Rehabilitation Act rather than filing for a bankruptcy proceeding. The monthly income of rehabilitation petitioners (¥246 268) is substantially higher than for those petitioners filing for bankruptcy (¥131 612).[125] Further, over a quarter of rehabilitation petitioners in 2014 had an income of over ¥300 000.[126] The amount of debt held by petitioners is also substantially higher than for those seeking bankruptcy. Debts of between ¥10 000 000 and ¥40 000 000 account for approximately 45 per cent of proceedings.[127] These results reflect the nature of the rehabilitation proceedings, which require that a petitioner has the potential to continue to earn an income and there is a possibility of carrying out a payment plan.[128] It also reflects the higher cost of filing for and completing an individual rehabilitation proceeding when compared to a bankruptcy proceeding.[129] On average, a small-scale individual rehabilitation requires payment into court (*yonōkin*) of approximately ¥41 784, and a wage earner etc rehabilitation matter requires approximately ¥89 919 in *yonōkin*.[130]

Similar considerations may be important for a debtor in Australia when choosing between a debt agreement[131] and personal insolvency agreement[132] as opposed to bankruptcy. Debtors with a high expectation of future income may be more likely to choose a debt agreement proceeding over a bankruptcy proceeding despite the proposed reforms. Moreover, making a debtor's income available to creditors for up to three years is unlikely to give debtors an incentive to obtain new or better employment in future. This proposal also appears at odds with

[121] For example, there were 64 081 personal bankruptcy cases filed in 2015, in contrast to 8477 individual civil rehabilitation cases filed: see Court Data Book 2016, above n 11.
[122] Yoshinari Nagashima, 'Menseki [Discharge]' in Tōkyō Bengoshikai Tōsanhō Bu [Tokyo Bar Association, Insolvency Division] et al, *Tōsanhō kaisei tenbō* [*Insolvency Law Reform Outlook*] (Shoji Hōmu, 2012) 568.
[123] Ibid.
[124] Nagashima, above n 122, 569.
[125] Committee for Addressing Consumer Problems, above n 2, 7.
[126] Ibid.
[127] Ibid. These amounts may or may not include home loan obligations.
[128] Ibid.
[129] On the costs of filing generally, see Steele, above n 91.
[130] Committee for Addressing Consumer Problems, above n 2, 11.
[131] *Bankruptcy Act 1966* (Cth) Part IX.
[132] *Bankruptcy Act 1966* (Cth) Part X.

the Australian government's goal of giving a debtor a fresh start, particularly when considered in light of what is possible under the Japanese framework.

D *Restrictions on Access to Credit, Travel, Licences and Industry Associations for Bankrupts and Discharged Bankrupts*

The Australian Proposals Paper also suggests limiting the period of restrictions placed on bankrupts to the default bankruptcy period of one year, subject to a possible extension for misconduct.[133] The reform proposals are threefold. First, reduce the period for restrictions on obtaining credit.[134] However the government does not propose to change the practice of retaining a permanent record of bankruptcy in the National Personal Insolvency Index.[135] Second, the Proposals Paper suggests also reducing the period of restriction on travel overseas by bankrupts to one year.[136] Finally, the government proposes consulting with licensing and industry associations to also align requirements placed on employment or membership by such associations with the new default period.[137] Moreover, to the extent that restrictions are governed by Commonwealth law, the legislation would be reformed to reduce those restrictions to one year: for example, the exclusion from being a company director or a Member of Parliament.[138] The Japanese approach to each of these limitations analysed in this section highlights the impact of the shorter and flexible discharge period in Japan on the capacity of an individual to resume economic activity when compared to the suggestion of a one year period in Australia, but these benefits may be somewhat limited in the context of Japanese entrepreneurs who are also subject to practical limitations on obtaining future credit.

Similar to the situation in Australia, a bankrupt in Japan is prohibited from travelling without obtaining the permission of the court.[139] This provision has to be interpreted, however, in light of the Japanese constitutional guarantee of a certain level of freedom of movement.[140] The bankruptcy prohibition has been interpreted, for example, as allowing a debtor to travel overnight for business or to return to her or his hometown.[141] Domestic travel for two nights or more, however, is considered to be subject to the *Bankruptcy Act* prohibition and is likely to require court approval.[142] The Tokyo District Court, for example, expects a bankrupt to obtain permission for any domestic travel of three or more nights duration.[143] The interpretation in relation to travel overseas, however, is more rigid, with the Tokyo District Court expecting a bankrupt to seek permission for any travel overseas.[144] These restrictions will typically be short-lived, however, because they only apply until the discharge becomes final and binding which usually occurs a few months after filing.

---

[133] Proposals Paper, above n 1, 8.
[134] *Bankruptcy Act 1966* (Cth) s 269.
[135] Proposals Paper, above n 1, 8.
[136] Ibid.
[137] Ibid 9.
[138] Ibid.
[139] *Bankruptcy Act* art 37.
[140] See *Nihon kokukenpō* [Constitution of Japan] art 22 (entered into force 3 May 1947): 'Every person shall have freedom to choose and change his residence and to choose his occupation to the extent that it does not interfere with the public welfare. Freedom of all persons to move to a foreign country and to divest themselves of their nationality shall be inviolate.'
[141] Ito et al, above n 33, 324.
[142] Ibid.
[143] Ibid.
[144] Ibid.

Finally, a bankrupt is permitted to act as a director in Japan. Previously, a person was prohibited from acting as a director of a stock corporation (*kabushiki gaisha*) if they were or had been a bankrupt.[145] The new *Kaisha hō* [Companies Act] (No 86, 2005) (Japan) does not include such a prohibition, based on concerns that it was an obstacle to people obtaining a fresh start, particularly where an entrepreneur's personal bankruptcy was the result of a personal guarantee given in relation to a related business.[146] In practice, a director's employment agreement may terminate on the commencement of a bankruptcy proceeding and a company may otherwise remove a director for bankruptcy by a vote at a general meeting of shareholders.[147] However, these events do not prevent the discharged bankrupt from being hired by another company or starting a new business straight away. Other laws prohibit bankrupts from participating in a number of business occupations, including lawyer, patent attorney, certified public accountant, notary public, guardian, curator, executor of a will, trustee, and limited or general partner. These prohibitions have been criticised in Japan, and there are calls for more consideration to be given to the abolition of provisions restricting people from using their qualifications on the basis that they are bankrupt.[148] In practice, the prohibitions do not last for long, however, because they also cease after a discharge becomes final and binding after a few months.[149]

The recording of bankruptcy on credit databanks poses the biggest obstacle to a discharged entrepreneur's fresh start in Japan. The Australian Proposals Paper also refers to the 'practical difficulties in obtaining credit'.[150] In Japan, a person's credit rating will show whether she or he is a discharged bankrupt where a financial institution records that information with a credit information service.[151] There appears to be no legislative provision on the length of time that this information may be retained. The period seems to depend on the individual data collection service and be somewhere between five and 10 years.[152] In practice, these private reporting systems mean that the discharged bankrupt may be unable to obtain a credit card or new loan from a new bank for five to 10 years.[153] Accordingly, despite the shorter discharge period offered in Japan, the practical duration of a discharged bankrupt's financial incapacity may continue for a similar length of time to Australia. This aspect of Japanese practice drives some entrepreneurs to seek a private workout or restructuring under a civil rehabilitation proceeding,

---

[145] *Kyūshō hō* [Old Company Act] (Act No 48, 1890) (Japan) art 254.2(2).

[146] *Kaisha hō* [Companies Act] (Act No 86, 2005) (Japan) art 331 sets out the limited list of persons who may not act as a director in Japan.

[147] Ito, above n 25, 177.

[148] See Miyagawa Tomonori, *Shōhisha kōsei no hōriron: saimusha kōseihō kōsō kakuron* [*Legal Theory of Consumer Rehabilitation: Debtor Rehabilitation Law Concepts and Debates*], (Shinzansha, 1997) 191ff. From the perspective of protecting a debtor's employment and thus assisting her / him to rehabilitate financially, Miyagawa emphasises that restrictions on a bankrupt acting in certain professional capacities should be abolished. Alternatively, assuming that complete abolition of any restrictions is politically impossible, Nishizawa argues that any restrictions should be limited to the absolutely necessary minimum: Munehide Nishizawa, 'Tōsansha no chii [The Status of Insolvents]' (1997) 1111 *Jurisuto* [*Jurist*] 169.

[149] *Bankruptcy Act* art 255(1).

[150] Proposals Paper, above n 1, 8.

[151] There are three credit information service institutions in Japan: Japan Credit Information Reference Centre Corporation (JICC), <http://www.jicc.co.jp/english/index.html>; Credit Information Centre (CIC), <http://www.cic.co.jp/en/index.html>; and Japanese Bankers Association (JBA), <http://www.zenginkyo.or.jp/en/>.

[152] JICC, CIC and JBA keep the records of negative credit information during the event and for up to five years from the completion of the event. See JICC, *Tōroku naiyō to tōroku kikan* [*Recorded Matters and Period of Recordings*] <http://www.jicc.co.jp/whats/about_02/index.html>; CIC, *CIC ga hoyūsuru shinyōjōhō* [*Credit Information that CIC Retains*] <http://www.cic.co.jp/confidence/posession.html#sst02>; JBA, *Retaining Term of Credit Information* <http://www.zenginkyo.or.jp/en/pcic/retaining/>.

[153] *Burakkuristo wa nannen tatstu to kieru nodeshōka?* [*How Many Years Does It Take to Be Removed from the Blacklist?*] <http://www.caldwellfn.com/005.html>.

and was an important driver for the establishment of the Guidelines for Individual Debtor Out-Of-Court Workouts in 2011.[154]

IV IMPACT OF PERSONAL GUARANTEES GIVEN BY ENTREPRENEURS

A *New Japanese Guidelines for Personal Guarantees Given by Entrepreneurs in Respect of an Enterprise*

Despite the passing of the *Civil Rehabilitation Act* in 1999[155] and reforms to the *Bankruptcy Act* which became effective in 2005, the implications for business people who give personal guarantees to financial institutions in respect of their companies' obligations also remained a significant issue for Japanese SMEs. Historically, Japanese financial institutions require small business owners to provide a personal guarantee for bank finance. On the basis of the JFBA surveys, guaranteed debt or third party obligations consistently appear as the reason for filing in approximately one quarter of cases.[156] Further, whilst the number of people owing money to registered money lending businesses has decreased after a Supreme Court of Japan decision in relation to grey-zone interest, the number of people owing money to guarantee companies saw a major increase from 6.33 per cent in 2008 to 11.21 per cent in 2011 and rose further to 15.10 per cent in 2014.[157] Criticism of early applications for legal workouts as being an abuse of the insolvency process and directors' concerns about the financial and reputational implications of personal bankruptcy, have also traditionally led debtors to simply reschedule repayments with key creditors.[158] Accordingly, by the time legal proceedings are instituted, the parties typically have no option other than bankruptcy, for both the company and the directors because it is too late for rehabilitation.

Recently, the Japanese Financial Services Agency ('FSA') has been pursuing a policy of requiring banks to lend without security or guarantees and rely instead on a thorough assessment of an enterprise's business prospects.[159] The FSA issued Administrative Guidance on 5 December 2013 to encourage financial institutions to refrain from enforcing personal guarantees given by directors and managers in relation to corporate debt, especially of SMEs, in certain circumstances.[160] The Guidelines became effective on 1 February 2014 and apply to

---

[154] See Steele and Jin, above n 10.

[155] Please note that the Act became effective from 2000.

[156] Committee for Addressing Consumer Problems, above n 2. The method for categorising guaranteed debt dates from and including 2011.

[157] Ibid 3. On consumer credit and grey-zone interest, see generally Souichirou Kozuka and Luke Nottage, 'The Myth of the Cautious Consumer: Law, Culture, Economics and Politics in the Rise and Partial Fall of Unsecured Lending in Japan' in Johanna Niemi, Iain Ramsay, William C Whitford (eds), *Consumer Credit, Debt and Bankruptcy: Comparative and International Perspectives* (Hart Publishing, 2009) 199.

[158] On criticisms of using proceedings too early, see Takashi Sonoo, 'Hōteki seiri to shiteki seiri wa kongo doko ni mukau no ka — Tōsan jiken genshō no haikei to shōrai tenbō [Where are Legal Workout and Private Workouts Going Now? Background to Insolvency Case Phenomenon and Future Prospects]' (2016) 2050 *Kinyū hōmu jijō* 6, 14.

[159] 'Kigyō no kyūhaigyō kaizan saiō [Increase in Enterprises Being Wound Up or Dissolved]', *Nikkei Newspaper* (morning ed) (Tokyo), 14 January 2017, 5. This report suggests that many companies are being wound up by elderly entrepreneurs prior to insolvency and thus they avoid having to file for formal bankruptcy proceedings, the numbers of which have in turn decreased.

[160] Guidelines in Relation to a Business Owner's Personal Guarantee, above n 5. On the Guidelines, see Nobuaki Kobayashi, 'Keieisha hoshō ni kansuru gaidorain no gaiyō (ue) [Outline of the Guidelines in Relation to Business Owner Guarantees (Part One of Two)]' (2014) 1018 *New Business Law* 14; Nobuaki Kobayashi, 'Keieisha hoshō ni kansuru gaidorain no gaiyō (shita) [Outline of the Guidelines in Relation to Business Owner Guarantees (Part Two of Two)]' (2014) 1019 *New Business Law* 68; Zadankai [Roundtable discussion: Hiroshi Kato, Manabu Suzuki, Akimitsu Takai and Keizo Fujiwara], 'Keieisha hoshō gaidorain no unyō kaishi kara 2 nen wo mukaete

financial institutions as well as the government's Credit Guarantee Corporation (*Shinyō hoshō kyōkai*) which provides guarantees to financial institutions on behalf of SMEs who could not otherwise obtain a loan.[161] To the extent that the Credit Guarantee Corporation provided support, it was historically expected to insist on its rights as a creditor against the business owner if the Corporation was required to pay a financial institution when a guarantee was called.[162] In this respect, the Guidelines represent a change in government policy and institutions such as the Credit Guarantee Corporation are expected to comply with the Guidelines as administrative guidance, even though technically they are not binding rules.

One aim of the Guidelines is to encourage the winding up of struggling and so-called zombie companies, or companies with no foreseeable future growth prospects, by either formal or informal insolvency proceedings. The underlying obligor is typically a company (the principal debtor) which the guarantor has guaranteed in her or his capacity as director, chair, chief executive officer or owner of the principal debtor. The directors are given incentive to file in relation to the company because by using the Guidelines in relation to personal debt, the director should be able to avoid a formal personal bankruptcy filing. Because the director does not have to file for personal bankruptcy, her or his personal credit rating score is not affected. A debtor must disclose all personal assets and pay as many debts as possible to be eligible for relief under the Guidelines. Under the Guidelines, the financial institution and lawyer acting for the applicant investigates the debtor's payments and assets to assess the eligibility of the applicant. As an additional incentive, the Guidelines are also designed to allow entrepreneurs to keep more exempt assets than would otherwise be available to them in a formal bankruptcy proceeding. A director, for example, is typically able to retain a modest residential house and between ¥1 000 000 and ¥3 600 000 in cash and deposits to support the director's living expenses, which is more than the ¥990 000 provided for under the *Bankruptcy Act*.[163] For entrepreneurs to keep more exempt assets than would otherwise be available to them in a formal bankruptcy proceeding, however, there must be a corresponding benefit to creditors. The benefit is calculated by comparing the amount which is expected to be realised for distribution to creditors in the rehabilitation insolvency process in relation to the principal debtor (that is, the enterprise), and the expected realisation amount if the enterprise had been placed into formal bankruptcy proceedings. If the comparison leads to a positive amount, the guarantor is entitled to a greater amount as exempt assets than would be the case if the *Bankruptcy Act* provisions applied.[164] These provisions are designed to encourage an entrepreneur who has

— Junsokugata shiteki seiri tetsuzuki no tekiyō jirei ni okeru kadai to tenbō [Welcoming the Second Year from the Commencement of the Operation of the Guidelines in Relation to a Business Owner's Personal Guarantee — Issues and Outlook Based on Applied Examples under Rule-Based Private Workout Proceedings]' (2015) 2018 *Kinyū hōmu jijyō* 6. The Guidelines provide for four situations: promoting funding without relying on a personal guarantee; procedures when entering into a personal guarantee; procedures for reviewing an existing personal guarantee; and workout of a personal guarantee in parallel with the debt of the debtor.

[161] Established under the *Shinyo hoshō Kyōkai Hō* [Credit Guarantee Association Act] (Act No 196, 1953) (Japan). See also Zenkoku Shinyō Hoshō Kyōkai Rengōkai [Japan Federation of Credit Guarantee Corporations] <www.zenshinhoren.or.jp>.

[162] On the Japanese system of public credit guarantees, see Ichiro Uesugi, Koji Sakai and Guy M Yamashiro, 'The Effectiveness of Public Credit Guarantees in the Japanese Loan Market' (2010) 24 *Journal of the Japanese and International Economies* 457. For an analysis on loan guarantee schemes based on US data, see Diana Hancock, Joe Peek and James A Wilcox, 'The Repercussions on Small Banks and Small Business of Procyclical Bank Capital and Countercyclical Loan Guarantees' (Paper presented to AFA 2008 New Orleans Meetings, March 2007) <http://ssrn.com/abstract=973976> 1.

[163] Chūshō kigyō chō [The Small and Medium Enterprise Agency], *Keieisha hoshō ni kansuru gaidorain* [*Guidelines in Relation to a Business Owner's Personal Guarantee*] <http://www.chusho.meti.go.jp/kinyu/keieihosyou/>.

[164] See Kobayashi, 'Outline of the Guidelines Part Two', above n 160, 72.

guaranteed the debts of an enterprise to file for enterprise rehabilitation or enterprise liquidation as early as possible. This incentive is a key driver for the Guidelines.[165] If the entrepreneur uses the Guidelines and follows the payment plan, the entrepreneur's remaining debts will be discharged and there will be no record of the insolvency on credit information services. Accordingly, the entrepreneur may avoid the restrictions on access to credit discussed above.[166]

Consent of all creditors is not required for use of the Guidelines. It is possible that other creditors may not even know of the application, because the debtor will make an application directly to the financial institution which has the benefit of the guarantee. Accordingly, other creditors continue to be paid, although the Guidelines prohibit payments, including dividends, to family members or relatives of business owners. The ability to continue to pay trade creditors is also an advantage of using the Guidelines over a formal filing with the court.[167] After commencement of a proceeding, the *Civil Rehabilitation Act* and *Bankruptcy Act* prohibit payments of claims arising against the bankrupt or rehabilitation debtor in the future, based on a cause that has occurred prior to the commencement of proceedings, although the court may consent to such payments in some cases.[168]

Obtaining information about everyday practice under the Guidelines is difficult, because they are not a public procedure like a bankruptcy proceeding, although industry representatives have participated in roundtables and their comments have been published.[169] Knowledge of the Guidelines and how to apply them is increasing amongst legal professionals and is expected to lead to an increased use of the Guidelines. From a financial institution's perspective, the Guidelines provide potential benefits, such as possibly retaining restructured debtors as clients, and achieving a higher return for creditors by avoiding formal proceedings, which may damage enterprise asset prices. The FSA's influential support of the Guidelines and the expectation that the Credit Guarantee Corporation will cooperate should also overcome historical stalemates between various stakeholders, which prevented entrepreneurs and companies from being restructured. The government also provides legal assistance for clients who apply for relief under the Guidelines. The use of these types of administrative guidelines is common in Japan and the content of the Guidelines is unlikely to be legislated for at this stage.[170]

B *The Role of Personal Guarantees in Funding Entrepreneurs in Australia*

The prevalence of personal guarantees given by entrepreneurs to support business activity has also been noted in Australia, but the issue was not addressed by the Proposals Paper, and there is a general lack of research in this area in the context of insolvency law.[171] The role of housing

[165] Ibid
[166] Ibid 76.
[167] On financing small and medium-sized enterprises in Japan, see Kenshi Taketa and Gregory F Udell, 'Lending Channels and Financial Shocks: The Case of Small and Medium-Sized Enterprise Trade Credit and the Japanese Banking Crisis' (2007) 25 *Monetary and Economic Studies* 1. They analyse the different types of lending channels in Japan and how they were affected by the Japanese financial crisis. See also Hirofumi Uchida, Gregory F Udell and Nobuyoshi Yamori, 'How do Japanese Banks Discipline Small- and Medium-Sized Borrowers? An Investigation of the Deployment of Lending Technologies' (2015) *Institutional Approach to Global Corporate Governance: Business Systems and Beyond* (online) <http://dx.doi.org/10.1016/S1569-3767(08)09003-1> 57. This analysis focuses on the use of financial statement lending.
[168] *Bankruptcy Act* art 34(2); *Civil Rehabilitation Act* art 84(1).
[169] See eg, Zadankai [Roundtable discussion], above n 160.
[170] The Guidelines are not intended for general use by institutions not regulated by the FSA.
[171] On access to finance by small and medium-sized enterprises generally, see Gregory F Udell, 'SME Access to Intermediated Credit: What Do We Know and What Don't We Know?' (2015) *Reserve Bank of Australia Conference* 61. He differentiates between inside and outside collateral. Inside collateral refers to those assets

collateral, and thus personal guarantees, in small business lending in Australia, was considered by a paper presented at a Reserve Bank of Australia Conference in 2015.[172] The authors argued that 'higher housing prices increase the value of personal guarantees', because entrepreneurs use the value in their personal assets, such as residential property, as security for business debts, which are also supported by a guarantee.[173] Similarly to Japan, these researchers' interviews with Australian lenders suggests that a typical requirement for a loan to a small business is a personal guarantee, and Australian lenders are more likely to take a personal guarantee than lenders in the United States or the United Kingdom.[174] Australian lenders argue that they need the guarantee because Australia lacks robust personal credit reporting regimes, which is an argument that Japanese lenders have also used.

The issue of reform to the law relating to guarantees in an insolvency context generally was noted by the seminal Harmer Report in 1988.[175] The voluntary administration procedure introduced as a result of the Harmer Report provides that a guarantee or a liability of the company cannot be enforced as against a director, or spouse or relative of a director, during the administration except with the leave of the Court.[176] Courts are reluctant to grant leave to enforce under such a guarantee.[177] The stay on enforcement of personal guarantees for directors who file for voluntary administration was seen as an innovative solution to the problem of the chilling effect of guarantees on directors considering whether to seek assistance when their companies were in financial distress.[178] The mechanism was designed to encourage directors to appoint an administrator as early as possible, to give the company the best chance of recovery.[179] According to the corporate regulator, the Australian Securities and Investments Commission, the 'effect of the appointment of a voluntary administrator is to provide the company with breathing space while the company's future is resolved'.[180] The moratorium on enforcing director guarantees was designed with this goal in mind. However, once a proceeding finishes and a deed of company arrangement ('DOCA') is signed, a creditor may take action under the personal guarantee depending on the contents of the DOCA.[181] Accordingly, it is still important for a guarantor to obtain support for a DOCA from a creditor who holds a guarantee and ensure that any guaranteed debt is dealt with as part of that DOCA.[182]

---

owned by the business entity, which are used to raise finance. Outside collateral is based on the entrepreneur's own assets and thus 'pierces the corporate veil of limited liability': at 91.

[172] Ellis Connolly, Gianni La Cava and Matthew Read, 'Housing Prices and Entrepreneurship: Evidence for the Housing Collateral Channel in Australia' (2015) *Reserve Bank of Australia Conference*, 115.

[173] Ibid 116.

[174] Ibid 119.

[175] Law Reform Commission (Aust), *General Insolvency Inquiry* (Report No 45, 1988) vol 1, 6–8 ('Harmer Report').

[176] *Corporations Act 2001* (Cth) s 440J.

[177] Michael Murray and Jason Harris, *Keay's Insolvency: Personal and Corporate Law and Practice* (Thomson Reuters, 9th ed, 2016) 682 [19.85].

[178] On the disadvantage to other creditors of the guarantor, see Colin Anderson and David Morrison, *Crutchfield's Corporate Voluntary Administration* (Lawbook Company, 3rd ed, 2003) 15.

[179] Ibid.

[180] For a summary of the procedure by ASIC, see 'Voluntary Administration: A Guide for Creditors' (Information Sheet No 74, Australian Securities and Investments Commission, December 2008) <http://download.asic.gov.au/media/1348514/Voluntary_administration_guide_for_creditors.pdf>.

[181] See Murray and Harris, above n 177, 682 [19.85].

[182] Anderson and Morrison, above n 178, 15, warn that beneficiaries of a guarantee 'should be careful to ensure that the right to subsequently call upon the guarantee in relation to the debt, as compromised, is not prejudiced by acceptance of the deed of company arrangement'. They also note (at 197) that a guarantor will be bound by the DOCA in the guarantor's capacity as a contingent creditor of the company. Any extinguishment of the principal debt under a DOCA does not, however, release the guarantor. A release of the guarantor in this context would

Apart from these reforms as part of the voluntary administration procedure, however, the authors of the Harmer Report refrained from making particular recommendations on the basis that the issue of the treatment of guarantees in an insolvency context in Australia required a further in-depth analysis and was outside the Commission's Terms of Reference.[183] Three decades have passed since the Harmer Report, but the matter of guarantees and their interaction with insolvency law is yet to be the subject of a law reform review.[184] The new Japanese Guidelines may suggest options to Australia, even if it is simply that it is time to reconsider the treatment of personal guarantees in the context of personal bankruptcy.

V CONCLUSION: WHERE TO FROM HERE FOR AUSTRALIA?

Australia's proposals for bankruptcy law reform aimed at giving debtors a fresh start are overall less debtor friendly than current legislation and practice in Japan. Reducing the default bankruptcy period and changes in relation to objections to discharge could focus more on the individual debtor's circumstances and less on a particular time period, whether that time period be one or three years, or some lesser period. The Japanese processes are predicated on a reliable and professional body of *bengoshi* (attorneys) who make up the majority of trustees and pre-petition representatives. The courts place a great deal of trust in the *bengoshi*, particularly in the case of simultaneous termination proceedings and small-scale proceedings supervised by trustees. Moreover, an obligation to make income contributions for three years under the Australian proposals appears conservative in light of recent Japanese debates, and detracts from the concept of a fresh start.

Recent Japanese government support for Guidelines in relation to guarantees also highlights the possibility of other continuing obstacles to a 'fresh start' in Australia. Even if restrictions on discharged bankrupts are eased and the time to discharge is shortened in Australia, to the extent that directors cannot avoid personal bankruptcy due to the prevalence of personal obligations which guarantee SME debt, the current reform proposals may not go far enough to achieve the goal of encouraging entrepreneurial activity. Further consideration should be given in Australia to the interaction between SME borrowing and personal guarantees given by directors, if Australia's reform goal of encouraging 'entrepreneurial endeavour' is to be achieved.

require a separate agreement as between the creditor and the debtor which discharges the debtor, thus discharging the guarantor: at 198.

[183] Law Reform Commission, above n 172, vol 1, 6–8.

[184] See generally Connolly, La Cava and Read, above n 171.

QUT Law Review ISSN: Online-2201-7275
Volume 17, Issue 1, pp. 97–113 DOI: 10.5204/qutlr.v17i1.704

SHOULD PENSION SAVINGS BE A PROTECTED PROPERTY AT BANKRUPTCY?

TRISH KEEPER*

In 2015, the New Zealand Court of Appeal held, in Trustee Executors Ltd v The Official Assignee,[1] *a test case brought by the Official Assignee (OA), that the OA could not access the KiwiSaver balances of a bankrupt. In response, the Ministry of Business, Innovation and Employment released a Discussion Document in July 2016, proposing a law change to make some, or all, of a bankrupt's pension savings available to the OA for the benefit of a bankrupt's creditors. This article outlines the Court of Appeal decision and its implications within the context of both the New Zealand Insolvency Act 2006 and the KiwiSaver Act 2006. It then critically discusses the law change proposed in the Discussion Document and suggests that, given the significant difficulties with this proposal, more limited reforms be implemented to prevent bankrupts unfairly using the inalienability of pension savings to defeat the interests of creditors.*

I INTRODUCTION

The 2015 decision of the New Zealand Court of Appeal in *Trustees Executors Ltd v The Official Assignee*[2] ('*Trustees Executors*') highlighted the tension that exists in New Zealand between the government objective of promoting retirement savings and certain objectives of insolvency law. In this case, the Court of Appeal held that New Zealand insolvency law does not override the government objective of promoting retirement savings in limited circumstances. If a debtor in New Zealand is an adjudicated bankrupt, under the *Insolvency Act 2006* and subject to specified statutory exceptions, all of the debtor's property vests in the Official Assignee ('OA').[3] The OA's principal responsibility is then to realise such property and distribute its proceeds to the bankrupt's creditors in accordance with the Act. In most jurisdictions, including Canada, the United Kingdom and Australia,[4] the specified exceptions include retirement savings invested in private pension schemes.[5] In contrast, in New Zealand, only some forms of

* BA, LLB (University of Otago), LLM (Victoria University of Wellington), Senior Lecturer in Commercial Law, School of Accounting and Commercial Law, Victoria University of Wellington, New Zealand. The author thanks the two anonymous referees for their insightful feedback on the earlier draft of this article.

[1] [2015] NZCA 118.

[2] Ibid.

[3] *Insolvency Act 2006* (NZ) s 101 ('*Insolvency Act*').

[4] Donna McKenzie Skene, 'The Composition of the Debtor's Estate on Insolvency: A Comparative Study of Exemptions' (2011) 20 *International Insolvency Review* 29, 38–9.

[5] See also the US Supreme Court decision in *Patterson v Shumate* 504 US 753 (1992), where the trustee sought to recover a debtor's interest in an *Employee Retirement Income Security Act* (ERISA) plan for inclusion in the bankruptcy estate. The Supreme Court upheld the decision of the Court of Appeals for the Fourth Circuit (943 F 2d 362) that a debtor's interest in ERISA-qualified plan was excludable from estate property. In addition, to considering the wording of the relevant provisions of the Bankruptcy Code, which excluded from a debtor's estate an interest in property subject to restriction on transfer enforceable under applicable non-bankruptcy law, the Supreme Court held (at 765) this interpretation was consistent with the public policy of protecting pension benefits underlying ERISA. The Court referred to its decision in *Nachman Corporation v Pension Benefit Guaranty Corporation*, 446 US 359, 375 (1980) where that goal was described as ensuring that 'if a worker has been promised a defined pension benefit upon retirement — and if he has fulfilled whatever conditions are required to obtain a vested benefit — he actually will receive it'.

pensions are given statutory protection in the event of bankruptcy. In situations where there is no express legislative guidance, New Zealand courts have had to determine whether specific forms of pension savings are available to the OA upon bankruptcy.

The *Trustees Executors* decision relates to KiwiSaver, a private, workplace superannuation scheme that has become the most common form of pension scheme in New Zealand. It was set up and continues to be regulated by the *KiwiSaver Act 2006*. The Court of Appeal decision in this case determined that a member's KiwiSaver interest is inalienable against the OA, but the case has highlighted the legislative lacuna with respect to the alienability of private pension schemes in New Zealand. The first part of this article outlines the legislative context in which the *Trustees Executors* case arose and then outlines the High Court and Court of Appeal decisions. The second part of the article discusses the Discussion Document published by the Ministry of Business Innovation and Employment ('MBIE') in July 2016,[6] which arose out of the decision in the Trustee Executors case. The Discussion Document proposes that all forms of private retirement savings should be subject to the same rules, namely, that all or part of a bankrupt's retirement savings should be accessible by the OA, regardless of the type of scheme in which such savings are invested. This article reviews this proposal and argues that it is ill-conceived, would be difficult to apply in practice – particularly with respect to defined benefit schemes – and fails to take into account the rehabilitative objective of New Zealand's insolvency law. In addition, it is an approach that is diametrically opposite to that taken in other advanced economies.

The article argues that the MBIE objective of consistency and certainty in this area can be achieved by an amendment to the *Insolvency Act 2006* stating that all private pension savings are inalienable and do not vest in the OA on adjudication. The article also recommends that the Act be amended by the introduction of new clawback powers under which the OA can seek the divestment of funds paid into a pension scheme made with the intention to defeat creditors.

II BANKRUPTCY UNDER NEW ZEALAND LAW — THE LEGISLATIVE CONTEXT

A *Bankruptcy and the Insolvency Act 2006*

The origin of New Zealand's insolvency law is English personal insolvency law.[7] Early New Zealand bankruptcy statutes were based on the then current statutory regimes in the United Kingdom and subsequently in Australia.[8] Although the current New Zealand statute, the *Insolvency Act 2006* ('*Insolvency Act*') did introduce a new formal insolvency procedure[9] for a debtor who has no realisable assets, the rules governing bankruptcy in the Act are largely unchanged in substance from earlier New Zealand personal insolvency statutes.[10]

Briefly, under the Act, on adjudication of bankruptcy, all property belonging to the bankrupt vests in the OA.[11] A bankrupt is entitled to retain certain assets, including tools of trade,

[6] Ministry of Business, Innovation and Employment (NZ), *Discussion Document: Accessibility of Retirement Savings in Bankruptcy for the Repayment of Creditors* (2016).
[7] For a history of New Zealand's laws of bankruptcy see Ivan A Hansen, *Bankruptcy in the Beginning: A Historical Survey of the Laws of Bankruptcy* (New Zealand Institute of Credit and Financial Management, 1980).
[8] Lynne Taylor and Grant Slevin, *The Law of Insolvency in New Zealand* (Thomson Reuters, 2016) 3–5.
[9] The no asset procedure was introduced as an alternative to bankruptcy for debtors with no realisable assets and debts of not more than NZ$40 000: *Insolvency Act* ss 361–77.
[10] Taylor and Slevin, above n 8, 5.
[11] *Insolvency Act* s 101.

household and personal effects and a motor vehicle up to a value of NZ$6000.[12] Upon adjudication of bankruptcy, creditors of the bankrupt are unable to pursue individual actions against the bankrupt. Instead, the OA acts for all unsecured creditors to realise assets on behalf of the collective interests of the unsecured creditors. A bankrupt is normally automatically discharged from bankruptcy after a three-year period.[13]

Vesting of property in the OA, occurs automatically under section 101(a) of the *Insolvency Act* without the OA having to take any steps to facilitate transfer. The section provides:

> all property … belonging to the bankrupt or vested in the bankrupt vests in the Assignee without the Assignee having to intervene or take any other step in relation to the property, and any rights of the bankrupt in the property are extinguished; and
> the powers that the bankrupt could have exercised in, over, or in respect of any property… for the bankrupt's own benefit vest in the Assignee.

The term 'property' is given a broad meaning for the purposes of the Act as 'property of every kind, whether tangible or intangible, real or personal, corporeal or incorporeal and includes rights, interests and claims of every kind in relation to property however they arise'.[14] Sections 102 to 104 also deal with the status of the bankrupt's property during bankruptcy. Section 102(a) provides that all property which the bankrupt acquires between the commencement of bankruptcy and discharge vests automatically in the Assignee. Furthermore, any rights that the bankrupt has in the property are extinguished. The focus of section 105 is the effect of sections 101 to 104 on other laws. Section 105(2) states that 'sections 101 to 104 do not affect the operation of any other law that prevents any property from vesting in the Assignee'.

1 *Statutory objectives*

The *Insolvency Act* arose out of a Ministry of Economic Development review of New Zealand's corporate and personal insolvency laws that started in 1999. As part of this review, a list of objectives for New Zealand's insolvency law which Taylor and Slevin describe as 'diverse and sometimes competing'[15] were identified.[16] In terms of relevant objectives for personal insolvency law, these included maximising returns to creditors by providing flexible and effective methods of insolvency administration and enabling persons in bankruptcy to again participate fully in the economic life of the community by discharging them from their remaining debts in appropriate circumstances.[17]

The *Insolvency Act* does not contain a statutory purpose provision and New Zealand courts, when called upon to interpret the Act, have relied upon extrinsic sources, including the Explanatory Notes to the Insolvency Law Reform Bill[18] and statements made in Parliament during the passage of the Bill. For example, this passage by the then Acting Minister of

[12] Ibid s 158.
[13] Ibid s 290.
[14] Ibid s 3.
[15] Taylor and Slevin, above n 8, 6.
[16] New Zealand, Ministry of Economic Developments, *Insolvency Law Review: Tier One Public Discussion Documents* (2001) 15.
[17] Explanatory Note, Insolvency Law Reform Bill 2005 (14-1) (NZ) 2.
[18] The Insolvency Law Reform Bill 2005 was divided into three Bills by the Insolvency Law Reform Bill 2005 Supplementary Order Paper 2006 (No 61), ie: the Insolvency Bill 2006 (NZ); the Companies Amendment Bill 2006 (NZ); and the Cross-Border Insolvency Bill 2006 (NZ).

Commerce from the Third Reading of the Bill was referred to by both the High Court[19] and the Court of Appeal[20] in the *Trustees Executors* decisions:

> These bills…are designed to promote innovation, responsible risk-taking, and entrepreneurialism by not excessively penalising business failure. They are designed to distribute the proceeds to creditors in an equitable manner and in accordance with their relative pre-insolvency entitlements. They are designed to maximise returns to creditors by providing flexible and effective methods of insolvency administration and enforcement that encourage early intervention when financial distress first becomes apparent. They are designed to enable individuals in bankruptcy to participate fully again in the economic life of the community.[21]

It should be noted that this Ministerial statement simply restates the list of Ministry of Economic Development's objectives and does not provide any guidance as to which of the 'diverse and sometime competing' objectives should take priority in the event of a conflict between them.

B *Retirement Savings and the KiwiSaver Act 2006*

The *KiwiSaver Act 2006* ('*KSAct*') substantially came into force on 1 December 2006.[22] The purpose of the Act, set out in section 3, is to:

> … encourage a long-term savings habit and asset accumulation by individuals who are not in a position to enjoy standards of living in retirement similar to those in pre-retirement. The Act aims to increase individuals' well-being and financial independence, particularly in retirement, and to provide retirement benefits.

The *KSAct* is generally focused on employees, who become enrolled automatically in a default KiwiSaver scheme at the start of new employment, although they may opt out within time limits specified in the Act.[23] Employers are required to contribute to an employee's KiwiSaver account, and make deductions from the employee member's wages and salary. The Crown also makes an initial 'kick-start' payment of NZ$1000 and provides annual tax credits.[24] Accordingly, a member's interest comprises three elements: the member's own financial contribution; the employer's financial contribution (where applicable);[25] and the Crown kick-start payment and annual tax credits.

To achieve the purposes of the *KSAct*, it provides that a KiwiSaver account cannot, with prescribed early withdrawal exceptions, be accessed until the member's 'end payment date', which for most will be when the member turns 65.[26] The early withdrawal rules are set out in Schedule 1 of the *KSAct*. These include withdrawals in instances of significant financial hardship, including hardship arising from serious illness; withdrawals to allow a member to purchase a first home; and the ability to transfer to foreign schemes on permanent emigration from New Zealand. Clauses 10 and 11 of Schedule 1 contain rules for significant hardship and serious illness. Any withdrawal in cases of significant financial hardship is at the discretion of

[19] *Official Assignee v Trustees Executors* [2014] NZHC 345, [18].
[20] *Trustees Executors Ltd v The Official Assignee* [2015] NZCA 118, [26].
[21] New Zealand, *Parliamentary Debates*, vol 634, 28 October 2006, 6171.
[22] Except ss 10–21, 22, 23, 33–39, 40–43, 45, 66, and sch 3 as it relates to sub-ss NE3(2)–(6) of the *Income Tax Act 2004* (NZ).
[23] *KiwiSaver Act 2006* ss 9, 10 and 13 ('*KSAct*').
[24] Ibid ss 4 and 226; *Income Tax Act 2007*, s MK1.
[25] *KSAct* s 64(1).
[26] Ibid sch 1, cl 4.

the relevant KiwiSaver scheme manager or administrator who may permit a withdrawal only if there are no reasonable alternative sources of funding and the amount to be withdrawn is limited to an amount sufficient to alleviate the particular hardship.[27] Guidance in clause 11 indicates that 'significant financial hardship' includes difficulties that arise because of a member's inability to meet minimum living expenses or to meet mortgage repayments on his or her principal family residence, resulting in the mortgagee seeking to enforce the mortgage on the residence.[28]

The *KSAct* was amended in 2014 because the *Financial Markets Conduct Act 2013* introduced new governance rules for all managed investment schemes, including KiwiSaver schemes. Section 128 of the *Financial Markets Conduct Act* provides that the purpose of all KiwiSaver schemes must include the provision of 'retirement benefits directly to individuals'[29] and must 'accordingly, restrict exemptions, withdrawals, and the provision of benefits in respect of a member's accumulation (including in the way the trust deed is applied) to those permitted under the KiwiSaver scheme rules under the *KiwiSaver Act 2006'*.[30] The High Court observed in *Trustees Executors* that section 128 was introduced to 'reinforce the clear Parliamentary intention to lock in savings for the future benefit of individual members and to permit early withdrawals only in carefully constrained circumstances'.[31]

Section 127 of the *KSAct*,[32] restricts the ability to assign a member's interest in the following terms:

> (1) Except as expressly provided in this Act, a member's interest or any future benefits that will or may become payable to a member under the KiwiSaver scheme must not be assigned or charged or passed to any other person whether by way of security, operation of law, or any other means.
> (2) However, subsection (1) does not prevent a member's interest or any future benefits that will or may become payable to a member under the KiwiSaver scheme from being released, assigned, or charged, or from passing to any other person if it is required by the provisions of any enactment, including a requirement by order of the court under any enactment (including an order made under section 31 of the *Property (Relationships) Act 1976*).

Accordingly, although both the *Insolvency Act* and the *KSAct* were enacted within six months of each other, neither Act contains any material reference to the other.[33] The question as to how to reconcile the provisions of the two Acts was the central issue before the courts in the *Trustees Executors* decisions.

III THE *TRUSTEES EXECUTORS* DECISIONS

In *Trustees Executors*, the OA's position was that the KiwiSaver accounts of two recently adjudicated bankrupts were property for the purposes of the *Insolvency Act*, and therefore these accounts vested in the OA at the time of adjudication under section 101. In addition, any additional funds accumulated in the accounts during the period of their bankruptcy also were vested in the Assignee. It follows therefore that the OA was entitled to exercise the right of a member under the *KSAct* to apply for early withdrawal of a KiwiSaver account as bankruptcy

[27] Ibid sch 1, cl 10(3)(a)–(b).
[28] Ibid sch 1, cl 11.
[29] *Financial Markets Conduct Act 2013* (NZ) s 128(1)(b).
[30] Ibid s 128(1)(c).
[31] *Official Assignee v Trustees Executors* [2014] NZHC 34, [38].
[32] Prior to the 2014 amendments, s 127 was s 194.
[33] *Official Assignee v Trustees Executors* [2014] NZHC 34, [22].

was an event of 'significant financial hardship' in terms of Schedule 1. Ronald Young J in the High Court found that a KiwiSaver account was 'property' for the purposes of the *Insolvency Act*.[34] He held that such an account was a chose in action as it is a right to receive something in the future that arises in circumstances where the right to claim the account interest is enforceable and will eventuate.[35] In reaching this conclusion, his Honour relied upon the reasoning of Justice Blanchard (as he was at that time) in *Official Assignee v NZI Life Superannuation Nominees Ltd*[36]*('NZI Life')* in relation to whether savings in a private pension scheme were 'property' for the purposes of the *Insolvency Act 1967*. The definition of 'property' in the earlier Act stated that it included any 'valuable thing', and Blanchard J found that a member's interest in such a scheme is

> …at the very least, a contingent interest arising out of a valuable thing. Therefore … in New Zealand an Official Assignee becomes vested … with the bankrupt's rights, whatever they may be, in relation to a superannuation scheme: they are "property … belonging to, if not vested in" the bankrupt.[37]

Ronald Young J held in *Trustees Executors* that the private pension scheme in the *NZI Life* case, which was established under the *Superannuation Schemes Act 1976*, had many features in common with schemes governed by the *KSAct*. This conclusion assisted his Honour to determine that a KiwiSaver account is more than just an expectancy[38] and instead a member has a 'fundamental entitlement'[39] to the member's account balance on retirement at 65. His Honour determined that this fundamental entitlement to receive a KiwiSaver interest, with minimal exceptions, underlay the submission 'that the KiwiSaver scheme is more than an expectancy' and therefore 'a member has a property interest in the scheme'.[40]

The High Court's finding that a KiwiSaver account was property for the purposes of the *Insolvency Act* was accepted by both the OA and Trustees Executors and was not appealed. Instead, Trustees Executors focused its appeal to the Court of Appeal on the High Court's decision that the *KSAct* was not protected from the vesting provisions of the *Insolvency Act*. The OA cross-appealed the High Court's interpretation of the non-assignability provision of the *KSAct*.

Section 105(2) of the *Insolvency Act* provides that 'sections 101 to 104 do not affect the operation of any other law that prevents any property from vesting in the Assignee' but Ronald Young J concluded that the *KSAct* was not an 'other law' for the purposes of this section. He found that section 127(1)[41] of the *KSAct*, which provides that 'an interest under a KiwiSaver scheme must not be assigned or charged or passed to any other persons whether by way of security, operation of law, or any other means', did not apply to claims under the *Insolvency Act* because of the operation of section 127(2), which provides that section 127(1) does not apply to protect KiwiSaver accounts against claims required by another enactment, including

[34] Ibid [32], [51].
[35] Ibid [51].
[36] *Official Assignee v NZI Life Superannuation Nominees Ltd* [1995] 1 NZLR (HC) 684 ('*NZI Life*').
[37] Ibid 697.
[38] See also *Krasner v Dennison* [2000] 3 All ER 234 (CA); *In Re Landau (A Bankrupt)* (1988) Ch 223 where the English Court of Appeal concluded similarly with regard to a personal pension scheme.
[39] *Official Assignee v Trustees Executors* [2014] NZHC 34, [44] and [51].
[40] Ibid [51].
[41] The High Court judgment refers to sub-ss 196(1) and (2), but these provisions were renumbered in the 2014 amendments to sub-ss 127(1) and (2). For the sake of clarity, this article refers to the later numbering, which is also found in the Court of Appeal judgment.

an order under the *Property Relationships Act 1976*, and his Honour held that the *Insolvency Act* was 'another enactment' for the purposes of this provision.[42]

However, the Court of Appeal took the opposite approach and held that the correct interpretation of the Act is that a member's KSA interest is not assignable. Counsel for Trustees Executors argued that section 127(1) is expressed in 'emphatic terms'[43] and 'strong language',[44] and accordingly the divestment exemption in section 127(2) must be interpreted as requiring the enactment in question to provide expressly for the vesting, which is not the case in sections 101 and 102 of the *Insolvency Act*. The Court of Appeal accepted these arguments, although the Court did appear to want to adopt a 'practical and sensible'[45] approach, given the uncertainty arising out of the High Court decision, which left any decision to allow early release of a bankrupt's savings to the managers of the particular KiwiSaver scheme in question. In addition, the Court of Appeal considered that the lower court's finding that such savings were assignable to the OA would create significant practical difficulties in the event that a scheme manager subsequently declined to make the member's savings available to OA. A manager of a scheme would need to set up two separate accounts, one for the OA's interest and one for the member's contributions after discharge. In addition, it is unclear what right the OA would have in relation to those funds once a member has been discharged from bankruptcy.[46]

A *Implications of the* Trustees Executors *Decision*

The Court of Appeal decision in *Trustee Executors* clarifies that KSA funds are protected by the *KSAct*'s non-divestment provision as the law is currently drafted. As this conclusion was principally based on the text of the two enactments and the relevant statutory purposes,[47] by implication, the decision only applies to KiwiSaver schemes, and cannot be applied to other forms of private pension schemes. This is because there is no specific statutory protection for pension savings in the *Insolvency Act 2006*. In its place, New Zealand courts have had to rely on general principles of law, specific superannuation regulations and the terms of the scheme in question, when called upon to decide if funds invested in private pension schemes are exempt property.[48] This has led to inconsistent results.

As discussed above in the *NZI Life* case, the Court held that in the absence of any government regulations providing for it, a clause in a trust deed for a private pension scheme which purported to shield a bankrupt member's account from vesting in the OA was a fraud on the laws of bankruptcy.[49] Nonetheless, on the facts of the case, the Court determined that the forfeiture clause was a valid exception to that rule, because the clause was created by statutory regulation. As such, the clause did shield members who joined the relevant scheme before 1 April 1990. However, for those who joined after this date, the clause was void, as the enabling statutory regulation had been repealed on that date.[50] Accordingly, for those members who joined the scheme after 1 April 1990, their pension savings would vest in the OA on bankruptcy. But the OA was held only to have identical rights to those of the bankrupt members

[42] *Official Assignee v Trustees Executors* [2014] NZHC 34, [72]–[73].
[43] *Trustees Executors Ltd v The Official Assignee* [2015] NZCA 118, [51].
[44] Ibid [52].
[45] Ibid [50].
[46] Ibid [67]–[68].
[47] Ibid [80].
[48] *Official Assignee v NZI Life Superannuation Nominees Ltd* [1995] 1 NZLR (HC) 684.
[49] Ibid 694.
[50] Ibid 695.

of the fund. As the bankrupt member under the terms of the trust deed was not entitled to receive benefits other than on death, permanent disability, permanent emigration or retirement age of 60 (unless the trustee exercised its discretion to make an early payment on the grounds of hardship), the OA was required to wait for the occurrence of the first of the eventualities before being entitled to receive any benefit from the fund.[51] The *NZI Life* decision has been described as giving the OA an interest that 'might merely represent a pyrrhic victory for creditors'.[52] This would be the case especially if the bankrupt member is relatively young and where 'it will be difficult if not impossible for the Official Assignee to realise that interest for the benefit of creditors'.[53]

Nonetheless, the *NZI Life* decision does stand for the principle that some forms of private pensions may be available to meet the debts of a bankrupt.[54] In contrast, other forms of pensions are expressly stated to be inalienable. For example, the *Government Superannuation Fund Act 1956* (which regulates the provision of a government superannuation fund for certain public sector employees) provides in section 92 that a retirement allowance under that Act is inalienable. Furthermore, the New Zealand National superannuation, which is a universal pension payable at 65 to all New Zealanders, is expressly stated not to be assignable and exempt from OA claims.[55] New Zealand first introduced a pension that was not means tested in 1938, as part of a range of measures in the *Social Security Act 1938* under a broad framework of citizenship entitlement.[56] Universal entitlement continues to be a feature of the New Zealand regime,[57] as the current statute expressly provides that every person is entitled to receive New Zealand superannuation, subject only to satisfying the age and residency requirements of the Act.[58] Accordingly, a person's financial or employment status does not affect that person's entitlement to New Zealand superannuation. However, receipt of superannuation (or any other form of government benefit) by a bankrupt is taken into account by the OA in determining whether to provide an allowance for the support of the bankrupt and his or her relatives and dependants, or the amount of any such allowance.[59]

As stated above, the claim by the OA against Trustees Executors was brought as a test case to clarify the status of funds invested in a KiwiSaver scheme on the insolvency of a member of the scheme. As the OA was ultimately unsuccessful, MBIE published a Discussion Document about retirement savings being accessible for creditors of a bankrupt,[60] in July 2016. The Discussion Document proposed changes to the current statutory regime, and these are discussed in the next part of this article.

---

[51] Ibid 697.
[52] Paul R Heath and Julie K Maxton, 'Superannuation Schemes and Insolvency' (1997) 3 *New Zealand Business Law Quarterly* 43, 55.
[53] Ibid 55.
[54] McKenzie Skene, above n 4, 39.
[55] *Government Superannuation Fund Act 1956* (NZ) s 92. Similar exceptions also apply to other government benefits such as war pensions under the *Veterans Support Act 2014* (NZ) s 207(1).
[56] Margaret Tennant, *The Fabric of Welfare: Voluntary Organisation, Government and Welfare in New Zealand, 1840–2005* (Bridget Williams Books, 2007) 73.
[57] The *Social Security Act 1964* (NZ) s 84(1) provides that benefits, as that term is defined in that Act and which includes New Zealand Superannuation, are expressly stated to be not capable of being assigned or charged or passed to any other person by operation of law.
[58] *New Zealand Superannuation and Retirement Income Act 2001* (NZ) ss 7(1) and 8. Note there is an exception to this entitlement in sub-s 7(2), if a person has made an election under the *Injury Prevention, Rehabilitation and Compensation Act 2001* (NZ) to receive weekly compensation under that Act rather than to receive New Zealand superannuation.
[59] *Insolvency Act* s 163. See also *Insolvency Regulations 2007*, cl 8 that requires a bankrupt to provide the OA with details of all income.
[60] Ministry of Business Innovation and Employment, above n 6.

B *Ministry of Business, Innovation and Employment Discussion Document*

1 *Policy Objectives and International Practice*

MBIE's starting point in the Discussion Document is that the inconsistency around the treatment of 'retirement savings' in bankruptcy in New Zealand is unsatisfactory and creates uncertainty for retirement scheme managers, bankrupts and their creditors.[61] This is an assertion that ignores the fact that KiwiSaver schemes are increasingly dominating the superannuation savings landscape in New Zealand and the Court of Appeal decision in *Trustees Executors* has clarified the law in this respect. Furthermore, as discussed above, it overstates any uncertainty that derives from the *NZI Life* decision. Nonetheless, as a solution to this 'problem', MBIE proposes a law change whereby some or all of a bankrupt's pension savings will be made available to the OA and this change would apply across all types of pension schemes. However, in the case of KiwiSaver savings, accessible assets would exclude contributions from the Crown (kick-start contributions and a member's tax credits) on the basis that, otherwise, Crown contributions would be used to repay private debt.

In addition to providing consistency of treatment for private pensions, the asserted rationale for this proposed change is the existence in New Zealand of the universal National Superannuation. MBIE observed that this means 'most individuals will not be in poverty in retirement if they do not have additional retirement savings'.[62] The Discussion Document continues by noting that 'currently, private retirement savings … are considered to be an addition to an adequate retirement income provided by New Zealand Superannuation'. This is a claim that goes against the government policy objective behind the enactment of the *KSAct* which is to encourage Kiwis to save for their retirement in order to allow people to live post-retirement with a standard of living enjoyed during pre-retirement. MBIE's argument also ignores the views of many academics and policymakers who consider that the current rules of eligibility for New Zealand Superannuation are unsustainable. For example, the Commission for Financial Capability, which is a government-funded, independent Crown entity to encourage and provide financial education and planning, states 'the cost of NZ Super (which is taxpayer-funded now) will double by mid-century. Healthcare costs will increase too.' MBIE also noted in its Discussion Document that New Zealand's ageing population is projected to put pressure on government spending.[63] 'Sorted', a government funded website run by the Commission for Financial Capability[64] to promote financial decision-making, states that for most people there 'will be a gap between the income NZ Super provides, and the income we want in retirement'.[65] The rate of NZ Super is set each year and the after-tax NZ Super rate for couples (who both qualify) is based on 66 per cent of the average ordinary time wage after tax.[66] For single people, the after tax rate is around 40 per cent of that average wage.[67]

One of the most important criticisms of the measures proposed in the Discussion Document, is that New Zealand would be out of line with the rules governing the treatment of pensions in comparable jurisdictions. In 2011, Donna McKenzie Skene undertook a survey of the laws regulating the composition of a debtor's estate in insolvency in Australia, Canada, France, Italy, New Zealand, South Africa, the Netherlands and the USA. The survey was completed by

[61] Ibid 5.
[62] Ibid 12.
[63] Ibid.
[64] Sorted, *About Us* < https://www.sorted.org.nz/about-us>.
[65] Sorted, *Guides: Planning for Retirement* < https://www.sorted.org.nz/guides/planning-for-retirement >.
[66] *New Zealand Superannuation and Retirement Income Act 2001*, s 15.
[67] Sorted, *Guides: About NZ Super* < https://www.sorted.org.nz/guides/about-nz-super>.

leading insolvency law academics in each jurisdiction, who were asked a number of questions regarding the nature and extent of the exemptions from a debtor's estate in their respective jurisdictions. In her report, she stated that 'in almost all jurisdictions, the pension fund (or at least, an approved/defined fund) itself is exempt'.[68] MBIE's assessment of why other countries do not allow retirement schemes to be accessed in bankruptcy is that in such countries the population is expected to rely on their own savings to fund their retirement. As discussed above, this is an expectation that now applies equally to the New Zealand population.

2 *Role of Creditors in Insolvency*

In the Discussion Document, MBIE stated that if a bankrupt's retirement savings are protected from the OA's claims, there will be less to meet creditors' claims. While this claim is not disputed, it ignores the reality that creditors also have some responsibility in the creation of debt, especially in relation to consumer debtors. Internationally, there has been a growing amount of research on the causes and consequences of the increasing number of consumer debtors. More recently, there is an emerging body of research on the link between credit and consumption, due to links between the underlying demand for credit and societal changes to consumption.[69] Burton argues that 'credit underpins many aspects of consumption and has been instrumental in the development of what has become known as consumer society'.[70] Related research into the deregulation of financial institutions also indicates that government action or inaction, particularly of the fringe market for financial services, has contributed to rising levels of consumer debt. Furthermore, globally a number of studies have recorded the rise in consumer debtors as a consequence of the lack of controls on the providers of consumer credit, including the providers of credit cards, and calling for increased protection against what is often referred to as predatory lending. Squires, after charting the rise of consumer debt in the United States in the second half of the 20th century, observed that 'accompanying expansion of credit, sometimes by consumer choice, sometimes in response to aggressive marketing by financial institutions, reflects restructuring of financial services in many ways'.[71] Ramsay commented that restructuring of regulation, including consumer lending practices such as 'securitisation and computerised risk-based lending' and the accompanying dominance of neo-liberal ideology, may be included in an account of the changes towards a credit culture in the United Kingdom.[72]

A 2013 World Bank Report into insolvency of natural persons[73] affirmed the value for a country of developing its insolvency regime to provide solutions for the increasing number of insolvent individuals. In this sense, the World Bank Report argues that, as most western societies accept, if not encourage the benefits of lending, the insolvency regime should be

[68] McKenzie Skene, above n 4, 39.
[69] See for example Jason J Kilborn, *Comparative Consumer Bankruptcy* (Carolina Academic Press, 2007); Johanna Niemi-Kiesiläinen, Iain Ramsay and William C Whitford (eds), *Consumer Bankruptcy in Global Perspective* (Hart Publishing, 2003); Stephanie Ben-Ishai and Saul Schwartz, 'Bankruptcy for the Poor?' (2007) 45 *Osgoode Hall Law Journal* 471; Mary Wyburn, 'Debt Agreements for Consumers under Bankruptcy Law in Australia and Developing International Principles and Standards for Personal Insolvency' (2014) 23 *International Insolvency Review* 101, 112–16; Katherine Porter, 'The Damage of Debt' (2012) 69 *Washington and Lee Law Review* 979.
[70] Dawn Burton, *Credit and Consumer Society* (Routledge, 2008) 38.
[71] Gregory D Squires, 'Inequality and Access to Financial Services' in Johanna Niemi, Iain Ramsay and William C Whitford (eds) *Consumer Credit, Debt and Bankruptcy: Comparative and International Perspectives* (Hart Publishing, 2009) 1, 12.
[72] Iain Ramsay, 'Wannabe WAGS and Credit Binges: The Construction of Overindebtedness in the UK' in Niemi, Ramsay and Whitford above n 71, 75, 77.
[73] World Bank, *Report on the Treatment of the Insolvency of Natural Persons* (2013).

viewed as representing 'a sort of trade-off for deregulation of consumer lending. If natural persons are to be exposed to inevitable risk that they do not — and likely cannot — understand or avoid, insolvency restores fair equilibrium by offering insurances against those risks, with the "premiums" financed through small and appropriately distributed increases in the costs of credit'.[74]

Furthermore, the Discussion Document states that from an insolvency policy perspective, the ideal outcome would be for a bankrupt's retirement savings account to be fully utilised to repay its creditors. This statement, however, does not take into account other objectives of New Zealand's insolvency law, including to encourage a former bankrupt to fully contribute to the community after discharge. While it can be argued that the clean slate from liability for most debts, on discharge from bankruptcy, achieves this objective, it can be argued that meaningful rehabilitation requires taking a broader approach.[75] Howell suggests, after reviewing recent bankruptcy literature, that ideas about the scope of these terms fall on a continuum. She states that at the narrow end of the continuum, it is confined to relieving the bankrupt from obligations to pay debts on discharge, or being freed from debt without a payment plan. She observes that other commentators nevertheless take a broader approach, arguing that 'debt discharge may not be sufficient to provide the opportunity for a fresh start for all, or even most, debtors'.[76] Debt discharge, she argues, may be merely a palliative solution that fails to address a debtor's underlying social, economic and financial problems in any meaningful way.[77] Prevention of future indebtedness, through supporting financial literacy education and attention to housing and employment prospects, form part of approaches at the other end of the continuum, which Howell characterises as a rehabilitation-focused fresh start.[78] It is worth noting that recent statistics published by New Zealand Insolvency and Trustee Services identify the most common cause of insolvency nominated by bankrupts who were adjudicated in 2015–16 was 'unemployment or loss of income', at 19 per cent. Domestic discord or relationship breakdown (8 per cent) and excessive use of credit facilities (8 per cent) are the second and third most common contributors to insolvency, as identified by debtors who responded to this question.[79] If the objective of New Zealand insolvency law is rehabilitative in this broader sense, then allowing a bankrupt to retain retirement savings may encourage the bankrupt's rehabilitation into the community or at least encourage the bankrupt to continue contributing where possible to his or her post-retirement funds.

MBIE's Discussion Document does not discuss the financial implications for a bankrupt of the proposed law change. In the United States, a number of studies have analysed the post-discharge financial situation of consumer debtors. In 2006, Porter and Thorne analysed the financial position of 359 debtors who had undertaken a Chapter 7 bankruptcy and found that post-bankruptcy, one in four debtors were struggling to pay routine bills, and one in three reported an overall financial position similar to or worse than when they filed debtor bankruptcy. They reported factors such as decline in household income through unemployment and underemployment, and illness or injury or old age undermined the chance of financial

[74] Ramsay, above n 72, 77.
[75] Nicola Howell, 'The Fresh Start Goal of the *Bankruptcy Act:* Giving a Temporary Reprieve or Facilitating Debtor Rehabilitation?' (2014) *QUT Law Review* 29, 31–3.
[76] Ibid 33.
[77] Howell refers to Jay L Zagorsky and Lois R Lupica, 'A Study of Consumers' Post-Discharge Finances: Struggle, Stasis, or Fresh Start?' (2008) 16 *American Bankruptcy Institute Law Review* 283, as support for this statement.
[78] Howell, above n 75, 33.
[79] New Zealand Insolvency and Trustee Service, *Insolvency Statistics and Debtor Profile Report: 1 July 2015–30 June 2016* (Ministry of Business, Innovation & Employment, 2016) 26. Note: 13 per cent of debtors had indicated 'other' as the primary cause of bankruptcy and 12 per cent of debtors had made no response to this question.

recovery.[80] Zagorsky and Lupica undertook analysis of a large national longitudinal survey which had tracked young baby boomers in the United States from 1979 to 2004 questioning the same group of people 22 times over this period. In 2004, the survey asked whether the individual had been declared bankrupt and 13.5 per cent of respondents answered affirmatively. The survey also asked all responders a series of questions about their financial wellbeing, including income, home and vehicle ownership, credit card debt and savings. The financial wellbeing data for filers and non-filers was then compared. They found that bankruptcy filers were less likely to own a home or have a credit card and that it took 14 years for bankruptcy filers to reach the same level of home ownership as non-filers.[81] Furthermore, filers earn less and have less total income immediately after bankruptcy, but they catch up with non-filers approximately 13 years after having received a discharge. Such studies support the view that releasing a person from debt does not guarantee rehabilitation, or at least that it will take some considerable time for a former bankrupt to be able to participate fully in the economic life of a community.[82]

As stated above, there have been no comparative studies undertaken in New Zealand. However, given the limitations on the business activities of a person who is adjudicated bankrupt,[83] together with the fact that their name is on a public register during the period of the bankruptcy and for four years after discharge, an adjudication of bankruptcy[84] would almost universally reduce a person's ability to achieve full financial recovery after discharge. If the MBIE proposal is implemented into New Zealand law, the likely result will be to further undermine the objective of economic rehabilitation.

3 *Other Implications*

MBIE suggests that it is equitable to treat pension savings equally to other assets of a bankrupt. In the same manner as any equity in real property and any personal property of a bankrupt (subject to limited exceptions) are assets that are realisable by the OA, pension savings should be available in the event of bankruptcy.[85] At first glance, there is some merit to this argument, at least with respect to the *KSAct*. A member of KiwiSaver scheme can apply for early withdrawal of part of their KiwiSaver account to buy a first home and, post-purchase, any equity in such a home would be available to the OA if the member became bankrupt. However, if pension savings are treated as property capable of vesting in the OA upon bankruptcy for the benefit of the unsecured creditors, then it also raises questions as to whether such assets can be treated as property for other purposes. Could a secured creditor claim an interest in pension savings? Alternatively, would it encourage a secured creditor to surrender its charge[86] and submit a proof of debt as an unsecured creditor if the bankrupt's pension savings are substantial?

The Discussion Document does not state what percentage of a bankrupt's retirement savings should be made available to the OA but instead sets out three options.[87] Option 1 provides that the OA can access all financial benefits, including personal and employer contributions (but

[80] Katherine Porter and Deborah Thorne, 'The Failure of Bankruptcy's Fresh Start' (2006–2007) 92 *Cornell Law Review* 67.
[81] Zagorsky and Lupica, above n 77, 298–304, 314.
[82] Ibid 314.
[83] *Insolvency Act* s 7.
[84] Ibid s 62.
[85] Ministry of Business, Innovation and Employment, above n 6, 12.
[86] *Insolvency Act* s 243 (1)(c).
[87] Ministry of Business, Innovation and Employment, above n 6, 14–16.

excluding Crown contributions) of a bankrupt, whereas Option 2 excludes employer contributions from being available to the OA. Option 3 suggests that a set percentage of all retirement savings be accessible by the OA. There is very little detail in the Discussion Document about how these options would work in practice, other than commenting that both Options 1 and 2 could be administratively complex as they would require separate funds for the accessible portion of a bankrupt's pension savings.

The Discussion Document does briefly outline other implications of the proposal to bring pension savings within the pool of assets that are realisable by the OA on behalf of creditors.[88] First, the inclusion of pension savings in the total assets of a bankrupt may reduce the number of debtors who are eligible for the no asset procedure[89] introduced by the *Insolvency Act*. There are also considerations as to whether such savings may be available under a summary instalment order. Perhaps more challenging is how any change might interact with vesting schedules in non-KiwiSaver retirement schemes and how it would influence a defined benefit scheme, where the amount that a member receives depends on his or her final salary and contributions over a fixed period. Finally, the Discussion Document raises the issue of foreign-sourced retirement savings that have been transferred to New Zealand based savings plans.[90]

In conclusion, MBIE's objective of achieving consistency in the treatment of all pension schemes is laudable, but this article suggests a different pathway is needed to achieve this result. Instead of amending the *Insolvency Act* to provide that all or part of retirement savings are accessible by the OA, it is suggested that the Act be amended to state expressly that all such savings be inalienable irrespective of the type of scheme. However, such protection should not be absolute and an order could be made requiring a manager to divest funds to the OA if there is evidence of fraud or that a bankrupt took measures to defeat the interests of creditors. This recommendation is discussed in the final part of this article.

III BANKRUPTCY AND ANTECEDENT TRANSACTIONS

A *The New Zealand Position*

Under the present law, where all KiwiSaver savings are protected from OA claims, these savings may include payments made by the bankrupt in the period leading up to the adjudication of bankruptcy and at a time when the debtor is not making payments to other creditors. Although the *Insolvency Act* does empower the OA to challenge certain transactions in the period prior to the adjudication of bankruptcy, it is unlikely that the insolvent transaction or insolvent gifting provisions of that Act would capture such payment. Such a payment would not be an insolvent transaction, as it does not enable a creditor to receive more than that person would receive or be likely to receive in the bankruptcy.[91] There is potentially an argument that such a payment could be challenged as an insolvent gift by the OA, provided the payment fell within the two year limit before adjudication.[92] However, the requirement in section 204, that

[88] Ibid 17–18.
[89] The eligibility criteria for the no asset procedure are set out in s 363(1) of the *Insolvency Act*, which provides that the debtor must have no realisable assets; have not previously been admitted to the no asset procedure or been adjudicated bankrupt; have total debts not less than NZ$1000 or more than NZ$40 000; and, under a prescribed means test, the debtor does not have the means of repaying any amount towards the debt.
[90] Ministry of Business, Innovation and Employment, above n 6, 17–18 where it is stated that further discussion will be needed with those countries that allow retirement savings to be transferred to New Zealand.
[91] *Insolvency Act* s 195(1)(b).
[92] Ibid s 204.

gift must be 'to another person'[93] is likely to be problematic, as case law has found that KiwiSaver savings are the property of the bankrupt for the purposes of the Act.[94]

There is potentially an alternative cause of action available to the OA under the subpart 6 of part 6 of the *Property Law Act 1997* (NZ). An order under this Act can be made in a wider range of circumstances and applies when a debtor who was insolvent at the time of transaction, or became insolvent as a result, makes a disposition with the intent to prejudice a creditor, or by way of gift, or without receiving reasonable value in exchange.[95] However, an action under this Act is likely to face similar challenges to one under the *Companies Act 1993* (NZ).

B *The Australian Solution*

An example of the difficult policy issues that can arise in such a situation is illustrated by the Australian case of *Cook v Benson*[96] in 2000. The case concerned the meaning and application of section 120 of the Australian *Bankruptcy Act 1966* (Cth). It provides that except for specified exceptions, a trustee in bankruptcy is able retrospectively to claw back property disposed of by the bankrupt within a given time of the commencement of the bankruptcy. In this case, within the specific period, the bankrupt, Benson, directed that a sum of A$80 000 of money under his control should be paid to three private superannuation corporations. He gave this direction knowing that, four months earlier, judgment had been entered against him for A$35 216.25 which remained unpaid at the time of his direction. Following a sequestration order made in respect of his estate, the trustee in bankruptcy sought to recover the $80 000 from the recipients to whom the payments had been made. The primary judge in the Federal Court (Marshall J)[97] and the dissenting judge in the Full Federal Court (Hely J)[98] found in favour of the trustee, with the majority of the Full Federal Court declining to make the order.[99] An appeal to the High Court by the trustee was unsuccessful, with the majority of the Court refusing to order that the funds be repaid.[100] Kirby J, in his minority judgment, noted that the Federal Court decision would result in significant and 'deleterious consequences for bankruptcy administration and the rights of creditors',[101] and 'would effectively permit persons such as the bankrupt, facing the possibility of bankruptcy, to put beyond the reach of creditors very significant funds (including in money or money's worth) by a simple device, beneficial to the bankrupt'.[102]

The *Bankruptcy Act 1996* (Cth) was amended in 2007 by the inclusion of two new provisions to allow recovery of superannuation contributions which can be seen as a 'legislative response to the legal position'[103] following the High Court decision in *Cook v Benson*. Section 128B is the main avenue of recovery and provides that the trustee may recover superannuation contributions from a person who later becomes bankrupt. It provides that a transfer of property by a person who later becomes a bankrupt (the transferor) to another person (the transferee) is void against the trustee in the transferor's bankruptcy if three requirements are met. First, that

---

[93] Ibid.
[94] *Official Assignee v NZI Life Superannuation Nominees Ltd* [1995] 1 NZLR (HC) 684; *Official Assignee v Trustees Executors* [2014] NZHC 34; *Trustees Executors Ltd v The Official Assignee* [2015] NZCA 118.
[95] *Property Law Act 2007* (NZ), ss 345–9.
[96] *Cook v Benson* (2003) 214 CLR 370.
[97] *Cook (Trustee); In the matter of Benson* [2000] FCA 1777.
[98] *Benson v Cook* (2001) 114 FCR 542, [142].
[99] Beaumont, Kiefel and Hely JJ.
[100] *Cook v Benson* (2003) 214 CLR 370.
[101] Ibid [44].
[102] Ibid.
[103] Michael Murray and Jason Harris, *Keay's Insolvency: Personal and Corporate Law and Practice* (9th ed, Thomson Reuters, 2016) 163.

the transfer is in fact a contribution to an eligible superannuation plan. Second, that the property which made up the transfer would probably have become part of the transferor's estate. Third, the transferor's main intention was to prevent the transferred property from being available to creditors or to hinder or delay the process of making the property available for division among the transferor's creditors.

Section 128B(2) provides that a transferor's main purpose in making a transfer is taken to be the purpose described in paragraph (1)(c) if it can reasonably be inferred from all the circumstances that, at the time of the transfer, the transferor was, or was about to become, insolvent. In addition, section 128B(3) states that regard must also be had to whether, during any period ending before the transfer, the transferor had established a pattern of making contributions to one or more eligible superannuation plans; and, if so, whether the transfer, when considered in the light of that pattern, is out of character. However, subsections (2) and (3) are expressly stated not to limit the ways of showing a transferor's main purpose. There is also a rebuttable presumption of insolvency where the transferor has not kept proper books and records relating to the time of the transfer.

A second provision permits a trustee to recover certain superannuation payments relating to the situation when the contribution is made by a third party for the benefit of a person who later become bankrupt.[104] This section is 'designed largely to cover arrangements under which the person agrees that money which would ordinarily be paid directly to them should instead be paid to a superannuation plan for that person's benefit'.[105] This most common third party contributor is a person's employer, including payments under a salary sacrifice arrangement. There are similar requirements as for section 128B. Sections 128E to 128K set out the procedure for the Official Receiver to recover funds which are void against the trustee under sections 128B or 128C. The Official Receiver may give a superannuation account freezing notice to the trustees of the relevant superannuation plan to recover the void contributions.[106]

C *Other Solutions*

There is a similar provision in section 342A of the *Insolvency Act 1986* (UK)[107] applying to England and Wales,[108] which also allows recovery of excessive pension contributions if a person has been adjudged bankrupt and the bankrupt has certain rights under an approved pension arrangement. The trustee of the bankrupt's estate may apply to a court for an order in respect of any 'excessive contributions', which are defined as contributions that have unfairly prejudiced the individual creditors.[109] The court can make any order that the Court sees fit to restore the position to what it would have been had the excessive contributions not been made. The relevant contributions that the court may consider are the contributions which the individual has made on his or her own behalf and any other contributions made on his or her behalf. In deciding if contributions are 'excessive', the court is required to take into account factors similar to those in the Australian *Bankruptcy Act 1966* (Cth), specifically, to consider whether the purpose of such contributions was to put assets beyond the reach of the person's

[104] *Bankruptcy Act 1966* (Cth) s 128C.
[105] Murray and Harris, above n 103, 163.
[106] See *Bankruptcy Act 1966* (Cth) s 128D for claims by a trustee in bankruptcy.
[107] *Insolvency Act 1986* (UK) c 45; ss 342A to 342C were inserted by s 95(1) of *the Pension Act 1995* (UK) c 26, and were repealed and substituted by the current provisions in 1999 under the *Welfare Reform and Pensions Act 1999* (UK) c 30, s 15.
[108] There is also a similar provision in the *Bankruptcy (Scotland) Act 1985* c 66, s 36A; which was consolidated into the *Bankruptcy (Scotland) Act 2016*, s 101.
[109] *Insolvency Act 1986* (UK) s 343A(2).

creditors and to look at the individual circumstances when those contributions were made. Section 342B provides that the court has a wide discretion as to the orders that can be made and that any sum that is required by order under section 342A is to be paid to the trustee in bankruptcy and forms part of the bankrupt's estate.

IV CONCLUSION

Heath and Maxton observed in 1997, after the *NZI Life* case, that this is an area of law where consistency of approach is all important.[110] They stated:

> The factory worker must be given the same opportunities to use his or her savings for retirement as the city executive. The ability of the executive to employ skilful professionals to make the investment in an inalienable form (eg a family trust) … should not be allowed to undermine the retirement policies of the day. After all, the object is to ensure that all citizens save for retirement so that the State is not obligated to expend large sums of money to maintain them. That is also the rationale for lower tax rates.
>
> We do not have any magic answers to the complexities of this area. Whatever decisions are taken they will have an extensive impact not only on individuals but on society generally.[111]

Heath and Maxton concluded by recommending that much more debate needs to occur before 'firm policy conclusions are drawn'.[112] Although these observations were made almost 20 years ago, they apply equally to the reforms proposed in the Discussion Document.[113] The Court of Appeal decision in *Trustees Executors* has eliminated any uncertainties for KiwiSaver managers arising from the earlier High Court decision[114] and thereby removed any urgency to repeal the law arising from the High Court decision. Any decision to alter the terms of private pension schemes on a uniform basis will be difficult to implement in practice and, in addition, may have a number of unintended consequences. The Discussion Document states that KiwiSaver accounts can have significant value, and if they are 'fully released this may provide an avenue by which creditors can be repaid a greater percentage of the money they are owed by bankrupt persons'.[115] This conclusion ignores the rehabilitative objective of insolvency law, the facts that for many debtors financial distress arises from factors outside of their control and that the proposed law change is contrary to the reality facing most New Zealanders — that an occupation based retirement plan will be essential to retirement security.

Murray and Harris noted that the anti-evasion provisions inserted into the Australian *Bankruptcy Act 1966* (Cth) filled a gap in legislation that gave too much protection to superannuation payments.[116] It is recommended that measures to increase the powers of the OA in cases of fraud or avoidance should also be included in New Zealand's insolvency laws.

---

[110] Heath and Maxton, above n 52, 67.
[111] Ibid 67, 68.
[112] Ibid 68.
[113] Submissions on the Discussion Document closed on 30 September 2016. There has been no response from the MBIE as to the number or content of submissions received at the time of writing of this article.
[114] See Ministry of Business, Innovation and Employment, above n 6, 5, where it is stated that before the Court of Appeal decision, some KiwiSaver managers had 'accepted that a bankrupt person's funds should be withdrawn on the basis of significant hardship in order to repay creditors'.
[115] Ministry of Business, Innovation and Employment, above n 6, 9
[116] Murray and Harris, above n 103, 165.

QUT Law Review ISSN: Online-2201-7275
Volume 17, Issue 1, pp. 114–126 DOI:10.5204/qutlr.v17i1.708

SUPERANNUATION AND BANKRUPTCY: IS THERE A MID-LIFE CRISIS LOOMING?

JENNIFER DICKFOS, CATHERINE BROWN, JASON BETTLES*

Research suggests that Australian bankrupts are increasingly older, have professional backgrounds and generally enjoy higher levels of income than has previously been the case. Significantly, available data also indicates that the numbers of persons entering into bankruptcy hold greater levels of real property, and associated mortgage debt, than in previous decades. Given these trends, the importance of protecting superannuation funds becomes paramount to a bankrupt. However, this paper argues that there is a need to balance the protected asset status of superannuation funds with other objectives, such as achieving a fair distribution of the bankrupt's assets among creditors. This paper examines the extent to which this balance is achieved, particularly in the context of self-managed superannuation funds.

I INTRODUCTION

When the Superannuation Guarantee scheme was introduced in 1992, superannuation funds were not considered to form part of the divisible property in bankruptcy, as members of the superannuation fund, like beneficiaries in a discretionary trust, do not hold a proprietary interest in the fund. Therefore, to ensure that the bankrupt's interest in the superannuation fund did not vest in the Trustee in Bankruptcy, superannuation deeds often contained forfeiture provisions, whereby a member's interest in the fund would cease should they become bankrupt.[1] However, superannuation funds were not specifically listed as exempted property under the *Bankruptcy Act 1966* (Cth) (Bankruptcy Act) until 1994.[2] At the time of passing the *Superannuation Industry (Supervision) Consequential Act 1993* (Cth) ('SIS Consequential Act'), the government's declared intention was to extend the limitation on divisible property to include the interest of a bankrupt in, or payment from, a regulated superannuation or approved deposit fund.[3] Specifically, section 7 of the SIS Consequential Act amended section 116(2) of the Bankruptcy Act by introducing specific exemptions for:

- the interest of the bankrupt in a regulated superannuation or approved deposit fund as defined by the *Superannuation Industry (Supervision) Act 1993* (Cth) ('SIS Act');[4] and
- a payment to the bankrupt from such a fund received on or after the date of the bankruptcy, provided the payment is not a pension within the meaning of SIS Act.[5]

*Jennifer Dickfos, BBus (QIT), LLB (QUT), LLM (QUT), PhD (UQ), Senior Lecturer (Griffith Business School, Griffith University); Catherine Brown, BBus (SCU), LLB (Hons) (SCU), LLM (Hons) (QUT), Lecturer (Griffith Business School, Griffith University); Jason Bettles, BBus (QUT), Partner (Worrells, Gold Coast, Australia). The authors are grateful for the feedback provided by the anonymous referees on this publication.

[1] See Victor J Bennetts, 'Bankruptcy and Superannuation' (1995) 11 *Queensland University of Technology Law Journal* 157. However, Bennetts suggests (at 161) that the interest held by a member of a superannuation fund would vest automatically once the member became bankrupt.

[2] *Superannuation Industry (Supervision) Consequential Act 1993* (Cth) s 7, commenced 1 July 1994.

[3] Supplementary Explanatory Memorandum, Superannuation Industry (Supervision) Consequential Amendments Bill 1993 (Cth) [4].

[4] *Bankruptcy Act 1966* (Cth) s 116(2)(d)(iii).

[5] Ibid s 116(2)(d)(iv).

Thus, the Bankruptcy Act now provides that the interest of a bankrupt in a regulated superannuation fund,[6] or a lump sum payment[7] to the bankrupt from such a fund received on or after the date of bankruptcy,[8] or a split payment from such a fund where the split payment is not a pension,[9] are protected assets, being exempt property of the bankrupt. Importantly, there is no asset protection from bankruptcy unless the fund is a 'regulated superannuation fund' within the meaning of section 19 of the SIS Act.[10] Section 19 requires that the superannuation fund has a trustee; either the trustee is a constitutional corporation pursuant to a requirement in the governing rules or the governing rules provide that the sole or primary purpose of the fund is the provision of old-age pensions; and that the trustee has made a non-revocable election in writing that the SIS Act will apply to the fund. In relation to personal insolvency, the election would appear to be all but mandatory, as without the election the fund is not exempt property of the bankrupt. However, failure to comply with the SIS Act does not, by itself, result in the removal of the exempt status of the fund. Rather, failure to comply with the SIS Act imposes a 'non-complying' status upon the superannuation fund, which has the effect of removing the fund's entitlement to taxation concessions.[11] Essentially, a complying fund is one which is an Australian resident regulated superannuation fund and the trustee has not contravened any of the applicable regulatory provisions[12] and, as a result, has not received a 'notice of compliance' from the relevant regulator.[13]

This paper considers whether superannuation funds are strictly exempt property under the Bankruptcy Act, and the extent to which the balance is achieved between the objectives of a fresh start and a fair distribution of assets to creditors in personal insolvency law. The remainder of the paper is organised as follows. Part II discusses the government policy underpinning the need to provide prudential protection of superannuation savings and the increasing popularity of self-managed superannuation funds ('SMSFs'), particularly in the context of the current Australian bankrupt demographic. Part III provides a discussion of both the narrow and broad view of the 'fresh start' goal in relation to personal insolvency and the need to achieve a balance between achieving a fresh start for the bankrupt and ensuring a fair distribution of the bankrupt's assets amongst creditors. Part IV of the paper considers limitations on achieving this balance by considering the interaction of bankruptcy, superannuation and taxation laws. In that context, the paper analyses two possible areas, in which balancing the objectives of providing a fresh start with ensuring a fair distribution of the bankrupt's assets amongst creditors causes tension; namely the impact of the bankruptcy of a member of a self-managed superannuation fund ('SMSF') on the tax compliant status of the SMSF and the serving of a statutory garnishee notice on a superannuation fund by the Australian Taxation Office ('ATO').

---

[6] Ibid s 116(2)(d)(iii), which also applies exempt property status to an approved deposit fund or an exempt public-sector superannuation scheme within the meaning of the SIS Act.
[7] Meaning a payment which is not a pension within meaning of the SIS Act.
[8] Where a person becomes bankrupt by virtue of a creditor's petition, the date of bankruptcy is the date on which a sequestration order is made: *Bankruptcy Act 1966* (Cth) s 43(2); whereas if the bankrupt presents a debtor's petition, the date of bankruptcy is the date on which the Official Receiver accepts the debtor's petition: *Bankruptcy Act* s 55A(4A).
[9] *Family Law Act 1975* (Cth) Part VIIIB.
[10] *Bankruptcy Act 1966* (Cth) s 116(2)(d)(iii)(D).
[11] SIS Act s 45.
[12] Ibid s 38A, which defines the regulatory provisions to include the SIS Act, the *Superannuation Industry (Supervision) Regulations 1994* (Cth), as well as certain provisions of the *Taxation Administration Act 1953* (Cth) and the *Corporations Act 2001* (Cth).
[13] SIS Act s 42A (in relation to self-managed superannuation funds), and s 42 (for all other superannuation funds).

II PROTECTION OF SUPERANNUATION FUNDS IN BANKRUPTCY: IS THERE A MIDDLE-AGED PROBLEM?

The compulsory superannuation guarantee scheme was introduced in 1992 as a response to Australia's expanding aged population. The aim of the scheme was to compel superannuation contributions by employers to strengthen the retirement savings, thus reducing the reliance on the government's aged pension and increasing Australia's national savings.[14] Twenty five years later, the Australian government introduced the Superannuation (Objective) Bill 2016 with the intended purpose of ensuring that the primary objective of the superannuation system, being to 'provide income in retirement to substitute or supplement the age pension', is enshrined in all future legislation and associated regulations that relate to superannuation.[15] If enacted, the primary objective would be supported by subsidiary objectives to be prescribed in regulations.[16] While the subsidiary objectives have not, as yet, been prescribed, it is expected that they will be able:

- To facilitate consumption smoothing over the course of an individual's life;
- To manage risks in retirement;
- To be invested in the interests of superannuation fund members;
- To alleviate fiscal pressures on government from the retirement income system; and
- To be simple, efficient and provide safeguards.[17]

The Bill was ultimately referred to the Senate Economics Legislation Committee, which indicated while there was general in-principle support for defining an overall policy objective among stakeholders,[18] there were numerous concerns about the primary objective as stated. These included the generic wording of the objective,[19] a lack of specificity around what level of income could be considered 'adequate',[20] ensuring that the subsidiary objectives are compatible with the primary objective,[21] and other matters. It is not clear how the primary objective, if legislated, will operate in relation in relation to other laws which may relate to superannuation, such as the Bankruptcy Act, though it is clear that primary and subsidiary objectives are not intended to affect the meaning of any other Commonwealth laws.[22]

In the context of the overall objectives of the superannuation scheme, there are particular risks that face the middle-aged investor.[23] For example, the Australian Competition and Consumer

---

[14] The Treasury (Aust), *Charter of Superannuation Adequacy and Sustainability and Council of Superannuation Custodians* (2013) ch 4 <http://www.treasury.gov.au/Policy-Topics/SuperannuationAndRetirement/supercharter/Report/Chapter-4>. See also Australia's Future Tax System Review, *Australia's Future Tax System: The Retirement Income System: Report on Strategic Issues* (2009) ch 2 <https://taxreview.treasury.gov.au/content/downloads/retirement_income_report_stategic_issues/retirement_income_report_20090515.pdf>.

[15] Superannuation (Objective) Bill 2016 (Cth) cll 5–7. See generally Explanatory Memorandum, Superannuation (Objective) Bill 2016 (Cth) [1.16]–[1.18].

[16] Superannuation (Objective) Bill 2016 (Cth) cl 5(2).

[17] Commonwealth, *Parliamentary Debates*, House of Representatives, 9 November 2016, 3378–3380 (Scott Morrison), 3379.

[18] Senate Economics Legislation Committee, Parliament of Australia, *Superannuation (Objective) Bill 2016* (2017) [2.2].

[19] Ibid [2.11]–[2.20].

[20] Ibid [2.21]–[2.30].

[21] Ibid [2.41]–[2.48].

[22] Superannuation (Objective) Bill 2016 (Cth) cl 5(2).

[23] 'Middle-aged', defined as '... commonly from about 45 to 60 years old': *Macquarie Dictionary* (online ed, 2017) <http://gateway.library.qut.edu.au/login?url=http://www.macquariedictionary.com.au/login>.

Commission ('ACCC') reported in its 2015 Scam Watch report that $24 million was lost by Australians in investment scams.[24] The 2015 Scam Watch Report further identified that do-it-yourself ('DIY') SMSF operators have been reported as prime targets for Australian investment scammers.[25] The ACCC has highlighted the risks of exploitation, particular to the middle-aged investor, stating:

> Australians approaching retirement or recently retired will naturally be looking for opportunities to invest or increase their investments. This mix of available funds through superannuation payouts and a desire to maximise wealth for retirement, leaves the over 55s open to exploitation by investment scammers who offer false promises of high returns and phoney assurances of low risks.[26]

Thus, such scams pose a significant investment risk for middle-aged investors, especially in the context of the current demographic of the average Australian bankrupt. For example, within Australia, approximately 40 per cent of bankrupts are aged 45 years or older and are more likely to have been made bankrupt due to non-business related circumstances, including being subject to a scam, than business-related circumstances.[27] More detailed analysis of the average Australian bankrupt's demographic, as carried out by Ramsay and Sim[28] and Morrison and Lee,[29] indicates an increase in the number of bankrupts with professional occupations, and consequently higher levels of personal income and household income. In noting this continuing trend, Morrison and Lee have also suggested a continuing increase in the level of personal insolvents' unsecured debt. This has led some commentators to suggest that bankruptcy is a 'middle class' phenomenon.[30]

The investment in superannuation in Australia is significant, with $2.1 trillion invested in superannuation industry assets as at 30 June 2016 ($2.0 trillion in 2015).[31] Of this amount, $1292.2 billion ($1246.0 billion in 2015) in assets were held by APRA-regulated superannuation entities and $621.7 billion ($589.9 billion in 2015) were held by SMSFs, which

---

[24] Australian Competition and Consumer Commission, *Targeting Scams: Report of the ACCC on Scam Activity 2015* (2016), 1 <https://www.accc.gov.au/publications/targeting-scams-report-on-scam-activity/targeting-scams-report-of-the-accc-on-scam-activity-2015>.

[25] Ibid 16–17, 29. See also Emma Koehn, 'How to Identify and Beat Investment Scams' *The Australian* (online), 18 June 2016 <http://www.theaustralian.com.au/business/wealth/how-to-identify-and-beat-investment-scams/news-story/afeaf78c08c4ef216fa8df50fce6208b>.

[26] Australian Competition and Consumer Commission, above n 24, 10.

[27] See Australian Financial Security Association, *Business and Non-Business Statistics: Time Series* <https://www.afsa.gov.au/statistics/time-series-0>. It should be noted that the available data on personal insolvency is on documentation completed by persons becoming bankrupt, which in turn is premised on the bankrupt's understanding of the various social factors being reported on. As such, the reliability of the data may be limited. See Ian Ramsay and Cameron Sim, 'Trends in Personal Insolvency in Australia' (Research Paper No 390, Centre for Corporate Law and Securities Regulation, University of Melbourne, 23 March 2009) <http://dx.doi.org/10.2139/ssrn.1367445>. However, it is worth noting that similar age and gender demographics appear to apply in relation to the average New Zealand bankrupt: New Zealand Ministry of Business, Innovation and Employment, *New Zealand Insolvency and Trustee Service: Insolvency Statistics and Debtor Profile Report*: *1 July 2015–30 June 2016* (2016) <https://www.insolvency.govt.nz/assets/pdf/Statistical-Data-Reports/Insolvency-statistics-full-report-2015-16.pdf>.

[28] Ian Ramsay and Cameron Sim, 'Personal Insolvency in Australia: An Increasingly Middle Class Phenomenon' (2010) 38 *Federal Law Review* 283, 291–298.

[29] David Morrison and Rachel Lee, 'Trends in Personal Insolvency in Australia: An Update' (2012) 20 *Insolvency Law Journal* 18.

[30] Ramsay and Sim, above n 28, 283. See also Teresa A Sullivan, Elizabeth Warren and Jay Lawrence Westbrook, *The Fragile Middle Class: Americans in Debt* (Yale University Press, 2000).

[31] Australian Prudential Regulation Authority, *Annual Superannuation Bulletin June 2016* (2017) 6, <http://www.apra.gov.au/Super/Publications/Documents/2017ASBEXCEL201606%20-%20PDF.pdf>.

are regulated by the ATO.[32] The comparatively higher rate of growth of investments in SMSFs between 2015 and 2016 (5.39 per cent, compared to 3.7 per cent growth in APRA-regulated superannuation entities), suggests that SMSFs are the fastest growing superannuation sector in Australia. The popularity of SMSFs is attributed to their ability to provide not only taxation and estate planning opportunities to their members, who must also be trustees of the fund, but also an increased control over investment decisions.[33] Regardless of the reasons underpinning their popularity, what is apparent from the available data is that the likelihood of insolvent persons holding an interest in an SMSF on becoming bankrupt is increasing. In the context of these trends, some consideration of the impact of becoming bankrupt on SMSF investments is warranted.

III BALANCING FRESH START FOR DEBTORS WITH A FAIR DISTRIBUTION AMONG CREDITORS

In Anglo-American legal systems such as Australia, the notion of 'fresh start' is said to be one of the main, if not the most important, objectives of bankruptcy legislation.[34] Despite its importance, what is meant by the term 'fresh start' is by no means clear. Howell[35] argues that the discourse on the fresh start concept ranges from the narrow view, focusing on the discharge of debts, to the broader notion of a 'rehabilitation-focused' fresh start, a view which encompasses the more holistic financial well-being of the debtor.

Proponents of the broader rehabilitation focus acknowledge that reliance solely on the bankruptcy legislation to achieve the fresh start objective is not sufficient and that other laws, policies and programs will impact the ability of a debtor to obtain a fresh start.[36] Thus, it is argued that adopting a rehabilitation focus to the fresh start objective requires consideration of the bankrupt's finances as a whole. In that regard, protection of the bankrupt's investments in superannuation funds plays a significant role in providing a discharged bankrupt with a fresh start. Howell provides support for this view, stating:

> Certain property is also exempt from realisation and distribution to creditors. This includes … superannuation interests. These exemptions facilitate the bankrupt maintaining at least a basic standard of living and opportunity for employment and social engagement … following discharge from bankruptcy. They therefore facilitate the wider, rehabilitation sense of the fresh start goal.[37]

Given the age of the average bankrupt, as discussed above, he or she may have only a limited number of full-time working years left before retirement. This shortened period of post-bankruptcy employment can be supplemented, however, by the availability of superannuation funds in retirement. By providing such income the bankrupt's superannuation fund assists the discharged bankrupt in enjoying a basic standard of living and, to that end, is considered to fall within the broader definition of fresh start. The provision of a fresh start is, however, not the only goal of bankruptcy law. A competing and equally important aim is the equal and equitable

[32] Ibid.
[33] See generally George Mihaylov et al, 'Tax Compliance Behaviour in Australian Self-Managed Superannuation Funds' (2015) 13(3) *EJournal of Tax Research* 740; Ron Bird et al, 'Who Starts a Self-Managed Superannuation Fund and Why?' (Working Paper No 127, Centre for International Finance and Regulation, September 2016).
[34] Nicola Howell, 'The Fresh Start Goal of the Bankruptcy Act: Giving a Temporary Reprieve or Facilitating Debtor Rehabilitation?' (2014) 14 *QUT Law Review* 29, 29.
[35] Ibid 33–34.
[36] Ibid 34.
[37] Ibid 36.

distribution of the bankrupt's assets amongst his or her creditors.[38] Given the tension that exists between such goals, a balance must be struck for both goals to be achieved.

The need to balance a fresh start for debtors and a fair distribution of the bankrupt's assets amongst creditors was recently affirmed by Logan J, in the *Trustees of the Property of Morris (Bankrupt) v Morris (Bankrupt)*[39] ('*Morris*') in which the balance favoured providing a fresh start to the bankrupt. The issue in *Morris* was whether two separate payments received by the bankrupt (Ms Morris) from her deceased husband's regulated superannuation funds after Ms Morris was declared bankrupt were after-acquired property, and therefore divisible among her creditors,[40] or exempt property.[41] In deciding that both payments were exempt property, Logan J considered the meaning and effect of the exemption of the bankrupt's 'interest in a regulated superannuation fund', stating:

> That interest was not proprietary but, upon the favourable exercise of the discretion, a proprietary interest was created, and that interest was, quite literally, an interest in a regulated superannuation fund, for there is no dispute between the parties that each of the [husband's superannuation funds] is a regulated superannuation fund within the meaning of the SIS Act.[42]

Logan J arguably adopted a broad view of the fresh start goal, noting earlier statements of parliamentary intention throughout Australia.

> When one looks at the progressive amendment, not just of s 116(2)(d), but elsewhere of s 116(2), one sees particular progressive value judgments by Parliament reflecting changes in Australian society and provision in that society in respect of benefits for retirement, either by age, invalidity or death, or alternatively, the division of such benefits in the course of resolving a property dispute in a matrimonial cause.[43]

However, there are limits to the extent to which a bankrupt's superannuation investment is protected. This point was highlighted by Edmonds, Gordon and Beach JJ in *Di Cioccio v Official Trustee in Bankruptcy (as Trustee of the Bankrupt Estate of Di Cioccio)*, who stated in relation to the proper construction of sections 58 and 116(2) of the Bankruptcy Act: 'The [Bankruptcy] Act may be read as encouraging a bankrupt to commence re-establishing themselves but, until discharged, the Act does not permit a bankrupt to commence acquiring all kinds of assets to the detriment of a bankrupt's creditors.'[44]

A regulated superannuation fund's asset protection only applies 'on or after the date of bankruptcy'[45] such that if an individual were to withdraw a lump sum cash payment from their superannuation fund prior to being declared bankrupt, those monies or any property purchased with those monies would not be protected. The bankruptcy trustee would be entitled to all or

[38] Australian Law Reform Commission, *General Insolvency Inquiry*, Report No 45 (1988) vol 1 [33].
[39] [2016] FCA 846.
[40] *Bankruptcy Act 1966* (Cth) s 58(1).
[41] Ibid ss 116(2)(d)(iii)(A), 116(2)(d)(iv), 116(2)(a).
[42] *Trustees of the Property of Morris (Bankrupt) v Morris (Bankrupt)* [2016] FCA 846, [27]. Note, that this will not extend to moneys paid from a regulated superannuation fund to a deceased estate as the payment will no longer retain the character of superannuation fund payments. See *Cunningham (Trustee) v Gapes, in the matter of Gapes (Bankrupt)* [2017] FCA 787, [22]-[23] (Collier J).
[43] Ibid [24]
[44] [2015] FCAFC 30, [32].
[45] *Bankruptcy Act 1966* (Cth) s 116(2)(d)(iv).

any of those remaining monies, or property purchased with those monies, at the date of bankruptcy for the benefit of creditors.[46]

The legislation governing both the APRA-regulated superannuation entities and ATO-regulated SMSFs is the SIS Act, the purpose of which is 'to substantially increase the level of prudential protection provided to the superannuation industry, to substantially strengthen the security of superannuation savings, and protect the rights of superannuation fund members'.[47] To achieve these objectives, the SIS Act provides:

- a clear delineation of the basic duties and responsibilities of trustees, and indicates that trustees have primary responsibility for the operation of funds; and
- that trustees and investment managers must be suitable to act as fund trustees and to manage fund moneys respectively.[48]

General anti-avoidance provisions, such as sections 120 and 121 of the Bankruptcy Act, along with the more specific anti-avoidance provisions provided for by sections 128B, 128C and 139ZU of the Bankruptcy Act, prevent the bankrupt's regulated superannuation fund being used as a repository for hiding the bankrupt's property from his or her creditors. For example, sections 128B and 128C are aimed at voiding transfers made by the debtor or third parties on the debtor's behalf where the intention of the transfer was to defeat creditors. This intention need not be the only purpose, but must be a main purpose of the transaction. Such an intention is subjective, and is usually inferred from the circumstances of the transaction, the debtor's financial position at the time, and the result of the transaction.

IV LIMITS TO ACHIEVING THE BALANCE

The protected asset status given to a regulated superannuation fund under the Bankruptcy Act is consistent with Australia's classification as a liberal bankruptcy jurisdiction, prioritising the notions of 'fresh start' for debtors and fair distribution of the bankrupt's assets amongst the bankrupt's creditors.[49] In the circumstances discussed above, such as the operation of the anti-avoidance provisions, it is argued that there is equilibrium between the fresh start and fair and equitable distribution of the bankrupt's assets amongst creditors. However, there are several factors which may affect the existing balance, including the operation of Australian taxation laws, thus causing tensions between the bankruptcy law objectives.

A *Disqualification of SMSF Trustees Due to Bankruptcy*

One area which affects the ability of the bankrupt to achieve a 'fresh start' in the broad sense is the approach taken by the legislature to waiving the disqualification of SMSF trustees who are 'insolvents under administration' ('IUA').[50] Section 17A of the SIS Act requires that all members of a SMSF must be trustees of the super fund, or, if the trustee is a company, directors of the corporate trustee. Section 120(1)(b) of the SIS Act provides that an IUA, which by definition includes an undischarged bankrupt or a person who has executed a Part X

[46] See *Zylvain Stanley Jemielita ex parte: Official Trustee in Bankruptcy* [1966] FCA 1208 and *Klewer v Official Trustee in Bankruptcy (No 2)* [2008] FCA 1788 in which similar circumstances existed.
[47] Explanatory Memorandum, Superannuation Industry (Supervision) Bill 1993, 1.
[48] Ibid.
[49] Rafael Efrat, 'Global Trends in Personal Bankruptcy' (2002) 76 *American Bankruptcy Law Journal* 81, 87–91.
[50] SIS Act s 120(1)(b).

agreement,[51] is disqualified from acting as a trustee of a SMSF. Similarly, section 206B(3) of the *Corporations Act 2001* (Cth) disqualifies an IUA from acting as a director of a company. Section 126K of the SIS Act requires a trustee who becomes a disqualified person to immediately resign as trustee of the super fund. Severe penalties are imposed on the IUA member if he or she does not resign immediately, including two years' imprisonment and a penalty of up to $10 800 if he or she fails to resign.[52]

To remain a complying superannuation fund, entitled to concessional tax treatment, the disqualified trustee needs to cease acting as trustee or director of the corporate trustee immediately. The remaining trustees of the SMSF must notify the ATO in writing within 28 days of the trustee's disqualification.[53] The SMSF then has six months[54] to:

- Roll-over or transfer the disqualified person's superannuation interest into another complying fund or, if the disqualified person can meet a condition of release, pay the interest to the person as a benefit and cease that person's membership of the fund;
- Appoint a small fund trustee who is licensed by APRA; or
- Wind up the fund.[55]

If none of the above options is actioned, the fund automatically becomes non-complying and loses its concessional tax status, which means a loss of benefits equal to the value of the additional tax levied on the fund, by all of the fund's members, not just the member/trustee who has been disqualified.

Maintaining the SMSF's status as a complying fund by achieving any of the options listed above would also seriously affect the bankrupt members' fresh start, given the costs involved and/or the loss of superannuation benefits. For example, rolling over the disqualified person's benefit entitlement into a larger APRA-regulated fund within the six-month limitation period may not be achievable, particularly where the SMSF holds assets that are not quickly realisable, such as real estate. Retaining complying superannuation status by appointing a small APRA licensed fund may also be challenging. Insolvency practitioners advise that the annual fees set by the two available bankruptcy trustees — Australian Executor Trustees and Perpetual Limited — for services as a small fund trustee may be prohibitive.[56] Furthermore, this may not be the most cost effective approach to SMSFs with smaller investment balances, for example where the sole asset of the fund is a negatively geared residential rental property, as the ongoing costs are proportionately greater than those with larger balances.[57] Finally, winding up the SMSF in circumstances where there is no roll over of members' benefits into another complying SMSF would mean a loss of benefits to each member of the SMSF and certainly would affect the fresh start capability of the insolvent member.

The imposition of disqualification status on a SMSF trustee due to bankruptcy is particularly severe as there is no ability to waive the SMSF trustee's disqualification. By contrast, if a

[51] Ibid sub-s 10(1).
[52] Ibid sub-ss 126K(1)–(2).
[53] Ibid s 42A.
[54] Ibid sub-s 17A(4).
[55] See generally Australian Taxation Office, *Disqualified Trustee as a Result of Dishonesty Conviction: Case Study Scenario* (SMSF Case Studies, 14 October 2016) <https://www.ato.gov.au/Super/Self-managed-super-funds/In-detail/SMSF-resources/SMSF-case-studies/Disqualified-trustee-as-a-result-of-dishonesty-conviction/>.
[56] See John Wasiliev, 'The Nitty-Gritty of Small APRA Funds', *The Australian Financial Review* (online), 11 October 2014.
[57] Ibid.

member of a SMSF is disqualified due to being convicted of an offence under section 126B of the SIS Act, the member may apply within 14 days of the conviction to have the disqualification waived.[58] The policy justifications for the introduction of this provision were clearly aimed at addressing the severity of the disqualification provisions, the Explanatory Memorandum stating that:

> These sections have been inserted to allow the Commissioner to waive the disqualified person requirements for trustees, and responsible officers of trustees, investment managers and custodians of superannuation entities, if the Commissioner believes, given the information provided, that the person is highly unlikely to be a prudential risk to a superannuation entity. Currently the impact of the disqualified person provisions means, for example, that even persons whose only offence was a minor offence involving dishonesty 20 years ago, for example shoplifting, are disqualified persons and cannot act as a trustee, or as responsible officers of trustees, investment managers or custodians. These new sections will enable the Commissioner to waive the disqualified person status of such an individual.[59]

However, if the trustee of the SMSF is disqualified due to being an IUA, it appears that disqualification cannot be waived, regardless of the underlying reason for the trustee's insolvency.[60] Furthermore, such a trustee is disqualified for the duration of their insolvency administration. The basis for not waiving disqualification for IUAs is difficult to discern. It suggests that an IUA is considered more reprehensible and unfit to manage the SMSF than a SMSF trustee convicted of a dishonesty offence, even where there is no dishonesty or *mala fides* associated with the bankrupt's insolvency.[61] Furthermore, the failure to provide a waiver of disqualification of the SMSF trustee is inconsistent with the latitude granted by section 206G(1) of the *Corporations Act 2001* (Cth) which permits a person disqualified from managing a company to apply to the court for leave to manage a particular company or companies.[62] The considerations taken into account when hearing an application for leave to manage a corporation while disqualified were considered in *Adams v ASIC*.[63] They included, among other things, that:

- The legislative policy is one of protecting the public, not one of punishing the offender.
- The aim of the legislation is generally to deter others from engaging in conduct of the particular kind in question and abusing the corporate structure to the disadvantage of stakeholders.
- The court in exercising its discretion should have regard to the nature of the offence that the person was convicted of, as well as the risks involved to other persons if the disqualification was waived.

By analogy to the justifications for waiver in relation to those persons disqualified from being a SMSF trustee or managing companies due to an offence being committed, it is argued that

---

[58] SIS Act s 126B(4).

[59] Explanatory Memorandum, Superannuation Industry (Supervision) Legislation Amendment Bill 1995, [87]–[88].

[60] SIS Act s 126B(1), which provides that the waiver is only applicable to persons disqualified solely because of the operation of s 120(1)(a)(i).

[61] Statistics consistently show that the majority of bankruptcy cases are caused by factors such as unemployment and excessive use of credit, rather than carrying on a business. Since 2007–08 consumer debt has accounted for 75 per cent (lowest: 2012–13) to 85 per cent (highest: 2008–09) of debtors entering bankruptcy, with the latest available figures in 2014–15 showing 78 per cent. See Australian Financial Security Association, above n 27.

[62] If permission is granted, the court order may allow full unrestricted access or impose limiting conditions on the disqualified person's right to direct the company.

[63] (2003) 46 ACSR 68, [8] (Lindgren J).

there may be circumstances which warrant the waiver of the SMSF trustee's disqualification due to bankruptcy.

Firstly, the impact of disqualification on the SMSF trustee may be particularly burdensome given the current demographic of the average Australian bankrupt and the recent popularity of DIY SMSF operators, particularly middle-aged operators, to be prime targets for Australian investment scammers.[64] As previously noted, this burden is not necessarily borne only by the disqualified trustee, but also by the remaining SMSF members, if the SMSF remains non-complying. Secondly, the inability of an IUA SMSF trustee to obtain a disqualification waiver, along with the consequential loss of concessional taxation treatment by the SMSF, invariably impacts upon the availability of fresh start opportunities for the IUA trustee. This loss may be tolerated where the need to substantially strengthen the security of superannuation savings and protect the rights of superannuation fund members[65] is at risk from such an IUA SMSF trustee. However, as is the case with section 206G(1) of the *Corporations Act 2001* (Cth), consideration should be given to the need to strengthen the security of superannuation savings as a determining factor in the decision to waive the disqualification,[66] rather than a justification for a blanket disqualification for every SMSF trustee who is an IUA. This would be consistent with the policy objectives of the superannuation system, discussed above. Thirdly, it may be considered in certain circumstances that the refusal to waive the disqualification is discriminatory in the sense that it has the effect of penalising not only the offending IUA SMSF trustee but also the remaining members of the SMSF, and imposes more than a short-term hardship on the trustee when the assessed risk to the remaining members of the SMSF and the public is relatively small.

SMSF trustees who are disqualified on the basis of being an IUA should be entitled to apply for a waiver of their disqualification. The current approach negatively affects the IUA member's ability to achieve a fresh start without a corresponding positive impact being spread amongst the IUA member's creditors. Where it is considered in the circumstances that the SMSF and the public are not at risk by allowing the IUA to retain his or her trusteeship, then disqualification should be waived. Doing so would mean the maximisation of a fresh start opportunity for the IUA SMSF trustee, as well as the maintenance of concessional tax treatment for the SMSF, for the benefit of remaining members.

B *The Impact of Servicing Garnishee Notices on Superannuation Funds*

As a general rule, a garnishee order requires a judgement creditor to obtain a court order against a third party who owes money to or holds money on behalf of the debtor, to pay those monies to the judgement creditor. Despite the ATO being an unsecured creditor in relation to a debtor's tax debts, the Commissioner of Taxation (Commissioner) has a number of collection and enforcement powers,[67] including a 'statutory garnishee power' pursuant to section 260-5 of schedule 1 of the *Taxation Administration Act 1953* (Cth). This statutory garnishee power provides the Commissioner with the power to recover tax related liabilities from third parties owing money to, or holding money for, a tax debtor.[68]

---

[64] Australian Competition and Consumer Commission, above n 24.
[65] See earlier discussion regarding the purpose of the SIS Act.
[66] The court gives consideration to such circumstances under s 206G(1) of the *Corporations Act 2001* (Cth) when granting leave to a disqualified person to continue to manage a corporation.
[67] See generally, Australian Taxation Office, *Enforcement Measures Used for the Collection and Recovery of Tax-related Liabilities and Other Amounts*, PS LA 2011/18, 3 July 2014, <http://law.ato.gov.au/atolaw/view.htm?Docid=PSR/PS201118/NAT/ATO/00001>.
[68] Ibid [97].

The Commissioner considers the 'serving of garnishee notices is an efficient and cost-effective way of obtaining payment of outstanding debt'.[69] If effective, the power to serve a statutory garnishee notice upon a superannuation fund would provide the Commissioner with effective priority of payment in insolvency, which would affect the fresh start objective of personal insolvency without a counter-balancing distribution of the proceeds of such a garnishee notice amongst the debtor's creditors. However, the Commissioner's ability to serve a statutory garnishee notice validly is subject to certain limitations.

The first limitation is that unless the tax debtor–member's superannuation benefits are payable under the superannuation fund rules, meaning that the superannuation fund trustees are under a presently existing obligation to pay such funds to the tax debtor–member who is legally and beneficially entitled to such funds, the serving of the statutory garnishee notice on the superannuation fund will be unsuccessful. ATO Practice Statement, *Enforcement Measures Used for the Collection and Recovery of Tax-related Liabilities and Other Amounts* states:

> A garnishee notice in respect of any tax-related liabilities may be served on a superannuation fund but it will not be effective until the tax debtor's (member's) benefits are payable under the rules of the fund (for example, the tax debtor retires or dies). A notice served on the fund will generally request payment as a lump sum unless the anticipated retirement income stream can guarantee repayment within a satisfactory period of time.[70]

In the recent case of *Commissioner of State Revenue v Can Barz Pty Ltd & Anor*[71] ('*Can Barz'*), the Queensland Court of Appeal considered the ability of the Queensland Commissioner of State Revenue to recover a payroll tax debt incurred under the *Payroll Tax Act 1971* (Qld) pursuant to section 50 of the *Taxation Administration Act 2001* (Qld) ('TAA Qld'). Section 50 of the TAA Qld, like its Commonwealth equivalent,[72] provides that where a debt is payable by a taxpayer, the Commissioner is empowered to issue a garnishee notice to a person who is 'liable or may become liable to pay an amount to the taxpayer'. In the *Can Barz* case, Can Barz Pty Ltd contracted to sell real estate which was held on trust for the benefit of Bird and Scott, as trustees of the Mewcastle Superannuation Fund ('the SMSF Fund'), which was a SMSF as defined by section 17A of the SIS Act. In the ordinary course of events, Can Barz Pty Ltd would have received the settlement monies from the real estate agent and purchasers and, on receiving instructions, paid those monies to Bird and Scott, who would then have held the sale proceeds as trustees of the SMSF Fund. However, before settlement, the Commissioner of State Revenue issued garnishee notices pursuant to section 50 of the TAA Qld to:

1. Real estate agents and purchasers, requesting them to pay the settlement monies to the Commissioner rather than Can Barz Pty Ltd; and
2. Can Barz Pty Ltd, requesting the company to pay to the Commissioner monies which it would otherwise have paid to Bird and Scott.[73]

In the circumstances before the court, it was clear that neither Scott nor Bird, as trustees of the Fund, held any beneficial interest in the assets of the SMSF Fund. In their capacity as trustees, they were obliged to comply with SIS Act and superannuation laws, as defined by the Mewcastle Trust Deed ('the Trust Deed'), which included an obligation to pay out to members

[69] Ibid [100].
[70] Ibid [118].
[71] [2016] QCA 323.
[72] *Taxation Administration Act 1953* (Cth) sch 1, s 260-5, previously *Income Tax Assessment Act 1936* (Cth) s 218.
[73] *Can Barz Pty Ltd & Anor v Commissioner of State Revenue & Ors* [2016] QSC 59, [6].

or dependants only when the circumstances provided for in the Trust Deed or relevant law had occurred.[74] In their capacity as members of the Fund, the Trust Deed provided that the fund was vested in the trustees and no other person had any legal or beneficial interest in any asset of the fund.[75]

The issue before the Court was the proper construction of section 50 of TAA Qld, specifically whether the statutory garnishee notices were invalid and ineffective where the Commissioner of State Revenue knew that the taxpayer's right to receive payment was not beneficially held by the taxpayer.[76] In the first instance, Bond J declared that the garnishee notices were invalid and ineffective stating:

> I would construe that phrase as encompassing only circumstances in which the right to payment from the garnishee was legally and beneficially held by the taxpayer and the taxpayer was free to use the right in the taxpayer's own interest. To take any other view would be to attribute intention to the parliament in a way which I am not prepared to do.[77]

The Court of Appeal upheld the primary judge's decision, specifically noting that:

> The purpose of the statute is not to permit the recovery of tax by recourse to money which belongs to someone other than the taxpayer or which, for some other reason, could not be lawfully applied by the taxpayer in the payment of his or her own tax debt.[78]

Philip McMurdo JA then went on to hold that it was not open for Bird and Scott, as trustees, to pay the Commissioner from the Fund as this would amount to a contravention of section 62 of the SIS Act, as well as the terms of the Trust Deed.[79]

The second limitation on the effectiveness of a statutory garnishee notice is the Commissioner of Taxation's acknowledgement that the issue of such notice is an exercise of coercive power, so that care must be taken when exercising the power.[80] In the case of *Denlay v Federal Commissioner of Taxation*,[81] Logan J found in favour of the applicant taxpayer in relation to a garnishee notice pursuant to section 260-5 of schedule 1 to the *Taxation Administration Act 1953* (Cth). On the question of the validity of the statutory garnishee notices, Logan J reasoned that section 260-5 confers a discretionary power on the Commissioner which required that the Commissioner take into account a number of mitigating factors when exercising that discretion. Those factors include, among other things, the impact of section 116(2)(d)(iii) of the Bankruptcy Act if the taxpayer were to become bankrupt,[82] the merits of the taxpayer's appeals against certain tax assessments,[83] and the effect of issuing section 260-5 notices on the taxpayer's ability to prosecute the appeals against their assessment.[84] The Commissioner's omission in considering such factors led Logan J to state that the decision to issue the section

[74] *Commissioner of State Revenue v Can Barz Pty Ltd & Anor* [2016] QCA 323, [7].
[75] Ibid.
[76] Ibid [8].
[77] *Can Barz Pty Ltd & Anor v Commissioner of State Revenue & Ors* [2016] QSC 59, [39].
[78] *Commissioner of State Revenue v Can Barz Pty Ltd & Anor* [2016] QCA 323, [81] (Philip McMurdo JA).
[79] Ibid [35]–[38], [82].
[80] Australian Taxation Office, above n 67, [101].
[81] [2013] FCA 307.
[82] Ibid [58].
[83] Ibid [73].
[84] Ibid [75].

260-5 notices was 'subversive of a considered judicial value judgment',[85] and therefore one that no decision maker, acting reasonably, would have made.[86]

When considering whether to issue a section 260-5 notice, it is the Commissioner's policy to pay regard to the financial position of the debtor, other debts of the debtor, whether the collection of tax revenue is at risk and the likely implications of issuing a notice on a tax debtor's ability to provide for a family or to maintain the viability of a business.[87] On the collection of tax revenue being at risk, Logan J noted:

> The 'risk to the revenue' referred to by the decision-maker is undoubtedly a relevant consideration in the making of a s 260-5 notice decision, just as it is in deciding whether or not to grant a stay of a judgment. Reference to that consideration is not a panacea for a failure to consider others. Further, 'risk to the revenue' is not to be considered in the abstract.[88]

In circumstances where prime consideration is given to the collection of tax revenue being at risk, as might typically occur in the event of insolvency, the serving of the section 260-5 notice on the superannuation fund does not ensure a fair distribution of the debtor's assets amongst the tax debtor's creditors, but rather prioritises payment to the ATO. For this reason, it is argued that the Commissioner should include additional considerations when considering whether to issue a statutory garnishee notice. These considerations could include those identified in the *Denlay* and *Can Barz* decisions. For example, the ATO's Practice Statement[89] on enforcement measures could be amended to include specific reference to clarify that the Commissioner is not authorised to issue a section 260-5 notice on a third party in respect of monies where the Commissioner knows that the taxpayer's right to receive payment is not beneficially held by the taxpayer.[90] Specific inclusion of all the factors provided in Logan J's reasoning in *Denlay* could also be included as policy, so as to gauge whether the decision to issue a section 260-5 notice is an excessive use of coercive power.[91]

V CONCLUSION

The protected asset status given to a regulated superannuation fund under the Bankruptcy Act plays a significant role in providing a discharged bankrupt with a 'fresh start'. However, the interaction of taxation, superannuation and personal insolvency laws is such that the balance between the objectives of providing the bankrupt with a fresh start and achieving a fair distribution of the debtor's assets among creditors is under threat. This threat is particularly evident in regard to SMSFs and the impact of a SMSF member becoming an insolvent under administration. Tensions also exist around the validity of the ATO serving a garnishee notice on a superannuation fund in recovering the unpaid taxes of a superfund member who is an insolvent under administration. This paper has suggested how to defuse those tensions through changes to the current approach which may assist in maintaining the importance of superannuation as a means of providing a 'fresh start' in the broad sense of the term while still retaining the equilibrium between the competing bankruptcy goals.

---

[85] Ibid [71].
[86] Ibid [72].
[87] Australian Taxation Office, above n 67, [102].
[88] *Denlay v Federal Commissioner of Taxation* [2013] FCA 307, [80].
[89] Australian Taxation Office, above n 67.
[90] *Can Barz Pty Ltd & Anor v Commissioner of State Revenue & Ors* [2016] QSC 59, [29].
[91] *Denlay v Federal Commissioner of Taxation* [2013] FCA 307.

QUT Law Review ISSN: Online-2201-7275
Volume 17, Issue 1, pp. 127–146 DOI: 10.5204/qutlr.v17i2.721

MEDICAL ASSISTANCE IN DYING: LESSONS FOR AUSTRALIA FROM CANADA

JOCELYN DOWNIE*

I INTRODUCTION

Canada has recently witnessed dramatic changes in end of life law and policy. Most notably, we have moved from a prohibitive to a permissive regime with respect to medical assistance in dying (MAiD). As a number of Australian states are actively engaged in debates about whether to decriminalise MAiD,[1] it is worth reviewing the Canadian experience and drawing out any lessons that might usefully inform the current processes in Australia.

II MEDICAL ASSISTANCE IN DYING IN CANADA (VOLUNTARY EUTHANASIA AND ASSISTED SUICIDE)[2]

A *The Past*

Until 2016, assisted suicide was clearly illegal in Canada. It was an offence under s 241(b) of Canada's *Criminal Code*.[3] Euthanasia was also clearly illegal in Canada—it was murder under the *Criminal Code*.[4] In the early 1990s, Sue Rodriguez, a woman with amyotrophic lateral sclerosis (ALS, a degenerative neurological condition), challenged the prohibitions under the *Canadian Charter of Rights and Freedoms* ('*Charter*'),[5] but was unsuccessful at the Supreme Court of Canada (by the merest 5–4 margin).[6] Over the years, there were a number of failed attempts made to pass legislation that would permit some assisted dying.[7] There was also a Special Senate Committee on Euthanasia and Assisted Suicide, but it too did not end up

*BA Hons (Philosophy) (Queens University), MA (Philosophy) (Queens University), MLitt (Philosophy) (University of Cambridge), LLB (University of Toronto), LLM (University of Michigan, SJD (University of Michigan. Jocelyn Downie is a University Research Professor in the Faculties of Law and Medicine at Dalhousie University. She is a Fellow of the Royal Society of Canada, the Canadian Academy of Health Sciences, and the Pierre Elliott Trudeau Foundation. She is also an Adjunct Professor at the Australian Centre for Health Law Research at the QUT Faculty of Law. Thanks to Kate Scallion for her meticulous and dogged research assistance, and to Ben White and Lindy Willmott for always challenging and stimulating conversations about end of life law and policy in Australia.

[1] See eg, Samantha Hutchinson, 'Andrews Victorian Government to Debate Assisted Dying Law Bill', *The Australian* (online), 25 July 2017 <www.theaustralian.com.au/national-affairs/state-politics/andrews-victorian-government-to-debate-assisted-dying-law-bill/news-story/4ef6b947c57efe05daece184c6bba50d>; Death with Dignity Bill 2016 (SA); 'Voluntary Euthanasia Laws Fail to Pass South Australian Parliament by One Vote', *Australian Associated Press* (online), 16 November 2016 <www.theguardian.com/society/2016/nov/17/voluntary-euthanasia-laws-clear-hurdle-in-south-australian-parliament-after-15th-attempt>; Voluntary Assisted Dying Bill 2016 (Tas); 'Assisted Dying Bill Fails to Pass Tasmanian Parliament', *Australian Associated Press* (online), 24 May 2017 <www.theguardian.com/australia-news/2017/may/25/assisted-dying-bill-fails-to-pass-tasmanian-parliament>.

[2] This section is a modified extract from my book chapter: Jocelyn Downie, 'End of Life Law and Policy in Canada' in Joanna Erdman, Vanessa Gruben and Erin Nelson (eds) *Canadian Health Law and Policy* (LexisNexis, 5th ed, 2017).

[3] *Criminal Code*, RSC 1985, c C-46, s 241(b).

[4] Ibid s 229.

[5] *Canada Act 1982* (UK) c 11, Sch B Pt 1 '*Canadian Charter of Rights and Freedoms*'.

[6] *Rodriguez v British Columbia (Attorney General)* [1993] 3 SCR 519.

[7] Jocelyn Downie, 'Permitting Voluntary Euthanasia and Assisted Suicide: Law Reform Pathways for Common Law Jurisdictions' (2016) 16(1) *QUT Law Review* 84.

recommending changes to the law.[8] However, for decades, there was strong majority public support for the decriminalisation of assisted dying.[9] There was also a growing body of evidence from permissive regimes demonstrating that the feared slippery slopes had not materialised.[10] Additionally, there were significant new decisions from the Supreme Court of Canada on various sections of the *Charter* (for example, introducing new 'principles of fundamental justice' and thereby opening up the possibility of new arguments to be made in court that were not available at the time of *Rodriguez*).[11] Finally, an Expert Panel of the Royal Society of Canada on End of Life Decision-Making recommended the decriminalisation of assisted dying.[12]

B *Three Recent Developments*

Against this historical backdrop, dramatic reform came in the shape of three major developments. Quebec introduced legislation to regulate medical aid in dying,[13] the Supreme Court of Canada ruled that the *Criminal Code* prohibitions on physician-assisted dying violate the *Charter*,[14] and the federal Parliament passed legislation to establish a federal regulatory framework for MAiD.[15]

1 *Quebec's Legislation*

The first development hailed from Quebec. On 12 June 2013, following a truly extraordinary process of expert and public consultation,[16] the Quebec government introduced *An Act Respecting End-of-life Care* ('the Act') to allow medical aid in dying.[17] After some skirmishes in court, the legislation came into force in December 2015.[18] The Act establishes a right to 'end-of-life care', defined as 'palliative care provided to end-of-life patients and medical aid

[8] Canada, Senate Special Committee on Euthanasia and Assisted Suicide, *Of Life and Death – Final Report* (1995).
[9] See eg, Ipsos News Center, 'As Dr Kevorkian Released, Just One Quarter (25%) Believe Doctor-Assisted Suicide Should Be Illegal' (Media Release, 10 June 2007) <www.ipsos-na.com/news/pressrelease.cfm?id=3526>.
[10] See eg, Frances Norwood, Gerrit Kimsma and Margaret P Battin, 'Vulnerability and the "Slippery Slope" at the End-of-Life: a Qualitative Study of Euthanasia, General Practice and Home Death in The Netherlands' (2009) 26(6) *Family Practice* 472; Margaret P Battin et al, 'Physician-Assisted Dying and the Slippery Slope: the Challenge of Empirical Evidence' (2008) 45 *Willamette Law Review* 91; Georg Bosshard, Esther Ulrich and Walter Bär, '748 Cases of Suicide Assisted by a Swiss Right-to-Die Organisation' (2003) 133 *Swiss Medical Weekly* 310.
[11] *Rodriguez v British Columbia (Attorney General)* [1993] 3 SCR 519. See eg, *R v Demers* [2004] 2 SCR 489; *R v Heywood* [1994] 3 SCR 761; *Canadian Foundation for Children, Youth and the Law v Canada (Attorney General)* [2004] 1 SCR 76; *R v Malmo-Levine* [2003] 3 SCR 571.
[12] Udo Schuklenk et al, 'The Royal Society of Canada Expert Panel: End-of-Life Decision-Making' (Final Report, Royal Society of Canada, November 2011) 6-7 <www.rsc-src.ca/en/expert-panels/rsc-reports/end-life-decision-making>; concurrently published as 'End-of-Life Decision-Making in Canada: The Report by the Royal Society of Canada Expert Panel on End-of-Life Decision-Making' (2011) 25(S1) *Bioethics* 1.
[13] *An Act Respecting End-of-Life Care*, RSQ c S-32.0001.
[14] C*arter v Canada (Attorney General)* [2015] 1 SCR 331.
[15] *An Act to Amend the Criminal Code and to Make Related Amendments to Other Acts (Medical Assistance in Dying)*, SC 2016, c 3, 2411.1.
[16] The consultation included 32 experts, 273 briefs, 239 individuals and organisations at public hearings, 114 individuals during 'open mic' sessions, 6 558 completed online questionnaires, 16 000 comments, 21 meetings during a mission in Europe, and 51 deliberative meetings of the Committee. Details are available in *Select Committee on Dying With Dignity Repor*t (Assemblée National Quebec, March 2012) 12-14 <www.assnat.qc.ca/en/travaux-parlementaires/commissions/CSMD/mandats/Mandat-12989/index.html>.
[17] *An Act Respecting End-of-Life Care*, RSQ c S-32.0001.
[18] See *D'Amico c Québec (Procureure Générale)* **[**2015] QCCS 5556; *Quebec (Procureur General) c D'Amico* [2015] QCCA 2138; 'Quebec Court of Appeal Rules Assisted Dying Law Can Stand', *CTV News* (online), 22 December 2015 <montreal.ctvnews.ca/quebec-court-of-appeal-rules-assisted-dying-law-can-stand-1.2709907>.

in dying'.[19] Under the legislation, 'medical aid in dying' is defined as: 'care consisting in the administration by a physician of medications or substances to an end-of-life patient, at the patient's request, in order to relieve their suffering by hastening death'.[20]

The Act permits medical aid in dying for patients who meet all of the following criteria, i.e the patient:

(1) is an insured person within the meaning of the Health Insurance Act;
(2) is of full age and capable of giving consent to care;
(3) is at the end of life;
(4) suffers from an incurable serious illness;
(5) suffers from an advanced state of irreversible decline in capability; and
(6) suffers from constant and unbearable physical or psychological pain which cannot be relieved in a manner the person deems tolerable.[21]

Considerable safeguards are built into the legislation. These include:

- The patients must meet the criteria for access outlined above;
- The patient must request medical aid in dying themselves, in a free and informed manner;[22]
- Only physicians may provide medical aid in dying;[23]
- Physicians must ensure provision of information, confirmation of conditions being met, second independent opinion, and recording of all information;[24]
- Physicians must report medical aid in dying;[25]
- Institutions must report on continuous palliative sedation and medical aid in dying;[26]
- Inspection powers;[27] and
- Oversight by a Commission sur les soins de fin de vie [Commission on end-of-life care].[28]

In an effort to protect access to medical aid in dying and respect conscience, the legislation requires:

- Physicians who object to medical aid in dying must report requests for medical aid in dying to the executive director (or designate) of their institution (if they work in a public institution) or the local authority (if they work in a private facility) or the local community centre (if the patient lives somewhere with no local authority). The executive director must then find an alternative physician for the patient who has made the request.[29]

[19] *An Act Respecting End-of-Life Care*, RSQ c S-32.0001, s 3(3).
[20] Ibid s 3(6).
[21] Ibid s 26.
[22] Ibid s 26.
[23] Ibid s 30.
[24] Ibid s 29.
[25] Ibid ss 36, 46.
[26] Ibid s 8.
[27] Ibid s 21.
[28] Ibid ss 38–47.
[29] Ibid s 31.

- Institutions must offer medical aid in dying unless they offer only palliative care (in which case they may opt out).[30]

Between December 2015 and June 2016, there were 253 requests made for medical aid in dying and 166 cases in which it had been administered. Reasons for requests not (yet) resulting in administration include: the person did not meet the criteria at the time of making the request (27); the person did not meet the criteria during the assessment process or when administration was set to take place (9); the person withdrew the request (24); the person died prior to the scheduled administration (21); the evaluation was still pending (5); and the person rescheduled the administration (1).[31] Between June and December 2016, the number of requests for MAiD increased to 468 and 295 patients received it; as of 31 December 2016, a total of 461 patients were granted MAiD of the 721 who requested it.[32]

2 *Carter v Canada (Attorney General)*

The second development was *Carter v Canada (Attorney General)* ('*Carter*').[33] Kay Carter was a woman with an extremely painful degenerative condition (spinal stenosis) who decided her suffering had become too much; she asked her family to take her to Switzerland for an assisted suicide. They did, and they also became the first named plaintiffs in the case that would change the law in Canada. Then, Gloria Taylor, a woman with amyotrophic lateral sclerosis ('ALS') who wanted an assisted death, joined the case and the British Columbia Civil Liberties Association, representing suffering Canadians more generally, effectively carried the case.

The plaintiffs argued that the *Criminal Code* prohibitions on assisted suicide and voluntary euthanasia violate ss 7 and 15 of the *Charter*.[34] The plaintiffs were successful at trial,[35] lost the appeal (but only on the issue of *stare decisis* — whether the trial judge was bound by the 1993 Supreme Court of Canada decision in *Rodriguez*),[36] but were then successful again at the Supreme Court of Canada,[37] which ruled 9–0 that the *Criminal Code* prohibitions violated the *Charter* and were void. The Supreme Court found that the prohibitions on physician-assisted dying[38] violated s 7 as they limited the right to life, liberty, and security of the person and were

---

[30] Ibid ss 7, 72.

[31] Pierre Deschamps, 'Medical Aid in Dying in Quebec: A Status Report' (Webinar presented to the Canadian Bar Association, 23 November 2016).

[32] 'Over 450 Quebec patients received medical aid in dying last year', *CBC News* (online), 14 March 2017: <http://www.cbc.ca/news/canada/montreal/medical-assisted-death-cases-first-year-1.4023851>.

[33] *Carter v Canada (Attorney General)* [2012] BCSC 886; C*arter v Canada (Attorney General)* [2013] BCCA 435; C*arter v Canada (Attorney General)* [2015] 1 SCR 331.

[34] *Canada Act 1982* (UK) c 11, Sch B Pt 1 '*Canadian Charter of Rights and Freedoms*' s 7 provides that 'Everyone has the right to life, liberty and security of the person and the right not to be deprived thereof except in accordance with the principles of fundamental justice.' Section 15 provides that 'Every individual is equal before and under the law and has the right to the equal protection and equal benefit of the law without discrimination and, in particular, without discrimination based on race, national or ethnic origin, colour, religion, sex, age or mental or physical disability.'

[35] *Carter v Canada (Attorney General)* [2012] BCSC 886.

[36] *Carter v Canada (Attorney General)* [2013] BCCA 435; *Rodriguez v British Columbia (Attorney General)* [1993] 3 SCR 519. The issue of *stare decisis* is discussed by Smith J in *Carter v Canada (Attorney General)* [2012] BCSC 886, [898–910].

[37] *Carter v Canada (Attorney General)* [2015] 1 SCR 331.

[38] At trial, Justice Smith defined 'physician-assisted dying' and 'physician-assisted death' as 'generic terms that encompass physician-assisted suicide and voluntary euthanasia that is performed by a medical practitioner or a person acting under the direction of a medical practitioner': [2012] BCSC 886 [39]. She defined 'physician-assisted suicide' as 'the act of intentionally killing oneself with the assistance of a medical practitioner, or person acting under the direction of a medical practitioner, who provides the knowledge, means, or both': [2012] BCSC

overly broad.[39] The limit on s 7 rights was not saved by s 1 as the prohibitions did not minimally impair the right.[40] Therefore, the prohibitions were void:

> insofar as they prohibit physician-assisted death for 'a competent adult person who (1) clearly consents to the termination of life; and (2) has a grievous and irremediable medical condition (including an illness, disease or disability that causes enduring suffering that it intolerable to the individual in the circumstances of his or her condition'. 'Irremediable', [they added] …, does not require the patient to undertake treatments that are not acceptable to the individual.[41]

The Supreme Court made no comment on whether health care institutions could decline to provide physician-assisted dying. The court commented on, but did not resolve the issue of conscientiously objecting providers:

> In our view, nothing in the declaration of invalidity which we propose to issue would compel physicians to provide assistance in dying. The declaration simply renders the criminal prohibition invalid. What follows is in the hands of the physicians' colleges, Parliament, and the provincial legislatures. However, we note — as did Beetz J. in addressing the topic of physician participation in abortion in *Morgentaler* — that a physician's decision to participate in assisted dying is a matter of conscience and, in some cases, of religious belief (pp. 95–96). In making this observation, we do not wish to pre-empt the legislative and regulatory response to this judgment. Rather, we underline that the *Charter* rights of patients and physicians will need to be reconciled.[42]

The Supreme Court suspended their declaration of invalidity for 12 months (to February 2016) to give the government time to craft new legislation should they wish to do so.[43] There was a federal election after the *Carter* decision was released and subsequently a change in government. When the new Liberal government took office in November 2016, they asked for an extension on the suspension of the declaration of invalidity and were given four months (to 6 June 2016).[44] The Supreme Court also made provisions for individuals to be able to access physician-assisted dying through the courts during the period of the extension. These cases

886 [37]. She defined 'euthanasia' as 'the intentional termination of the life of a person, by another person, in order to relieve the first person's suffering': [2012] BCSC 886 [38].

[39] One principle of fundamental justice under s 7 is overbreadth: 'restrictions on life, liberty, and security of the person must not be more broadly framed than necessary to achieve the legislative purpose': *Carter v Canada (Attorney General)* [2012] BCSC 886 [1339].

[40] Section 1 of the *Charter* is a limitation clause as it subjects the rights and freedoms set out in the *Charter* to 'reasonable limits prescribed by law', that can be 'demonstrably justified in a free and democratic society'. The test for s 1 test includes a proportionality analysis, which asks whether the infringement of the right is minimally impairing of it. As noted by Justice Smith in *Carter v Canada (Attorney General)* [2012] BCSC 886 [1232]: 'The question, then, is whether there is an alternative means for the legislature to achieve its objective in a real and substantial way that less seriously infringes the Charter rights of Gloria Taylor and others in her situation.'

[41] *Carter v Canada (Attorney General)* [2015] 1 SCR 331 [127].

[42] Ibid [132].

[43] The government was under no obligation to legislate. It could simply have left the regulation of MAiD consistent with the declaration in *Carter* to the provinces and territories as a matter of health (which is under provincial and territorial jurisdiction). Indeed, there is precedent for this approach as the federal government has never passed legislation to replace the restrictions on access to abortion struck down by the Supreme Court of Canada in *R v Morgentaler* [1988] 1 SCR 30. Abortion is currently regulated by the provinces and territories as any other health service.

[44] 'Supreme Court Gives Federal Government 4-Month Extension to Pass Assisted Dying Law', *CBC News* (online), 15 January 2016 <www.cbc.ca/news/politics/assisted-dying-supreme-court-federal-1.3406009>.

followed the *Carter* criteria and there were 17 reported cases of people accessing physician-assisted dying in that way.[45]

The Supreme Court's decision ultimately took effect 6 June 2016, and, until the new federal legislation was passed (see below), the *Criminal Code* no longer prohibited physician-assisted dying where the *Carter* criteria were met.

Before moving on to the final development in this area, it is worth returning briefly to the trial decision in *Carter*. In her decision, Justice Lynn Smith made a number of important findings of fact (these are important as they were settled at trial and, as is most commonly the case, not unsettled by the Supreme Court of Canada). It is important to repeat them here, as they are the factual foundation for the current Canadian legal framework for medical assistance in dying.

On palliative care, Justice Smith found:

> Adequate palliative care can reduce requests for euthanasia or lead to their retraction.[46]
>
> However, despite the best possible palliative care, some patients suffer pain that cannot be alleviated …. As well, symptoms can cause suffering other than pain (such as nausea, vomiting, and shortness of breath) that cannot be alleviated even by the best palliative care.[47]
>
> Further, high quality palliative care is far from universally available in Canada.[48]

On ethics, she found:

> The preponderance of the evidence from ethicists is that there is no ethical distinction between physician-assisted death and other end-of-life practices whose outcome is highly likely to be death.[49]

On the slippery-slope arguments, she found:

> [T]he research does not clearly show either a negative or positive impact in permissive jurisdictions on the availability of palliative care or the physician-patient relationship.[50]
>
> No evidence of inordinate impact on vulnerable populations ....[51]
>
> Risks (eg, re: ability to make well-informed decisions, freedom from coercion or undue influence, physicians' ability to assess patients' capacity and voluntariness) exist, but they can be largely avoided through carefully-designed, well-monitored safeguards.[52]
>
> A system with properly designed and administered safeguards could, with a very high degree of certainty, prevent vulnerable persons from being induced to commit suicide while

[45] See Jocelyn Downie, 'Court Cases, Judicial Authorizations', *End-of-Life Law and Policy in Canada* (Health Law Institute, Dalhousie University) <eol.law.dal.ca/?page_id=242>.
[46] *Carter v Canada (Attorney General)* [2012] BCSC 886 [189].
[47] Ibid [190].
[48] Ibid [192].
[49] Ibid [335].
[50] Ibid [9].
[51] Ibid.
[52] Ibid [10].

> permitting exceptions for competent, fully informed persons acting voluntarily to receive physician-assisted death.[53]

3 *Federal Legislation*

As federal, provincial and territorial governments contemplated how to respond to the *Carter* decision, three groups were tasked by various levels of government with studying the question of how best to regulate assisted dying: a Federal Expert Panel on Options for a Legislative Response to *Carter*, appointed by then Prime Minister Stephen Harper; a Provincial–Territorial Expert Advisory Group on Physician-Assisted Dying; and a Special Joint Committee [of the federal House and Senate] on Physician-Assisted Dying. They all issued reports (the latter two with recommendations).[54] The Provincial–Territorial Expert Advisory Group recommended that governments: not have narrower eligibility criteria than those set out in *Carter*; permit access to MAiD for mature minors, individuals whose sole underlying condition is a mental illness, and those whose requests were made in advance of loss of capacity; and establish a duty to transfer care from conscientiously objecting providers.[55] The Special Joint Committee issued similar recommendations varying only in recommending a two-year delay in the coming into force of the permissive elements regarding mature minors.[56]

Ultimately the federal government introduced Bill C-14 in April 2016.[57] Most notably, the government adopted narrower eligibility criteria than those set out in *Carter* as the Bill did not permit access to MAiD for mature minors and requests made in advance of loss of capacity (at least not yet); and did not establish a duty to transfer care (although, it must be noted, that lies outside their jurisdiction).[58] A furious federal parliamentary debate ensued.[59] Attempts were made through the House of Commons (in Committee and on the floor) to amend the Bill to be less restrictive.[60] They failed.[61] The Senate sent an amended (less restrictive) Bill back to the

---

[53] Ibid [1367].

[54] External Panel on Options for a Legislative Response to *Carter v Canada*, *Consultations on Physician-Assisted Dying: Summary of Results and Key Findings: Final Report* (Government of Canada, 2015) <www.justice.gc.ca/eng/rp-pr/other-autre/pad-amm/index.html>; Provincial-Territorial Expert Advisory Group on Physician-Assisted Dying, *Final Report* (Ontario Department of Health, 2015) <www.health.gov.on.ca/en/news/bulletin/2015/docs/eagreport_20151214_en.pdf?>; Special Joint Committee on Physician-Assisted Dying, Parliament of Canada, *Medical Assistance in Dying: A Patient-Centred Approach* (2016).

[55] Provincial-Territorial Expert Advisory Group on Physician-Assisted Dying, above n 54, 5–11.

[56] Special Joint Committee on Physician-Assisted Dying, above n 54, 21.

[57] Bill C-41, An Act to Amend the Criminal Code and to Make Related Amendments to Other Acts (Medical Assistance in Dying), 42nd Parl, 1st Sess, 2016 (first reading as passed by the House of Commons, 14 April 2016) <eol.law.dal.ca/wp-content/uploads/2016/05/C-14_1.pdf>.

[58] Under the Canadian Constitution, provinces and territories have jurisdiction over the administration of health, and regulation of healthcare providers falls within that jurisdiction: *Canada Act 1982* (UK) c 1, Sch B '*Constitution Act 1982'.*

[59] See eg, Canada, *Parliamentary Debates*, House of Commons, 42nd Parl, 1st Sess, Vol 148, No 45 (22 April 2016), 1005 (Jody Wilson-Raybould); 1035 (Michael Cooper), 1255 (Murray Rankin); see also Vol 148, No 57 (17 May 2016), No 60 (20 May 2016), No 61 (30 May 2016); Canada, *Parliamentary Debates*, Senate, 42nd Parl, 1st Sess, Vol 150, No 42 (2 June 2016) 1450 (George Baker), 1650 (Serge Joyal); see also Vol 150, No 41 (1 June 2016), No 45 (8 June 2016), No 47 (10 June 2016), No 49 (14 June 2016).

[60] House of Commons, Standing Committee on Justice and Human Rights, Bill C-14 An Act to Amend the Criminal Code and to Make Related Amendments to Other Acts (Medical Assistance in Dying) (31 May 2016) <www.parl.gc.ca/Committees/en/JUST/StudyActivity?studyActivityId=8874111>.

[61] Ibid.

House,[62] but the House rejected the more permissive amendments.[63] Finally the Senate conceded and passed the House's restrictive Bill.[64]

After its tumultuous ride through the House and Senate, *An Act to Amend the Criminal Code and to Make Related Amendments to Other Acts (Medical Assistance in Dying)*[65] was passed and immediately came into force on 17 June 2016. It is worth repeating that the law as passed is narrower than that recommended by the Royal Society of Canada Expert Panel on End of Life Decision-Making,[66] the Provincial–Territorial Expert Advisory Group, the Special Joint Committee, and the amendments sought by the Senate.

The key elements of the federal legislation are as follows:

- Medical assistance in dying is the umbrella term that includes both voluntary euthanasia and assisted suicide.[67] It is defined in the legislation as:
  > (a) the admininstering by a medical practitioner or nurse practitioner of a substance to a person, at their request, that causes their death; or (b) the prescribing or providing by a medical practitioner or nurse practitioner of a substance to a person, at their request, so that they may self-administer the substance and in doing so cause their own death.[68]
- Recognising the scarcity of physicians in Canada (especially in rural and remote communities) as well as the competencies and accountability of nurse practitioners, both physicians and nurse practitioners are allowed to provide MAiD.[69]
- Recognising that health care is provided in teams and few physicians or nurse practitioners would be acting completely alone and also recognising that some patients would want their loved ones to be the ones to help them at the end, any person is permitted to assist the providers. So pharmacists, nurses, and friends and family members are all permitted to assist.[70]
- Recognising that patients may well ask a whole range of health care providers about assisted dying and that these providers could be very appropriate sources of information, information can be provided by social workers, psychologists, psychiatrists, therapists, medical practitioners, nurse practitioners, and other health care professionals.[71]

According to s 241.2(1) of the new legislation, only those who meet the following criteria can have access to medical assistance in dying. Patients must:

---

[62] Bill C-41, An Act to Amend the Criminal Code and to Make Related Amendments to Other Acts (Medical Assistance in Dying), 42nd Parl, 1st Sess, 2016 (third reading as passed by the Senate 15 June 2016) <eol.law.dal.ca/wp-content/uploads/2016/07/Senate-amendments-sent-to-House.pdf>.

[63] Canada, *Parliamentary Debates*, House of Commons, 42nd Parl, 1st Sess, Vol 148, No 74 (16 June 2016) 1035 <www.parl.gc.ca/HousePublications/Publication.aspx?Pub=Hansard&Doc=74&Parl=42&Ses=1&Language=E&Mode=1>.

[64] Canada, *Parliamentary Debates*, Senate, 42nd Parl, 1st Sess, Vol 150, No 52 (17 June 2016) 910 <sencanada.ca/en/Content/Sen/chamber/421/debates/052db_2016-06-17-e#16>.

[65] SC 2016, c 3 ('*Medical Assistance in Dying Act*').

[66] Schuklenk et al, above n 12, 6–7.

[67] *Medical Assistance in Dying Act*, SC 2016, c 3, s 241.1.

[68] Ibid.

[69] Ibid s 227.

[70] Ibid s 241.

[71] Ibid.

- be eligible for health services funded by government in Canada (or would be, but for a minimum period of residence or waiting period);
- be at least 18 years old;
- be capable of making decisions with respect to their health;
- have made a voluntary request;
- have given informed consent to receive medical assistance in dying after having been informed of means available to relieve suffering, including palliative care; and
- have a grievous and irremediable medical condition.

This is further explained in s 241.2(2) as:

- they have a serious and incurable illness, disease or disability;
- they are in an advanced state of irreversible decline in capability;
- that illness, disease or disability or that state of decline causes them enduring physical or psychological suffering that is intolerable to them and that cannot be relieved under conditions that they consider acceptable; and
- their natural death has become reasonably foreseeable, taking into account all of their medical circumstances, without a prognosis necessarily having been made as to the specific length of time that they have remaining.

The following procedural safeguards must also be met:

- A medical practitioner or nurse practitioner must be of the opinion that the person meets all of the eligibility criteria;[72]
- A request must be made in writing, signed and dated after the patient has been informed of their grievous and irremediable condition;[73]
- There must be two independent witnesses to the request;[74]
- A second independent medical practitioner or nurse practitioner must confirm that the eligibility criteria have been met;[75]
- There must be a 10-day waiting period between the day the request was signed and the day MAiD is provided (unless death or loss of capacity is imminent);[76] and
- The patient must be given the opportunity to withdraw consent and, indeed, must explicitly reconfirm the consent required immediately before MAiD is provided.[77]

Freedom of conscience was, of course, the subject of enormous debate in relation to the legislation. Some health care providers want to be able to opt out of MAiD entirely (including not providing information, transfers of care, or referrals to willing providers) and some institutions want to be able to opt out of allowing MAiD within their walls.[78] Patients and patient advocates in turn worry about lack of access if opting out is allowed. The legislation

[72] Ibid s 241.2(3)(a).
[73] Ibid s 241.2(3)(b).
[74] Ibid s 241.2(3)(c).
[75] Ibid s 241.2(3)(e).
[76] Ibid s 241.2(3)(g).
[77] Ibid s 241.2(3)(h).
[78] A transfer of care and a referral have the same result (a patient gains access to a provider who is willing to assess whether she meets the criteria for MAiD and, if so, to provide MAiD). However, some providers believe that a referral implies that the provider approves of MAiD while a transfer of care does not and therefore involves no (or less) moral compromise on the part of the provider. See Provincial-Territorial Expert Advisory Group on Physician-Assisted Dying, above n 54, 45.

itself does not resolve this conflict as it says only the following: 'nothing in this Act affects the guarantee of freedom of conscience and religion';[79] and 'nothing in this section compels an individual to provide or assist in providing medical assistance in dying'.[80]

The legislation also establishes the foundation for retrospective oversight as providers have a duty to file information on every written request for MAiD[81] (once the conditions for coming into force are met), there are penalties for non-compliance with the legislation,[82] and there will be a Parliamentary review of the provisions of Act and the state of palliative care in Canada, scheduled to start on 18 June 2021.[83]

The legislation also imposes some obligations on the Minister of Health as she must make regulations regarding provision, collection, analysis, and reporting of data,[84] and, after consultation with provinces and territories, she must establish guidelines on information to be included on death certificates.[85] The legislation also provides that the Ministers of Justice and Health must initiate one or more independent reviews of issues relating to mature minors, advance requests, and requests where mental illness is the sole underlying condition.[86] In addition, no more than two years after the initiation of the reviews (ie, by 14 December 2018), they must present one or more reports on the reviews to both Houses of Parliament.[87]

Finally, while not in the legislation itself, the federal government also promised to increase support for palliative and end of life care, and to work with the provinces and territories to establish a pan-Canadian system for access, a) to facilitate transfers of care; b) to protect the conscience of objecting providers; and c) to protect the privacy of willing providers.[88]

Despite the passage of the federal legislation, there remain some challenges: first, implementing the legislation; and, second, dealing with several outstanding legal issues. The implementation challenges include: gathering data (eg, standardizing what goes on medical certificates of death[89] and determining what information needs to be reported and to whom[90]);

---

[79] *Medical Assistance in Dying Act,* SC 2016, c3, Preamble.
[80] Ibid s 241.2(9).
[81] Ibid s 241.31(2).
[82] Ibid ss 241.3-4ff.
[83] Ibid s 10.
[84] Ibid s 241.31(3).
[85] Ibid s 241.31(3.1).
[86] Ibid s 9.1(1). These reviews will be conducted by an independent panel appointed by the Council of Canadian Academies (the umbrella organisation for the Royal Society of Canada, the Canadian Academy of Engineering, and the Canadian Academy of Health Sciences). Canadian Council of Academics, 'Council of Canadian Academies to Undertake Studies Related to Medical Assistance in Dying' (What's New, 14 December 2016) <www.scienceadvice.ca/en/news.aspx?id=186>.
[87] *Medical Assistance in Dying Act*, SC 2016, c 3, s 91(2).
[88] Department of Justice Canada, 'Government of Canada Moves Motion to Amend Bill C-14 – Medical Assistance in Dying' (News Release, 16 June 2016) https://www.canada.ca/en/department-justice/news/2016/06/government-of-canada-moves-motion-to-amend-bill-c-14-medical-assistance-in-dying.html>.
[89] The Canadian government now has non-binding guidelines for death certificates with respect to MAiD that recommend recording both the immediate cause of death (eg toxicity of drugs administered for MAiD) and the underlying cause of death (eg 'the disease or condition that initiated the train of morbid events leading to the medically-assisted death'); see 'Guidelines for Death Certificates' (online): <www.canada.ca/en/health-canada/services/publications/health-system-services/guidelines-death-certificates.html>. However, inconsistencies in practice across Canada remain.
[90] Draft regulations are due this fall. See Government of Canada, 'Interium update on medical assistencing in dying in Canada June 17 to December 31, 2016' (31 May 2017), online: <www.canada.ca/en/health-canada/services/publications/health-system-services/medical-assistance-dying-interim-report-dec-2016.html>.

establishing MAiD protocols (eg, what drugs, dosages, etc.); ensuring that the most appropriate drugs for MAiD are available in Canada;[91] determining who pays for the drugs and the services of the health care providers; managing the promised system for transfers of care in the face of conscientious objections; and educating health care professionals, lawyers, and the public. The key outstanding legal issues to be resolved are conscientious objection and the eligibility criteria.

Federal, provincial and territorial governments, and regulatory bodies will be challenged to clarify whether health care providers have a legal obligation to inform patients about MAiD, transfer care to a provider willing to conduct an assessment and provide assistance to a patient if eligible, and/or arrange an effective referral to a willing provider. The battlegrounds for these issues will be health professional regulatory bodies revising their guidelines and provincial and territorial governments deciding whether to introduce legislation to create statutory obligations for providers.[92] Litigation has already started as the Ontario College of Physicians and Surgeons Guidelines establishing a duty of effective referral are being challenged by a consortium of religious groups.[93] Federal, provincial and territorial governments will also be challenged to clarify whether publicly funded health care institutions have a legal duty to transfer patients, allow the provision of MAiD within their walls, or provide MAiD. Provincial and territorial governments will have to decide whether to insist upon provision by institutions (eg, through legislation,[94] their memoranda of understanding, or funding agreements). Patients may in turn litigate if it turns out that access is being severely hampered by claims of freedom of conscience by institutions. It seems increasingly likely that this will be an ongoing and growing source of friction as a significant number of institutions appear to be opting out without facing any consequences from the provinces or territories.[95]

The federal Parliament must also deal with outstanding issues concerning the eligibility criteria. As noted earlier, Parliament decided to exclude but undertake further study on issues

---

[91] Eg, the preferred drug for self-admininstered MAiD (oral secobarbital) is not available in Canada. See, Sheryl Ubelacker, 'Drugs for Physician-Assisted Death: What Will they Cost and Who Will Pay?' *Canadian Press* (online), 13 June 2016 <www.theglobeandmail.com/news/national/drugs-for-physician-assisted-death-what-will-they-cost-and-who-will-pay/article30414929/>; Health Canada, *Drug Product Database* <www.hc-sc.gc.ca/dhp-mps/prodpharma/databasdon/index-eng.php>.

[92] See eg, College of Physicians and Surgeons Alberta, *Standard of Practice: Medical Assistance in Dying* (June 2016) <www.cpsa.ca/standardspractice/medical-assistance-dying/>; College of Physicians and Surgeons Nova Scotia, *Professional Standard Regarding Medical Assistance in Dying* (2016) <www.cpsns.ns.ca/Standards-Guidelines/Medical-Assistance-in-Dying>.

[93] See Alex McKeen, 'Doctors challenge Ontario policy on assisted-death referrals', *Toronto Star* (online), 13 June 2017 <https://www.thestar.com/news/gta/2017/06/13/group-of-doctors-challenge-policy-requiring-referral-to-services-that-clash-with-morals.html>. The case was heard 13-15 June 2017. A decision has not yet been released. Court documents, including the notice of claim by the Christian Medical and Dental Society of Canada (CMDS), the Canadian Federation of Catholic Physicians' Societies, Canadian Physicians for Life, and intervor documents submitted by Dying with Dignity are available online: <www.dyingwithdignity.ca/cpso_court_challenge>.

[94] For contrasting approaches, see *An Act Respecting End-of-Life Care*, RSQ c S-32.0001, ss 7, 13, 17; Medical Assistance in Dying Statute Law Amendment Act, 2017, SO 2017 C7; and Bill 41, Patients First Act, 2016, SO 2016 C30;; and Bill 41, Patients First Act, 2016, SO 2016 C30; *Local Health System Integration Act*, 2006, SO 2006, c 4, s 20.2(4); *Public Hospitals Act*, RSO 1990, c P40, s 8.1(2).

[95] See eg, Sharon Kirkey, 'Ontario Hospitals Allowed to Opt Out of Assisted Dying, Raising Conscientious Accommodation Concerns', *National Post* (online), 10 June 2016 <news.nationalpost.com/news/ontario-hospitals-allowed-to-opt-out-of-assisted-dying-raising-conscientious-accommodation-concerns>; Tom Blackwell, 'BC Man Faced Excruciating Transfer After Catholic Hospital Refused Assisted-Death Request', *Globe and Mail* (online), 27 September 2016 <news.nationalpost.com/news/canada/b-c-man-faced-excruciating-transfer-after-catholic-hospital-refused-assisted-death-request>. Dying with Dignity Canada has launched a campaign to expose barriers that may prevent Canadians from accessing MAiD; see 'The Shine a Light Campaign' (online): <www.dyingwithdignity.ca/shinealight>.

of mature minors and requests made in advance of loss of capacity.[96] As required by the legislation, between now and December 2018, there are independent reviews of the questions of mature minors, advance requests, and mental illness as the sole underlying condition. Advocates on all sides of these issues will ultimately attempt to persuade Parliament to ensure that the legislation reflects their positions on these issues.

The Parliament also decided to exclude, with no promise of further study, those whose conditions are 'incurable', who are in an 'advanced state of irreversible decline in capability', and whose 'natural death' has become 'reasonably foreseeable'. There will be two kinds of challenges to these criteria. First, there will be cases questioning what the key terms or phrases mean. For example, in *AB v Canada (Attorney General)*, a woman sought clarification of the meaning of 'reasonably foreseeable'.[97] Second, there will also be *Charter* challenges to the exclusion criteria. In particular, there will be challenges to the requirements that the patient's condition must be incurable, the patient must be in an advanced state of irreversible decline in capability, and their natural death must have become reasonably foreseeable. Recall that the Supreme Court of Canada, in one voice, declared the *Criminal Code* prohibitions on MAiD void because they violated the *Charter* insofar as they prohibited physician-assisted death for:

> a competent adult person who (1) clearly consents to the termination of life; and (2) has a grievous and irremediable medical condition (including an illness, disease or disability that causes enduring suffering that is intolerable to the individual in the circumstances of his or her condition. 'Irremediable', [they added] …, does not require the patient to undertake treatments that are not acceptable to the individual.[98]

Contrast this with the federal legislation. There is no reference to 'incurable' in the *Carter case* declaration. There is no reference to 'advanced state of irreversible decline in capability' in the *Carter* declaration. There is no reference to 'reasonably foreseeable' in the *Carter* declaration. In sum, the following hypothetical people would be allowed access to MAiD through the *Carter* declaration and, as is already being argued, the *Charter* would require them to have access, but they would be denied access by the legislation: someone who has had three unsuccessful rounds of chemo and is refusing a fourth (if her disease is not considered incurable);[99] someone who had a traumatic injury five years ago (as there is no decline in

---

[96] Individuals whose sole underlying condition is mental illness are not included in this list of excluded groups because I am persuaded that, contrary to the assumption of some, the legislation does not exclude them. See Jocelyn Downie and Justine Dembo, 'Medical Assistance in Dying and Mental Illness under the New Canadian Law' (2016) 9 *Journal of Ethics in Mental Health* VI(iv) <http://www.jemh.ca/issues/v9/documents/JEMH_Open-Volume_Benchmark_Medical_Assistance_in_Dying_and_Mental_Illness_Under_the_New_Canadian_Law-Nov2016.pdf>, for an argument in support of the position that individuals whose sole condition is a mental illness are not excluded from accessing MAiD under the legislation (as long as they meet the s 241.2(2) criteria). There is no published rebuttal of this argument.

[97] 2017 ONSC 3759.

[98] C*arter v Canada (Attorney General)* [2015] 1 SCR 331 [127].

[99] It should be noted here that the Minister of Health and Department of Justice Senior Counsel both stated when appearing before the Senate that 'incurable' should be interpreted as including the phrase 'by any means acceptable to the patient': Canada, *Parliamentary Debates*, Senate, 42nd Parl, 1st Sess, Vol 150, No 41 (1 June 2016) 1650 (Dr Jane Philpott) <www.parl.gc.ca/Content/Sen/Chamber/421/Debates/041db_2016-06-01-e.htm> and Evidence to Senate Standing Senate Committee on Legal and Constitutional Affairs, Parliament of Canada (6 June 2016) (Chair: Bob Runciman) <www.parl.gc.ca/content/sen/committee/421/LCJC/52666-E.HTM>. Their position is grounded in the well-established right to refuse treatment. However, this phrase is not explicitly included the legislation in conjunction with the 'incurable' criterion. The phrase is explicitly included in the legislation in conjunction with the alleviation of suffering criterion ('… suffering that is intolerable to them and that cannot be relieved under conditions that they consider acceptable'). The logic of the defence for not explicitly

capability); someone with Chronic Obstructive Pulmonary Disease (as death is too uncertain); someone with Parkinson's Disease, ALS, multiple sclerosis, or Huntington's disease (when death is too far off); and even someone in Kay Carter's situation, who is only 60 instead of 89 (as death is too far off).

One *Charter* challenge to the new legislation was launched in *Lamb v Canada (Attorney General)*[100]—by the same legal team that argued and won the *Carter* case. Julia Lamb is a 25-year-old woman with spinal muscular atrophy. This is a degenerative muscle-wasting condition that is slowly depriving Julia of a wide range of muscular functions and, consequently causing considering pain and suffering. She does not wish to access MAiD now, but can anticipate a time at which she would find her suffering to be enduring and intolerable; however, her physicians would not be able to predict with sufficient certainty that her death is reasonably foreseeable. She is arguing that the new federal legislation violates her s 7 and s 15 rights under the *Charter*. This case will focus on Julia and other people who, the Supreme Court of Canada said in *Carter*, must not be prevented from having access to MAiD, but who do not have access under the federal legislation.

A second *Charter* challenge, *Jean Truchon and Nicole Gladu v Attorney General (Canada) and Attorney General (Quebec)*,[101] has been launched arguing that both the federal and Quebec laws are too restrictive. Jean Truchon has cerebral palsy, and Nicole Gladu, has post polio syndrome.

Governments and practitioners are also going to have to wrestle with the on-the-ground consequences of some of the provisions in the federal legislation. These include (but are not limited to):

- A patient is in agony from spinal stenosis but refuses pain medication at dosages sufficient to control the pain, in order to be competent at the time of the request and at the time of provision of MAiD.[102]
- A patient has advanced bone cancer pain that can be managed by such deep sedation that she is in a semi-conscious state. She has her sedation lightened (and is thereby returned to a state of experiencing severe pain) so that she will regain capacity at the time of provision of MAiD.[103]
- A patient has completed all of the requirements (including the 10-day waiting period) on a Friday afternoon, her MAiD provider is not available until Monday, she loses capacity on the weekend, and so becomes ineligible for MAiD and remains stranded in a state of enduring and intolerable suffering until she dies from her underlying condition months later.[104]

---

including 'by any means acceptable to the patient' for 'incurable' would also apply to the alleviation of suffering (in which case 'under conditions that they consider acceptable' is redundant in s 241.2(2)(c)). Since the principles of statutory interpretation require courts to read legislation in such a way as to avoid redundancy, it might be argued that a court would not be permitted to read the limit into s 241.2(2)(a).

[100] *Lamb v Canada (Attorney General)* (27 June 2016), Vancouver, SCBC, S-165851 (notice of civil claim).

[101] *Jean Truchon and Nicole Gladu v Attorney General (Canada) and Attorney General (Quebec)* (13 June 2017), Montreal, CQ (Civ Div) (notice of Application to Proceed for Declaratory Relief) filed 13 June 2017, online: <www.menardmartinavocats.com/documents/file/demande-introductive-da%C2%80%C2%99instance-en-jugement-d%C3%83%C2%89claratoire.pdf>.

[102] *Medical Assistance in Dying Act*, SC 2016, c 3, ss 241.2(1)(b) and (3)(h).

[103] Ibid s 241.2(3)(h).

[104] Ibid ss 241.2(1)(b) and (3)(h).

- A patient was diagnosed with Alzheimer's disease three years ago and made an advance request for MAiD and, if that wasn't available, an advance directive refusing all oral hydration and nutrition once she reached stage seven of the disease. She is now stage seven, incapable and therefore ineligible for MAiD, and so the institution stops giving her food and liquids and waits while she dies of dehydration.[105]
- A patient has multiple sclerosis but, although experiencing enduring and intolerable suffering, her death is not reasonably foreseeable. She decides to stop eating and reduce liquids in order to get close enough to death to qualify for MAiD while still retaining capacity. It takes 50 days without food and four days without liquid before her physician determines that she meets the eligibility criteria.[106]
- A patient has Huntington's disease and while experiencing enduring and intolerable suffering, her death is not likely for a number of years. She asks her physician to provide her with deep and continuous sedation and she refuses artificial hydration and nutrition. She dies 14 days later.[107]

As the public continues to learn of these situations that result from the way in which the legislation has been drafted, there is likely to be increased pressure on governments to revisit the provisions that create such situations and on providers to find ways to avoid the consequences while respecting the provisions.[108]

Finally, the inconsistencies between the Quebec legislation, the *Carter* decision, and the federal legislation will need to be addressed. For example, the Quebec legislation requires that patients be 'at the end of life', which is a much narrower criterion than *Carter*'s criterion of 'grievous and irremediable condition'. The federal legislation also requires a 10-day waiting period between the request and the provision of MAiD while the Quebec legislation does not.[109]

III LESSONS FOR AUSTRALIA

What then can Australia learn from the Canadian experience with decriminalising medical assistance in dying? First, ***be patient and adaptable***. In Canada, advocates of law reform concurrently worked on litigation, legislation, and prosecutorial charging guidelines.[110] They wanted to be able to go through any crack in any window of opportunity that opened. If one

[105] Ibid.
[106] Ibid ss 241.2(1)(b) and (2)(d).
[107] Ibid.
[108] Eg, could impending provision of palliative sedation be taken to mean that loss of capacity is imminent and therefore a shortening of the 10-day waiting period is permissible? Could all patients with diagnoses involving future dementia who want MAiD be advised to explicitly refuse oral feeding and liquids through advance directives?
[109] Rather, the Quebec legislation requires at s 29(1)(c) 'verifying the persistence of suffering and that the wish to obtain medical aid in dying remains unchanged, by talking with the patient at reasonably spaced intervals given the progress of the patient's condition'. The Deputy Minister of Health of Quebec instructed health care institutions to comply with the 10 day requirement. However, the Executive Director of the Conseil pour la Protection des Malades has filed a complaint with the Quebec Ombudsperson about this instruction. See Aaron Derfel, 'Dying with Dignity: Quebec Paves Way, but Critics Point to Problems' *Montreal Gazette* (online), 21 October 2016 <montrealgazette.com/news/local-news/medial-aid-in-dying-quebecs-experience>; Isabelle Paré, 'Six Ordres Professionnels Demandent un Appel sur L'aide à Mourir', *Le Devoir* (online), 6 December 2016 <www.ledevoir.com/societe/sante/486444/aide-a-mourir-six-ordres-professionnels-demandent-un-renvoi-en-cour-d-appel>.
[110] See eg, Jocelyn Downie and Simone Bern, 'Rodriguez Redux' (2008) 16 *Health Law Journal* 27, 44–54; Jocelyn Downie and Ben White, 'Prosecutorial Discretion in Assisted Dying in Canada: A Proposal for Charging Guidelines' (2012) 6(2) *McGill Journal of Law and Health* 113.

waits for the window to open before developing the arguments, drafting legislation, etc, then by the time the work is done, the window will have closed again. So the advocates prepared for all eventualities, were patient, and then took the litigation path when it opened and the legislation path when that followed.

Second, ***prepare the foundations for law reform initiatives***. It was essential to the plaintiffs' success in the *Carter* case that they were able to access robust empirical evidence on the experience with assisted dying around the world[111] as well as well-developed legal and ethical arguments on why assisted dying should be decriminalised.[112] Very clear strong public support for both the *Carter* decision and assisted dying were also important for the legislative process.[113]

Third, ***consult and engage broadly***. As noted earlier in this paper, this principle was embraced by the Quebec Select Committee on Dying with Dignity and is in no small part a reason for the widespread support for their medical aid in dying legislation. It was also respected (albeit on an abridged timeline) by the Provincial-Territorial Expert Advisory Group on Physician-Assisted Dying and the Special Joint Committee on Physician-Assisted Dying and, again, probably played a role in the strong positive response their reports received from the majority of Canadians. However, the perils of not consulting were also manifest in the Canadian process. For example, the Canadian government did not consult with the regulators of physicians, but rather just consulted with the Canadian Medical Association.[114] If they had consulted with those who are tasked with regulating physicians, they would have been advised not to use the criterion that 'natural death' be 'reasonably foreseeable'[115] and, had they followed that advice,

[111] See eg, the impact of the expert evidence provided by Johannes J M van Delden, Luc Deliens, and Linda Ganzini in the trial decision in *Carter v Canada (Attorney General)* [2012] BCSC 886.

[112] See eg, Jocelyn Downie, *Dying Justice: A Case for Decriminalizing Euthanasia and Assisted Suicide in Canada* (University of Toronto Press, 2004); Downie and Bern, above n 110. See also the impact of the expert evidence provided by Wayne Sumner, Margaret Pabst Battin, and Marcia Angell in the trial decision in *Carter v Canada (Attorney General)* [2012] BCSC 886.

[113] See eg, results of Ipsos Poll: Ipsos Public Affairs, *Dying with Dignity Canada*, (February 2016), <d3n8a8pro7vhmx.cloudfront.net/dwdcanada/pages/480/attachments/original/1455165944/DWDC-Ipsos_-_Feb_2016_poll_-_final.pdf?1455165944>.

[114] Senate Standing Senate Committee on Legal and Constitutional Affairs, Parliament of Canada, *Proceedings*, Issue No 9, Evidence, 42nd Parl, 1st Sess (10 May 2016) <www.parl.gc.ca/Content/SEN/Committee/421/lcjc/09ev-52575-e.htm?Language=E&Parl=42&Ses=1&comm_id=11>. Senator Joyal asked the Federation of Medical Regulatory Authorities of Canada (FMRAC) whether or not they had been consulted on Bill C-14 and FMRAC said they had not. Likewise the same question directed to the College of Physicians and Surgeons of Ontario revealed they had not been consulted. FMRAC is mandated 'to advance medical regulation on behalf of the public through collaboration, common standards and best practices': see FMRAC, *Mission* <fmrac.ca/about-us/>. The Canadian Medical Association (CMA) is 'a national association of physicians that advocates on behalf of its members and the public for access to high-quality health care' and 'provides leadership and guidance to physicians': see CMA, *History, Mission, Vision and Values* <www.cma.ca/En/Pages/history-mission-vision.aspx>. The CMA had historically been opposed to MAiD and so, despite the fact that the official position had become neutral on decriminalisation (see CMA, *CMA Policy: Euthanasia and Assisted Death: Update 2014* <www.cma.ca/En/Pages/end-of-life.aspx> 3), it came as no surprise that they were actively lobbying in support of a restrictive approach to the eligibility criteria.

[115] See Evidence to Senate Standing Senate Committee on Legal and Constitutional Affairs, Parliament of Canada, 42nd Parl, 1st Sess, Issue No 9, 10 May 2016, 9:47, (Dr Douglas Grant) <sencanada.ca/Content/SEN/Committee/421/lcjc/pdf/09issue.pdf>, where FMRAC rejects 'reasonably foreseeable' and 'natural death'; FMRAC, 'Bill C-14, Medical Assistance in Dying: Submission to the Senate Standing Committee on Legal and Constitutional Affairs' (What's New, 10 May 2016) <fmrac.ca/federation-of-medical-regulatory-authorities-of-canada-bill-c-14-medical-assistance-in-dying/>.

they would have avoided the firestorm that greeted their draft legislation and the *Charter* challenge to the legislation that has now been commenced.[116]

It is also essential to *be respectful of heterogeneity in communities*. The loudest voice does not necessarily articulate the most widely held or only held position. A good example of this phenomenon in Canada is with respect to persons with disabilities. There was a very vocal group representing persons with disabilities and arguing for as restrictive an approach as possible.[117] Yet there are many other people with disabilities who believe that the most restrictive approach is patronising, paternalistic, and infantilising.[118]

Remember also to *consult with indigenous communities*. In Canada, indigenous communities lack access to health services, are confronting a higher rate of suicide than non-indigenous populations, and have a range of different cultural values and beliefs relevant to end of life decision-making.[119] In Canada, they were not adequately engaged in the conversations about decriminalisation and implementation of MAiD.[120] As a result, policy-makers and providers are now playing catch-up and trying to undo misinformation and mistrust.

Fourth, ***prepare the infrastructure for assisted dying*.** It is essential to develop a mechanism for identifying willing providers, as providers can feel at risk of stigmatisation by their colleagues and attack from opponents of assisted dying, and so may not make their willingness known. But, in order to ensure access for patients, it is essential to know who and where the willing providers are. Some physicians in Canada have been very open about being willing

---

[116] *Lamb v Canada (Attorney General)* (27 June 2016), Vancouver, SCBC, S-165851 (notice of civil claim).

[117] Vulnerable Person Standard, *Materials Related to Bill C-14* <www.vps-npv.ca/materials-related-to-bill-c14/>; Senate Standing Senate Committee on Legal and Constitutional Affairs, *Proceedings*, Issue No 9, Evidence, 42nd Parl, 1st Sess (10 May 2016) (Michael Bach) <www.parl.gc.ca/Content/SEN/Committee/421/lcjc/09ev-52575-e.htm?Language=E&Parl=42&Ses=1&comm_id=11>; Evidence to Senate Standing Committee on Justice and Human Rights, Parliament of Canada, 42nd Parl, 1st Sess, No 12, 3 May 2016, 1950 (Michael Bach); and 42nd Parl, 1st Sess, No 13 (4 May 2016) 1800 (Dianne Pothier); Dianne Pothier, Submissions to the Senate Standing Committee on Legal and Constitutional Affairs, *Consideration of Bill C-14*, 28 April 2016, <www.vps-npv.ca/s/Pothier-Senate-Committee-submissions-on-C-14.pdf>; Senate Standing Committee on Justice and Human Rights, Parliament of Canada, *Evidence*, 42nd Parl, 1st Sess, 5 May 2016, (David Baker) <sencanada.ca/en/Content/Sen/committee/421/lcjc/52552-e>.

[118] Canada, *Parliamentary Debates*, Senate, 3 June 2016, 1st Sess, 42nd Parl, Vol 150, Issue 43 (Chantal Petitclerc) 1100: <www.parl.gc.ca/Content/Sen/Chamber/421/Debates/043db_2016-06-03-e.htm>; Senate Standing Committee on Justice and Human Rights, *Evidence*, 42nd Parl, 1st Sess, No 12, (3 May 2016) 1715 (Angus Gunn); *Carter v Canada* [2015] 1 SCR 331 (Factum of the Intervenor the Alliance of People with Disabilities who are Supportive of Legal Assisted Dying Society) <www.scc-csc.ca/WebDocuments-DocumentsWeb/35591/FM130_Intervener_Alliance-of-People-with-Disabilities.pdf>.

[119] For access to health services, see Jeff Reading and Regine Halseth, *Pathways to Improving Well-Being for Indigenous Peoples: How Living Conditions Decide Health* (National Collaborating Centre for Aboriginal Health, 2013) <www.nccah-ccnsa.ca/Publications/Lists/Publications/Attachments/102/pathways_EN_web.pdf>; for suicide, see Sherry Bellamy and Cindy Hardy, *Understanding Depression in Aboriginal Communities and Families* (National Collaborating Centre for Aboriginal Health, 2015) <www.nccah-ccnsa.ca/Publications/Lists/Publications/Attachments/150/2015-10-07-RPT-MentalHealth03-Depression-BellamyHardy-EN-Web.pdf>; for cultural beliefs and values, see Elaine Anselmi, 'Physician Assisted Dying: Offering a Choice Means Making Tough Decisions', *Northern Public Affairs* (online), 22 February 2016 <www.northernpublicaffairs.ca/index/physician-assisted-dying-offering-a-choice-means-making-tough-decisions/>.

[120] There was some engagement, but no community consultation. See eg, House of Commons Special Joint Committee on Physician-Assisted Dying, Parliament of Canada, *Evidence*, 42nd Parl, 1st Sess, No 9 (1 February 2016) 1715 (Dr Carrie Bourassa); No 10 (2 February 2016) 1900 (Dr. Alika Lafontaine). Alika Lafontaine, Carrie Bourassa and Melanie MacKinnon engaged with the Federal Expert Panel.

providers.[121] Some provinces and territories have set up a central team that can be contacted by patients.[122] Access is further enhanced if some entity capable of protecting provider privacy is given the mandate and resources necessary to act as a go-between to ensure patients have access to willing providers.[123] It is also essential to develop a transfer of care system if any conscientious objection by providers and/or publicly funded health care institutions will be permitted. Many provinces and territories in Canada have set up such systems and as a result some patients can access MAiD even when their own health care providers object to it.[124]

It is also necessary to make sure the most appropriate drugs are licensed. It was only realised after the fact that secobarbital (the drug preferred by Canadian providers, for self-administered MAiD) is not available in Canada, so patients who wish to self-administer may face real barriers to doing so (for example, an oral protocol is available in Alberta but not in Nova Scotia).[125] Australian patients could find themselves in the same bind if the barriers to access to secobarbital (or pentobarbital which may be preferred in Australia) are not removed when or before MAiD is decriminalised.

It is also important to establish educational programs for health professionals, lawyers, and the public. Everyone needs to understand what the law is and what their rights and obligations are, and providers need to know how to deliver MAiD. Support systems must also have been put in place for providers as well as patients and families. Canada is playing catch-up on both of these infrastructure pieces—MAiD is legal but not everybody has the information or support they need.[126]

It is also essential to establish the infrastructure for the oversight system: for the sake of accountability, transparency and trust, all cases should be reviewed; and death certificate forms

---

[121] See eg, Elizabeth Church, 'Ellen Wiebe is the Doctor Seeking a Smoother Path to Assisted Death', *Globe and Mail* (online), 2 March 2016 <www.theglobeandmail.com/news/national/ellen-wiebe-is-the-doctor-seeking-a-smoother-path-to-assisted-death/article29006968/>; Shannon Proudfoot, 'Q&A: Stefanie Green on Helping Doctors Navigate Assisted Dying', *Maclean's* (online), 25 November 2016 <www.macleans.ca/news/canada/qa-stefanie-green-on-helping-doctors-navigate-assisted-dying/>; Sandra Martin, 'Patients Should Talk Frankly With their Doctors about Assisted Dying', *Globe and Mail* (online), 12 November 2015 <www.theglobeandmail.com/life/health-and-fitness/health/patients-should-talk-frankly-with-their-doctors-about-assisted-dying/article27234624/>.

[122] See eg, Winnipeg Regional Health Authority, *Accessing Medical Assistance in Dying* (2016) <www.wrha.mb.ca/maid/contact.html>.

[123] See eg, Alberta Health Services, *Medical Assistance in Dying Care Coordination Services* (14 July 2016) <www.albertahealthservices.ca/assets/info/hp/maid/if-hp-maid-coordination-service.pdf>; Nova Scotia Health Authority, *Medical Assistance in Dying: Frequently Asked Questions for the Public* (4 July 2016) <www.nshealth.ca/sites/nshealth.ca/files/faq_for_public_2016_07_04.pdf>.

[124] Nova Scotia Health Authority, above n 123; Alberta Health Services, *Medical Assistance in Dying: Frequently Asked Questions for Patients and Family Members* <www.albertahealthservices.ca/assets/info/pf/if-pf-maid-faqs-public.pdf>.

[125] The Health Canada Drug Product database shows no results for secobarbital, indicating its licence has lapsed. Health Canada, *Drug Product Database* <https://health-products.canada.ca/dpd-bdpp/index-eng.jsp>. This drug was cancelled post-market in 2004. Janet French, 'Nearly 80 Alberta Doctors Have Stepped Forward to Offer Physician-Assisted Death' *Edmonton Sun* (online) 13 March 2016 <www.edmontonsun.com/2016/03/13/nealy-80-alberta-doctors-have-stepped-forward-to-offer-euthanasia-physician-assisted-death>; Alberta Health Services, above n 124; Alberta Health Services, *Medical Assistance in Dying — Phase Four Action Phase* (26 August 2016) <www.albertahealthservices.ca/assets/info/hp/maid/if-hp-maid-process-admin-medication.pdf>.

[126] One group filling this void is the Canadian Association of MAiD Assessors and Providers, <http://camapcanada.ca/>. It has been set up by a small group of MAiD providers on a voluntary mutual-assistance basis. It would have been better if such an organisation could have been set up prior to the coming into force of the legislation and with sufficient government support to enable it to play a robust role in education and support from the outset.

need to be modified and instructions given on the completion of death certificates (what is the manner of death, the underlying cause of death, etc).[127] These steps enable robust data gathering, analysis and reporting, which again is essential for accountability and transparency, and having and deserving the trust of the public. They also enable research to be conducted on a range of issues aimed at improving end of life care. Unfortunately, Canada did not get its oversight infrastructure in place prior to the legalisation of MAiD. Indeed, more than a year after the legislation came into force, there is no pan-Canadian oversight system; there is considerable variability with respect to who is conducting case reviews (where any case review is being done), and there is no standard approach to what information is being reported and to whom. Even the death certificate forms and instructions are not consistent across the country.[128]

More positive lessons can be learned from other permissive jurisdictions, for example, the Netherlands and Belgium have robust systems for reviewing and reporting on all cases and the Netherlands, Belgium, and the permissive American states all gather and report on robust data sets.[129] The Netherlands also commissions a major end of life decision-making research study every five years rather than (as in Belgium) leaving this to researchers to find their own funding independently (and therefore somewhat irregularly).[130] However, nobody yet has developed a system that gathers reliable data on all requests (which can provide important evidence on a variety of issues such as patient access) or that facilitates research in an efficient, reliable, and cost-effective manner (eg, by linking MAiD cases through death certificates with large health information databases). Again, while these issues were flagged for the Canadian authorities, they did not get out ahead of them and so we are in a sense building the ship while sailing it—and this is definitely not ideal.

Fifth, ***beware of negative consequences*** that can accompany particular turns of phrase in legislative drafting and particular positions taken on substantive issues in the debate about criteria for access and procedural safeguards. In particular, as illustrated earlier, there are serious negative consequences flowing from the following elements of the Canadian

---

[127] Jocelyn Downie and Kacie Oliver, 'Medical Certificates of Death: First Principles and Established Practices Provide Answers to New Questions' (2015) 188(1) *Canadian Medical Association Journal* 49.

[128] Eg, until Ontario passed Bill 84 (above n 94), coroners in Ontario completed the medical certificates of death for MAiD cases and they are instructed to report 'combined drug toxicity' as the cause of death with reference to the underlying medical condition that qualified the person for MAiD and with 'suicide' as the manner of death (with reference to MAiD): the attending physician now prescribes what is written on the medical certificate of death; e-mail communication from Cheryl Mahyr, Issues Manager, Office of the Chief Coroner of Ontario Forensic Pathology Service, 31 January 2017 and 14 August 2017. Providers in Nova Scotia are being instructed to report the drugs as the immediate cause, the grievous and irremediable condition as the underlying cause, and whatever would have been recorded as the manner of death had the person died from the grievous and irremediable condition. MAiD is also noted at the bottom of the form: telephone communication from Krista Dewey, Deputy Registrar General, Nova Scotia.

[129] Eg, information for the Netherlands is available at Regionale Toetsingscommissies Euthansie, *Frequently Asked Questions* <www.euthanasiecommissie.nl/uitspraken/publicaties/faq-engels/faq/faq/frequently-asked-questions>; section 5 of the Belgian Euthanasia Act requires physicians to complete Federal Control and Evaluation Commission form (*Belgian Act on Euthanasia of May 28, 2002* <eol.law.dal.ca/wp-content/uploads/2015/06/Euthanasia-Act.pdf>; Oregon State publishes annual dying with dignity reports: see Oregon Health Authority, *Annual Reports* <public.health.oregon.gov/ProviderPartnerResources/EvaluationResearch/DeathwithDignityAct/Pages/ar-index.aspx>; Washington State also publishes data: see Washington State Department of Health, *Death with Dignity Data* <www.doh.wa.gov/YouandYourFamily/IllnessandDisease/DeathwithDignityAct/DeathwithDignityData>.

[130] A van der Heide et al, 'End-of-Life Decisions in the Netherlands over 25 Years' (2017) 377(5) *New England Journal of Medicine* 492, doi: 10.1056/NEJMc1705630.

legislation: capacity required at time of provision; mandatory waiting periods; access limited to those for whom death is 'reasonably foreseeable';[131] and allowing providers and institutions to opt out. This is not to say that legislators must avoid all of these elements (although I would argue for that). Rather, it is to say that legislators must be aware of the consequences of proceeding with those elements. It might be argued that the Canadian government did not know and therefore should not be blamed for the consequences of their legislative drafting. However, any jurisdiction that follows Canada will have been forewarned and will therefore bear the responsibility for the suffering that ensues.

Sixth, take the opportunity of assisted dying being on the legislative agenda to also ***address related end of life issues***. The Canadian legislation only deals with MAiD, so it did not resolve the following issues: unilateral withholding or withdrawal of potentially life-sustaining treatment (can a physician withhold or withdraw potentially life-sustaining treatment without the knowledge of or against the wishes of the patient or patient's substitute decision-maker?);[132] palliative sedation (can you provide deep and continuous sedation and respect a refusal of artificial hydration and nutrition for a patient with a neurodegenerative condition who is not expected to die for years but whose suffering has become enduring and intolerable?);[133] and voluntary stopping of eating and drinking (can patients stop eating and drinking until death and can they refuse not only artificial hydration and nutrition but also oral feeding through an advance directive?).[134] End of life decision-making is best seen as a spectrum of care and countries should have clear laws about the entire spectrum so that they can care best for all patients at the end of life. Canada does not. Australia does not. Yet both countries can and should.

The final lesson to be drawn from the Canadian experience is that ***the hard work that it takes to decriminalise MAiD is worth it***. Approximately 970 people have been able to access MAiD as of 31 December 2016.[135] Some (a much larger number) will have made a request for MAiD and qualified, but never self-administered or had a physician or nurse practitioner admininster it. An unknown number (but still higher) have been comforted to know that MAiD would or will be available to them, should, or when, they reach the point of enduring and intolerable suffering. Still others (a much, much larger number) will never have made a request but will

[131] This lesson is immediately relevant to the Australian context as drafts of legislation in different states have relied upon variations on the criterion of 'terminal illness'. If this criterion is defined in terms of a life expectancy rather than lethality of the condition, the legislation will likely generate the same negative consequence as has accompanied the Canadian criterion of 'reasonably foreseeable' (ie, patients starving themselves to get close enough to death to qualify).

[132] Lindy Willmott, Ben White and Jocelyn Downie, 'Withholding and Withdrawal of "Futile" Life-Sustaining Treatment: Unilateral Medical Decision-Making in Australia and New Zealand' (2013) 20 *Journal of Law and Medicine* 907.

[133] Jocelyn Downie, 'And Miles to Go Before I Sleep: The Future of End-of-Life Law and Policy in Canada' (2016) 39 *Dalhousie Law Journal* 413.

[134] Thaddeus Pope and Lindsey Anderson, 'Voluntarily Stopping Eating and Drinking: A Legal Treatment Option at the End of Life' (2011) 17 *Widener Law Review* 363; Thaddeus Pople and Amanda West, 'Legal Briefing: Voluntarily Stopping Eating and Drinking' (2014) 25(1) *Journal of Clinical Ethics* 68; Nataša Ivanović, Daniel Büche and André Fringer, 'Voluntary Stopping of Eating and Drinking at the End of Life – a "Systematic Search and Review" Giving Insight into an Option of Hastening Death in Capacitated Adults at the End of Life' (2014) 13(1) *BMC Palliative Care* 1.

[135] Government of Canada, 'Interium update on medical assistencing in dying in Canada June 17 to December 31, 2016' (31 May 2017), online: <www.canada.ca/en/health-canada/services/publications/health-system-services/medical-assistance-dying-interim-report-dec-2016.html>. The most regular, up-to-date, and comprehensive (within a province) data are available on the Alberta MAiD website: Alberta Health Services, *Medical Assistance in Dying: Data* <www.albertahealthservices.ca/info/Page14930.aspx>.

have been relieved just to know that the option would be there for them to pursue should their suffering ever become enduring and intolerable.

Obviously much still remains to be done in Canada. But these are at least some of the lessons that can be learned so far. My hope is that Australian states can take the good, leave the bad, and thereby profoundly enhance end of life care in Australia.

QUT Law Review ISSN: Online- 2201-7275
Volume 17, Issue 1, pp. 147–159 DOI: 10.5204/qutlr.v17i2.693

HAS THE RIGHT TO BREACH PATIENT CONFIDENTIALITY CREATED A COMMON LAW DUTY TO WARN GENETIC RELATIVES?

WENDY NIXSON*

This paper discusses the conflict between a medical practitioner's duty of care and duty to maintain patient confidentiality, and their statutory right to inform a relative about a possible genetic condition. The statutory right arguably creates a Rogers v Whitaker *type duty to provide the same information a patient might require in order to make informed choices about testing and treatment. In the event that reasonable clinical judgment is not applied to disclosure, the genetic relative ought to be offered the opportunity to seek redress through the common law if they suffer harm as a result.*

I INTRODUCTION

This paper sets out the current domestic position on disclosure of genetic information by medical practitioners *without patient consent* to do so, and reviews whether that position was altered by the amendments to the *Privacy Act 1988* (Cth) a decade ago. Whilst this involves only the minority of patients (since the majority willingly divulge genetic information to family members),[1] the issue has significant implications for the healthcare provider who 'faces a choice between preserving the confidentiality of one patient and preventing harm to another' as genetic testing becomes more prevalent in the future.[2]

The author sets out the existing duties to patients of both confidentiality and care and the circumstances in which a breach of patient confidentiality may be legally permissible. Whilst one cannot ignore the ethical ramifications of conflicting duties to patients and third parties, this article affords only a cursory glance at them due to its primary focus on the legal connotations of the question.

The remainder of the paper considers the current statutory *right* of a medical practitioner to disclose genetic information to relatives. In doing so, the author has considered the application of both domestic and international common law precedent (most recently, the UK decision of *ABC v St George's Healthcare NHS Trust)*[3] on the duty of care to third parties in a number of different clinical settings to determine whether this right has been, or could be, extended to a positive common law *duty to warn*.

Finally, the paper touches on the issue of foreseeability and its correlation to the causation of harm that might flow from non-disclosure but does not extend to a thorough analysis of the

* BA(Hons) University of Central England, General Manager of Shine Lawyers Pty Ltd.

[1] Margaret Otlowski, 'Australian Reforms Enabling Disclosure of Genetic Information to Genetic Relatives by Health Practitioners' (2013) 21 *Journal of Law and Medicine* 217.

[2] Anneke Lucassen and Malcolm Parker, 'Confidentiality and Serious Harm in Genetics: Preserving the Confidentiality of One Patient and Preventing Harm to Relatives' (2004) 12 *European Journal of Human Genetics* 93, 93; Sandi Dheensa, Angela Fenwick and Anneke Lucassen, '"Is This Knowledge Mine and Nobody Else's? I Don't Feel That." Patient Views About Consent, Confidentiality and Information-sharing in Genetic Medicine' (2016) 42 *Journal of Medical Ethics* 174.

[3] [2015] EWHC 1394 (QB), on appeal.

interrelating issues of breach of duty, factual causation or damage. Overall, the paper concludes that whilst a positive duty is not established, the doorway is certainly open for courts to find such a duty and in the author's view, it would not offend the common law principles of negligence if it was.

II DUTY OF CONFIDENTIALITY

Ingrained not only in their ethical duties towards patients but found in information protection laws,[4] health statutes (which sometimes create offences for disclosure),[5] and common law principles,[6] healthcare providers must keep information about, or provided by their patients confidential, even from family members, unless permitted to do otherwise.

The Hippocratic Oath establishes:

> What I may see or hear in the course of the treatment or even outside of the treatment in regard to the life of men, which on no account one must spread abroad, I will keep to myself, holding such things shameful to be spoken about.[7]

This premise reflects the importance and value of trust in the doctor-patient relationship so as to reinforce the continued role of 'public as well as private health'.[8] It is based in the ethical principle of autonomy, allowing an individual to have control over decisions affecting their medical treatment and arguably providing choice over what happens to the information they impart.[9]

The author assumes that for most practitioners, if not all, a breach of such an ingrained duty would be difficult to contemplate, let alone justify. The discussion in this paper reflects only the situation where disclosure of information is made absent the consent of the patient. In most cases, particularly in the context of genetic information, patients are willing to divulge information to relevant family members, or at the very least, allow their medical practitioner to do so.[10] Two studies undertaken firstly in a small group of Jewish women in Boston relating to a predisposal to BRCA1/2 mutation and secondly in a small group of students and professors at a university in the UK, both found that whilst patient confidentiality was important to the respondents, 'condition preventability' was the primary factor in determining whether patients would be willing to inform family members or have them informed by their medical practitioner.[11]

---

[4] *Privacy Act 1988* (Cth); *Privacy Amendment (Enhancing Privacy Protection) Act 2012* (Cth); *Privacy Legislation Amendment Act 2006* (Cth); *Health Records (Privacy and Access) Act 1997* (ACT); *Privacy and Personal Information Protection Act 1998* (NSW); *Information Privacy Act 2000* (Vic); *Health Records Act 2001* (Vic); *Information Privacy Act 2009* (Qld); *Health Legislation Amendment Act 2012* (NSW); *Data Protection Act 1998* (UK).

[5] *Health Act 1911* (WA); *Public Health Act 1997* (Tas); *Public Health Act 2005* (Qld); *Health Care Act 2008* (SA); *Public Health Act 2010* (NSW); *Public Health Act 2011* (SA).

[6] *Furniss v Fitchett* [1958] NZLR 396; *Hunter v Mann* [1974] QB 767.

[7] Ludwig Edelstein, *The Hippocratic Oath: Text, Translation, and Interpretation* (Johns Hopkins Press, 1943).

[8] *X v Y* [1988] 2 All ER 648 [653] (Rose J).

[9] Lucassen and Parker, above n 2.

[10] Otlowski, above n 1.

[11] Timothy Heaton and Victoria Chico, 'Attitudes Towards the Sharing of Genetic Information with At-risk Relatives: Results of a Quantitative Survey' (2016) 135 *Human Genetics* 109, 109; Lisa Lehmann et al, 'Disclosure of Familial Genetic Information: Perceptions of the Duty to Inform' (2000) 109 *The American Journal of Medicine* 705, 707.

Some commentators have suggested that:

> best practice is represented by striving to avoid the need to use the provisions [of the amended Privacy Act]. With a combination of professionalism and patience, most apparent conflicts can be resolved without recourse to disclosing private information without consent.[12]

Others believe the primary responsibility (or duty) of disclosure of such information falls on the individual patient themselves,[13] which would negate any duty on the medical practitioner and therefore any liability to family members entirely, although comprehending genetic information without medical assistance could be very difficult for some family members and therefore the medical practitioner would still have a role to play, albeit not a mandated one.[14]

However in line with the above, the question becomes whether a similar level of autonomy (or the duty of beneficence) should be extended to family members of patients with genetic conditions, such that they too could make informed decisions about the treatment that they may or may not wish to undergo with the benefit of the information provided.[15] Some suggest that 'the greater harm in maintaining patient confidentiality is to the relative, and therefore the rights of the relative should predominate'.[16]

Given this conflict, it has been suggested that a better approach would be a 'joint account' model where all relevant family members hold an equally vested interest to familial information[17] or that a model of 'comity' should be preferred over individual rights.[18] In fact, the Australian Medical Association advocated in 2012 for 'a national approach to raising public awareness of the risks and benefits of genetic testing including … the shared nature of genetic information'.[19] The reason for this joint approach to information sharing is that irrespective of how sacred the duty of confidentiality to a patient may be, it is recognised that there will always be occasions when harm to the patient (if confidentiality is breached) may be outweighed by the benefit of disclosure to others, particularly where the breach has the potential to protect others from harm.[20] This is clearly an intricate balancing exercise which will undoubtedly end

---

[12] Graeme Suthers, Elizabeth McCusker and Samantha Wake, 'Alerting Genetic Relatives to a Risk of Serious Inherited Disease Without a Patient's Consent' (2011) 194 *Medical Journal of Australia* 385, 386.

[13] Angus Clarke et al, 'Genetic Professionals' Reports of Nondisclosure of Genetic Risk Information Within Families' (2005) 13 *European Journal of Human Genetics* 556; Pascal Borry and Kris Dierickx, 'What Are the Limits of the Duty of Care? The Case of Clinical Genetics' (2008) 5(2) *Personalized Medicine* 101, 101–104; Marni Falk et al, 'Medical Geneticists' Duty to Warn At-risk Relatives for Genetic Disease' (2003) 120A *American Journal of Medical Genetics* 374.

[14] Loane Skene, 'Patients' Rights or Family Responsibilities? Two Approaches to Genetic Testing' (1998) 6 *Medical Law Review* 1.

[15] Roy Gilbar and Charles Foster, 'Doctors' Liability to the Patient's Relatives in Genetic Medicine' (2015) 24 *Medical Law Review* 112.

[16] Sharon Keeling, 'Duty to Warn of Genetic Harm in Breach of Patient Confidentiality' (2004) 12 *Journal of Law and Medicine* 235, 244.

[17] Malcolm Parker and Annette Lucassen, 'Genetic Information: a Joint Account?' (2004) 329 *British Medical Journal* 165; Charles Foster et al, 'Testing the Limits of the "Joint Account" Model of Genetic Information: A Legal Thought Experiment' (2015) 41 *Journal of Medicine and Ethics* 379; Skene, above n 14.

[18] Angela Davey, Ainsley Newson and Peter O'Leary, 'Communication of Genetic Information Within Families: The Case for Familial Comity' (2006) 3 *Bioethical Inquiry* 161.

[19] Australian Medical Association, *Genetic Testing – 2012* (1 April 2012) <https://ama.com.au/position-statement/genetic-testing-2012>, [1.5].

[20] Australian Law Reform Commission (ALRC) and National Health and Medical Research Council, Australian Health Ethics Committee (AHEC), *Essentially Yours: The Protection of Human Genetic Information in Australia*, Report No 96 (2003).

up resulting in a determination that one party's rights are more significant than another's unless a joint account approach can be adopted.[21]

III PERMISSIBLE BREACHES OF DUTY OF CONFIDENTIALITY

Disclosure in the above context will therefore be based on clinical judgement, an often difficult path to tread, so even in circumstances where the patient expressly prohibits it, the medical practitioner is afforded some legal protection in certain circumstances if they do disclose information to others. For example, a medical practitioner may be required by law to provide information about a patient, either in the context of legal proceedings, in the event of knowledge relating to an offence, child abuse or neglect, or under various public health statutes and regulations relating to notifiable diseases in order that appropriate action may be taken to avoid the spread of disease.[22] It has been proposed therefore that a positive common law duty to disclose genetic information would not be inconsistent with these requirements.[23]

Perhaps the most difficult to define is what is known as 'the public interest exception' to the duty of confidentiality which is finely balanced between the 'rival interests' of patients to confidentiality and of society to public safety.[24] As genetic relatives are arguably representatives of the public when viewed from within the confines of the patient-doctor relationship, this exception could be utilised to permit disclosure of genetic information. However, for many this was 'not regarded as a suitable basis on which to allow for disclosure',[25] as the harm would not extend to the community at large, and more carefully constructed regulation on the point was required.

A *Legal* Right *to Inform*

A decade ago, amendments were made to the *Privacy Act 1988* (Cth) following the *Essentially Yours* report of the Australian Law Reform Commission and the Australian Health Ethics Committee of the National Health and Medical Research Council ('NHMRC').[26] The amendments specifically permitted the disclosure of genetic (as opposed to 'health') information without a patient's consent in circumstances where the medical practitioner 'reasonably believes that the use or disclosure is necessary to lessen or prevent a serious threat to the life, health or safety (whether or not the threat is imminent) of another individual who is a genetic relative'[27] of their patient. The report suggested that 'developments in genetic medicine have implications for the extent to which the confidentiality of the doctor and patient relationship should be given primacy over other ethical considerations'[28] and called for a set of

[21] Suthers, McCusker and Wake, above n 12.
[22] *Health Act 1911* (WA); *Public Health Act 1997* (ACT); *Public Health Regulation 2000* (ACT); *Public Health Act* 2005 (Qld); *Public Health Regulation 2005* (Qld); *Public Health and Wellbeing Act 2008* (Vic); *Public Health and Wellbeing Regulations 2009* (Vic); *Public Health Act 2010* (NSW); *Public Health Regulation 2012* (NSW); *Public Health Act 2011* (SA); *Public Health (General) Regulations 2013* (SA). Janine McIlwraith and Bill Madden, *Health Care & The Law* (Thomson Reuters, 5th ed, 2010) 287. Included in a national list of over 70 communicable disease outbreaks of national significance.
[23] Meredith Blake, 'Should Health Professionals Be Under a Legal Duty to Disclose Familial Genetic Information?' (2008) 34 *Commonwealth Law Bulletin* 571.
[24] Alister Abadee, 'The Medical Duty of Confidentiality and Prospective Duty of Disclosure: Can They Co-exist?' (1995) 3 *Journal of Law and Medicine* 75.
[25] Otlowski, above n 1, 222.
[26] Amendments were made by the enactment of the *Privacy Legislation Amendment Act 2006* (Cth) and the introduction of section 95AA approving guidelines by the NHMRC. See ALRC and AHEC, above n 20.
[27] *Privacy Act 1988* (Cth) Schedule 3 National Privacy Principle 2.1(ea)(ii), since repealed.
[28] ALRC and AHEC, above n 20, 548.

guidelines to assist 'health professionals in providing effective health services to their patients'.[29] In more recent times, the legislation was further amended by the enactment of the *Privacy Amendment (Enhancing Privacy Protection) Act 2012* (Cth) which unified public and private sector approaches by repealing the National Privacy Principles and creating the Australian Privacy Principles ('APPs').

Currently, APP 6 specifically permits a medical practitioner to disclose a patient's genetic information if the disclosure is conducted in accordance with guidelines approved under section 95AA of the *Privacy Act 1988* (Cth) and the recipient of the information is a *genetic relative* (author's emphasis) of the patient, despite recommendations by the NHMRC to cover threats to *any known* individual.[30] This suggests that obvious practical issues surrounding disclosure, discussed in more detail below, have helped to shape the scope of the medical practitioners' right to inform.

The guidelines do not create a legal duty to disclose a patient's genetic information, rather 'a framework ... to make disclosure in appropriate circumstances'.[31] As with all other aspects of the duties of a medical practitioner, clinical judgement will remain the keystone to disclosure of genetic information, particularly in determining whether the threat of a genetic condition is serious and whether disclosure should be made because the genetic condition is capable of being prevented or ameliorated. Whilst this appears to tie in with the study referred to above suggesting 'condition preventability' is the primary consideration for disclosure,[32] it does beg the question as to whether other 'non-serious' genetic conditions ought to be disclosed. Certain guidelines suggest that 'where genetic information is diagnostic or highly predictive of an illness or relationship, it might carry greater significance that in other situations'[33] which would suggest that predictability, even of a 'non-serious' genetic condition, should be the influential factor for disclosure. In the former case, consideration is required of the potential for harm where disclosure is not made whereas in the latter case, any potential for harm caused by the disclosure, should the condition not eventuate, needs to be considered.

The *Essentially Yours* report identified that health professionals ought to be afforded some legal protection when such disclosure was made because 'the question of whether non-consensual disclosure would be legally defensible butts heads with the legal duty of confidentiality'.[34] The legislative amendments, which are an arguable statutory spin-off from the public interest exception to confidentiality, remain the most internationally detailed on point.[35] Yet it remains to be seen whether they are being utilised by the Australian medical profession, given the seemingly ad hoc nature of the decision-making process and there being no requirement for central reporting of these decisions.[36] Whilst protection from statutory

[29] Ibid 544. These guidelines were subsequently established as: National Health and Medical Research Council and Office of the Privacy Commissioner, *Use and Disclosure of Genetic Information to a Patient's Genetic Relatives Under Section 95AA of the Privacy Act 1988 (Cth): Guidelines for Health Practitioners in the Private Sector* (NHMRC, 2009) and updated in 2014: see <https://www.nhmrc.gov.au/guidelines-publications/pr3>.

[30] Defined in the *Privacy Act 1988* (Cth) s 6(1) as 'another individual who is related to the first individual by blood, including but not limited to a sibling, a parent or a descendant of the first individual'.

[31] Otlowski, above n 1, 224.

[32] Heaton and Chico, above n 11, 109.

[33] Royal College of Physicians, Royal College of Pathologists and British Society for Human Genetics, 'Consent and Confidentiality in Clinical Genetic Practice: Guidance on Genetic Testing and Sharing Genetic Information' (Report of the Joint Committee on Medical Genetics, 2nd ed, RCPath, 2011), 2.

[34] Mireille Lacroix et al, 'Should Physicians Warn Patients' Relatives of Genetic Risks?' (2008) 178 *Canadian Medical Association Journal* 593, 594.

[35] Otlowski, above n 1.

[36] Ibid.

liability is offered,[37] there is no case law considering the extension of such protection to tortious liability although it is argued that 'disclosure made in compliance with established guidelines would be evidence that it accorded with accepted standards of professional practice',[38] thus a defence might be established. [39]

B *The Right* Not *to Know*

Of equal importance when considering the individual's right to be fully informed of genetic information, is the individual's right not to know the information at all (or a medical practitioner's positive 'duty not to interfere with my ignorance').[40] The decision might be influenced by any number of legal and social implications such as 'life and health insurance, employment, loans, marriageability, reproductive choices, adoption, school admission and suicide'.[41] One side of the argument equates to an autonomous right premised on self-determination although in fact many will choose not to investigate their risk further, even if informed.[42] The other, although understood and encompassed in some human rights legislation and raised as a concern in some guidelines,[43] has been argued to be incompatible with autonomy because ignorance leads to the individual being unable to make informed choices.[44]

If one considers the right not to know in the context of foreseeable harm, the balancing of the competing rights remains the same. One could envisage circumstances where a family member receiving information against their will suffers psychological harm or alternatively family members who remain uninformed by another's ignorance suffer physical harm by being unable to take action regarding their own health.[45] It would appear to the author that the legislative changes seek to balance these competing rights by *not* enforcing a legal duty on medical practitioners and allowing clinical judgement to remain the driving force.

IV DUTY OF CARE

The existence of an established obligation to take care of another, particularly in the setting of healthcare provider and patient, can be demonstrated in many facets of our society. The Hippocratic Oath taken by all medical practitioners, the ethical principle of non-maleficence (doing no harm), the common law tort of negligence, and various statutes and codes of conduct – all provide obligations on healthcare providers to act, treat and address issues of health concern by their patients.[46] These obligations already extend in certain circumstances beyond

[37] Under the *Privacy Act 1988* (Cth).
[38] ALRC and AHEC, above n 20, 565.
[39] Tortious liability under the various Civil Liability Acts: *Civil Liability Act 1936* (SA) s 41; *Civil Liability Act 2002* (NSW) ss 5P, 5O; *Civil Liability Act 2002* (Tas) ss 21, 22; *Civil Liability Act 2002* (WA) ss 5O, 5PB; *Civil Liability Act 2003* (Qld) ss 21, 22; *Wrongs Act 1958* (Vic) ss 59, 60.
[40] Philippa Malpas, 'The Right to Remain in Ignorance About Genetic Information: Can Such a Right Be Defended in the Name of Autonomy?' (2005) 118 *New Zealand Medical Journal* U1611, 3.
[41] Skene, above n 14, 9.
[42] Keeling, above n 16.
[43] *Universal Declaration on the Human Genome and Human Rights*, GA Res 29 C/17, 29th sess (11 November 1997) Article 5(c) which says 'the right of each individual to decide whether or not to be informed of the results of genetic examination and the resulting consequences should be respected'; see also NHMRC and Office of the Privacy Commissioner, above n 29.
[44] Jane Wilson, 'To Know or Not to Know? Genetic Ignorance, Autonomy and Paternalism' (2005) 19 *Bioethics* 492.
[45] Ibid.
[46] Matthew Lynch and David Ranson, 'Doctors' Duties and Third Parties' (2000) 7 *Journal of Law and Medicine* 244.

the doctor-patient relationship, discussed above. However, as can be seen below, the Courts have battled with whether a similar duty of care can be established towards others.

A legal duty of care is one of the three well-founded principles of the tort of negligence, often defined by reference to the position, responsibility, proximity and/or relationship between the parties. The early landmark decision in the UK of *Donaghue v Stevenson*[47] established that a foreseeable class (in that case, purchasers of ginger beer), were owed a duty (by the manufacturer of the ginger beer) on the basis of what became known as Lord Atkin's 'neighbour test' in which he stated:

> You must take reasonable care to avoid acts or omissions which you can reasonably foresee would be likely to injure your neighbour. Who, then, in law is my neighbour? The answer seems to be persons who are so closely and directly affected by my act that I ought reasonably to have them in contemplation as being so affected when I am directing my mind to the acts or omissions which are called in question.[48]

The case established a number of legal principles relating to the duty of care; the standard of the care to be provided (not discussed further in this paper); to whom a duty might be owed; and whether the act or omission of one party to another was one which might foreseeably cause harm. These principles have been cited with approval in many key international decisions, particularly in the UK and Australia; they have become enshrined in modern civil liability legislation, and feature heavily in the context of this issue.

A *What Does the Duty of Care Encompass?*

The content of the legal (and arguably ethical) duty to a patient comes from the requirement for medical practitioners to exercise reasonable care and skill in their practice of medicine to their patients.[49] It extends not only to positive actions, such as positive diagnosis or surgical technique, but also omissions, such as the failure to refer for specialist opinion or follow up test results.

Of most relevance, here is what is commonly called the 'duty to warn', a concept confirmed in the leading authority of *Rogers v Whitaker*,[50] in which the High Court was tasked with considering how to measure the failure of the medical practitioner to advise his patient of the risks involved in the medical treatment she was to undergo. Unanimously, the Judges of the High Court agreed that a duty of care should include the provision of information and advice 'if in the circumstances of the particular case, a reasonable person in the plaintiff's position, if warned of the risk [of sympathetic opthalmia], would be likely to attach significance to it…'.[51] The plaintiff in that case had 'incessantly' questioned the doctor as to possible complications of her surgery. She was particularly concerned that her 'good' left eye would not be affected, although she did not ask specifically whether the surgery to her right eye would affect her left eye. The rare risk of sympathetic ophthalmia eventuated, and the plaintiff was rendered almost totally blind. She alleged the doctor should have given her advice or information regarding this risk. Gaudron J found that:

---

[47] [1932] AC 562.
[48] *Donaghue v Stevenson* [1932] AC 562, 580 (Atkin L).
[49] *Rogers v Whitaker* (1992) 175 CLR 479.
[50] Ibid.
[51] Ibid 490 (Mason CJ, Brennan, Dawson, Toohey and McHugh JJ).

> a patient may have special needs or concerns which, if known to the doctor, will indicate that special or additional information is required. In a case of that kind, the information to be provided will depend on the individual patient concerned. In other cases, where, for example, no specific enquiry is made, the duty is to provide the information that would reasonably be required by a person in the position of the patient.[52]

In the event that a patient raises specific concerns about their illness or condition in the context of whether it is likely to affect a family member, *Rogers v Whitaker*[53] seems to establish clearly that the duty of care would encompass such a discussion. The more difficult assessment is whether, in the knowledge that a genetic condition would affect the patient's family member, the doctor is obliged to provide such information when no such specific enquiry has been made.

The duty to provide information about risks has found significant favour in civil liability legislation across the country and medical codes of conduct.[54] In the author's view, if the law considers that a 'reasonable person' is entitled to information which would assist their decision about whether to undergo treatment or follow advice, it follows that 'the common law might conceivably impose a duty on a doctor to warn relatives' who might be forced to make the same decisions as the patient (or plaintiff) with a known genetic condition.[55]

B *Scope of Duty*

The author suggests however, that it is the scope of that duty that has caused the most controversy in the various international authorities. The questions regarding to whom the duty is owed and in which circumstances it ought to be applied have been the key features of the cases discussed below.

Given that those within the class of 'purchasers' were not specifically known to the manufacturer of the ginger beer in *Donaghue v Stevenson*, it would seem that the duty of care was always envisaged to extend 'not only to patients but to others whose personal wellbeing ... may be harmed by failure to take reasonable care of a patient'.[56] However, it took several decades after that case before developments in the law across the globe established a special relationship of proximity between a healthcare provider and a person not previously their patient and even then a cautious approach to the extension of tortious liability has been applied.[57]

---

[52] Ibid 493 (Gaudron J).
[53] (1992) 175 CLR 479.
[54] For example, s 21 of the *Civil Liability Act 2003* (Qld) in which it states that a doctor does not breach a duty owed to a patient to warn of risk of personal injury to the patient, unless the doctor at that time fails to give or arrange to be given to the patient (a) information that a reasonable person in the patient's position would, in the circumstances, require to enable the person to make a reasonably informed decision about whether to undergo the treatment or follow the advice; (b) information that the doctor knows or ought reasonably to know the patient wants to be given before making the decision about whether to undergo the treatment or follow the advice. Medical Board of Australia, 'Good Medical Practice: a Code of Conduct for Doctors in Australia' (2014) <http://www.medicalboard.gov.au/Codes-Guidelines-Policies/Code-of-conduct.aspx> 3.3.6 promotes 'Ensuring that patients are informed of the material risks associated with any part of the proposed management plan'.
[55] Skene, above n 14, 21.
[56] McIlwraith and Madden, above n 22, 186.
[57] Allison Langford, 'Doctor's Liabilities to Third Parties' (2001) 75(11) *Law Institute Journal* 74.

In the US, the complexity of the decision to extend the duty of care to a third party first arose in the seminal case of *Tarasoff v Regents of the University of California*,[58] ('*Tarasoff*') in which the Supreme Court:

> sought to balance the ... foreseeability of harm to a third party, the degree of certainty that she would suffer injury, the closeness of the connection between the defendant's conduct and the third party's injury; the moral blameworthiness attached to the defendant's conduct and the potential consequences to the community in making its decision.[59]

This case opened the doors for the duty of care to be applied to third parties in other circumstances, although US courts were very careful to only 'develop novel categories of negligence incrementally and by analogy with established categories'.[60]

Some twenty years after *Tarasoff*, the US first considered its application to genetically transmissible conditions in *Pate v Threlkel*,[61] ('*Pate*') and *Safer v Estate of Pack*.[62] In both cases, the Courts established that the medical practitioners involved owed a duty of care to their patients' children to warn of the risk of a genetic condition. However, in *Pate*, the Florida Supreme Court found on appeal that the scope of the duty was too onerous, as 'to require the physician to seek out and warn various members of the patient's family would often be difficult or impracticable and would place too heavy a burden on the physician'.[63] It was held that the duty would be sufficiently discharged if the patients themselves were warned of the risk to their relatives, suggesting that practical difficulties have some bearing on whether indeed a duty of care to genetic relatives ought to be imposed at all.

In the UK, the case of *Caparo Industries plc v Dickman*[64] ('*Caparo*'), still cited today, established a three-stage test to determine the scope of duty, based on foreseeability, proximity and fairness, justice and reasonableness.[65] The proximity test has caused most difficulty in cases brought by third parties (it was not adopted by the High Court of Australia in *Sullivan v Moody*,[66] discussed below) since in many cases the plaintiff had no previous relationship with the defendant and in other cases would not have been within a readily identifiable class. The latter issue is not relevant to the question of genetic information, for which the plaintiffs belong to an 'ascertainable and finite' group at risk.[67]

In Australia, in the case of *BT v Oei*,[68] the Court held that Oei; a medical practitioner, owed a duty of care to BT, the sexual partner of his patient, AT; and that BT contracted HIV due to the defendant's failure to diagnose and adequately counsel AT in relation to his HIV status.[69]

---

[58] 551 P 2d 334 (1976).
[59] Judith Regan, Ann Alderson and William Regan, 'Health Care Providers' Duty to Warn' (2002) 95(12) *Southern Medical Journal* 1396, 1396.
[60] Including cases involving contagious and/or communicable diseases or the administration of prescription medication to car drivers who subsequently have accidents. See per Brennan J in *Sutherland Shire Council v Heyman* (1985) 157 CLR 424, [481].
[61] 640 So 2d 183 (1994).
[62] 677 A 2d 1188 (1996).
[63] *Pate v Threlkel*, 661 So 2d 278 (1995) [282].
[64] [1990] 2 AC 605 (HL).
[65] Medical Board of Australia, above n 54; Rachael Mulheron, *Medical Negligence: Non-Patient and Third Party Claims* (Ashgate, 2013).
[66] (2001) 207 CLR 562.
[67] Keeling, above n 16, 56.
[68] [1999] NSWSC 1082.
[69] Ibid [14].

The focus of the Court's decision in this case appears to have been on the foreseeability of the harm caused, while 'specifically steering clear of any decision to the effect that there is a duty to warn a "non-patient" of the potential risk posed by a patient',[70] a finding subsequently followed in *PD v Dr Nicholas Harvey* (and upheld on appeal).[71] Whilst the Court held that the doctors were negligent firstly in their treatment of PD and secondly in their public duty to minimise the risk of the spread of the disease, it held there was no positive duty to inform PD of her sexual partner's HIV status, and in fact nor could Dr Harvey do so, because the law at the time expressly prohibited such disclosure.[72]

In *Sullivan v Moody*, the High Court considered whether the defendants owed a duty of care to the plaintiff; a suspect in a criminal investigation of sexual abuse of his daughter, for failure to exercise reasonable care in the conduct of the investigation, thereby causing him psychological injury. The High Court did not follow the proximity part of the three-stage test outlined in *Caparo* and was at pains to point out that the scope of the duty should not be extended where it 'would give rise to inconsistent obligations' (in this case, firstly, the statutory obligations of a local authority and secondly, the apparent competing interests of the victim and the plaintiff).[73] It was held that finding 'a duty of care would so cut across other legal principles as to impair their proper application'.[74]

In the more recent group of Australian cases involving those who suffer harm at the hands of a psychiatric patient,[75] courts held that a public authority with statutory powers under the *Mental Health Act 1990* (NSW) did not owe a duty of care to those into whose care the psychiatric patient was released. Relying heavily on the principles in *Sullivan v Moody*, these cases again highlighted the conflict between the duty of care to the patient and a duty owed to known third parties. It is worth noting that the courts were again not concerned by the fact that there was no previous relationship between the medical practitioners and the plaintiffs in these cases, suggesting that 'the lack of a previous or current relationship between the health professional and the [third party] is not a bar to the finding of a duty to warn'.[76]

In 2015, the UK High Court heard its first case involving a genetic relative alleging a failure to warn of a genetic condition.[77] The plaintiff's father in that case, after killing the plaintiff's mother, was detained in a mental health hospital where he was subsequently diagnosed with Huntington's disease. At the time of his diagnosis, the defendant sought permission to disclose it to the plaintiff (she was pregnant at the time) but the patient refused permission. The plaintiff only became aware of the fact some time later, after she had given birth to her daughter. She was diagnosed with the condition but, given her daughter's age, was unable to have her tested so at the time of the hearing, it was not known whether the plaintiff's daughter also had the condition. The plaintiff alleged that she should have been advised of the diagnosis at the time of her pregnancy and that, given the result, she would have terminated her pregnancy.

[70] Lynch and Ranson, above n 46, 245.
[71] [2003] NSWSC 487; *Harvey v PD* (2004) 59 NSWLR 639 (Court of Appeal).
[72] Bernadette Richards, '*PD v Dr Nicholas Harvey*: A Threat to Confidentiality or Straightforward Breach of Duty' (2003) 7 *University of Western Sydney Law Review* 162.
[73] *Sullivan v Moody* (2001) 207 CLR 562, [60] (Gleeson CJ, Gaudron, McHugh, Hayne and Callinan JJ).
[74] Ibid [53].
[75] *Hunter and New England Area Health Service v McKenna; Hunter and New England Area Health Service v Simon* (2014) 253 CLR 270; *Hunter Area Health Service v Presland* (2005) NSWLR 22.
[76] Keeling, above n 16, 240.
[77] *ABC v St George's Healthcare NHS Trust* [2015] EWHC 1394 (QB).

Applying the *Caparo* test, the Court held that it would not be fair, just and reasonable to find that the defendant owed a duty of care to the plaintiff stating that 'it would be a radical departure to impose liability in circumstances such as these'[78] and that doing so might set a precedent for clinicians to breach confidentiality without justification (the author respectfully disagrees).[79] The Court also stated that it would ordinarily be troubled by a lack of special relationship between the plaintiff and defendant, although that did not apply to the facts of this case.[80] The case is currently on appeal but has already been applied in *Smith v University of Leicester NHS Trust*,[81] a case involving the second cousins of a patient with a long-standing, but undiagnosed, genetic disease.

V HAVE THE AMENDMENTS TO THE PRIVACY ACT 1988 CREATED A DUTY TO WARN?

On consideration of the legal test in duty to warn cases, enunciated in *Rogers v Whitaker*, it would appear that any reasonable person ought to be offered the opportunity to consider his or her genetic health issues and treatment options. In the author's view, it would not be sufficient to rely on patients themselves to disseminate genetic information as a means of discharging a medical practitioner's duty, since doctors could not be confident that the information was passed on at all, or that it was passed on with the appropriate advice.

The statutory right to inform, and the guidelines which apply to it, have been carefully constructed so as to provide medical practitioners with the tools to exercise clinical judgement before making such disclosure, and a clear process by which that disclosure ought to be carried out. In the event that this is not followed, or indeed reasonable clinical judgment is not applied, the genetic relative ought to be offered the opportunity to seek redress through the common law if they suffer harm as a result.

However, the raft of case law outlined above demonstrates that domestic courts are still not readily amenable to extending a positive duty of care to third parties in general. By inference, this would suggest that in this scenario the law is likely to place higher worth on the patient's rights than those of the relative, who may in fact suffer an equally serious harm. In cases where the patient and genetic relative share a common interest, i.e., both need to be warned about the same genetic condition and treatment options so as to make informed decisions about their health, there would be little conflict between the rights of each and therefore it follows that a duty to the genetic relative could be imposed.[82] Where the plaintiff fails to establish a duty of care, as evidenced in the cases above, this tends to be on the basis that the interests of the patient and the plaintiff are very different and the Courts have valued the patient's (or even society's) interests first. However, 'this does not mean that no duty is owed .... It simply means that the scope of the duty of care does not extend to disclosure'.[83]

At the time of writing, there is no case law in Australia on the specific issue of disclosure of genetic information to a relative. Given the advances in, and accessibility to genetic testing, the author is surprised there has been no judicial consideration of this point, although one argument might be that this is evidence that the statutory right to inform genetic relatives *is* being exercised by medical practitioners, such that genetic relatives are making informed, and timely,

[78] Ibid [27].
[79] *Sullivan v Moody* (2001) 207 CLR 562 [13].
[80] Ibid [28].
[81] [2016] EWHC 817 (QB).
[82] Gilbar and Foster, above n 15.
[83] Blake, above n 23, 591.

decisions about testing and treatment options. Alternatively, it may be that despite the issue of whether a duty even exists, the other legal hurdles, such as breach, causation and damage cannot be met. It may be for this reason that some believe that the imposition of a duty to genetic relatives is unlikely to be successful here and it was unsupported by the NHMRC in the *'Essentially Yours'* report.[84]

Some commentators are confident, and the author agrees, that '[w]hen the usual principles of negligence, and the legislative reforms of tort law[85] are applied to genetic harm, a duty to warn unknowing blood relatives of their risk of serious genetic disease should be found in the common law'.[86] It seems that domestic courts have abandoned the need for a relationship of proximity with the defendant to be established in order for a duty of care to be imposed, unlike the current UK position. That being so, and given that the majority of patients will disclose information to their genetic relatives, the pool of possible plaintiffs will be relatively small but more importantly readily identifiable. This practical hurdle, which has impeded success in other international cases, appears capable of being overcome in our domestic courts. Overall, it is the author's view that considering policy and legal principles, domestic courts could readily determine a duty of care to genetic relatives.

A *Practical Issues of a Duty to Warn*

The literature raises a number of practical issues relating to the imposition of a duty, including identifying the likely plaintiffs (which should not be difficult, given the legislative definition of a genetic relative), tracking them down once identified, the means by which the information is provided to them, whether there should be an ongoing obligation to provide updates on their risk of disease,[87] the inter-familial consequences of disclosure, the content of the duty for effective discharge of liability (which, in the author's view, should be measured in accordance with professional standards of practice in line with that afforded to patients) and the further cost and workload burden on healthcare providers (which could arguably be addressed by notification to a statutory body for their action).[88] In some cases discussed above, these practical issues have informed the Courts' views as to whether the scope of the duty of care can be extended to third parties. In the author's view, they should not impede the imposition of a duty to warn relatives of genetic information because they have already been adequately foreshadowed by the relevant statutory guidelines for such disclosure.

B *Foreseeability of Harm*

Finally, in considering foreseeability of harm in the context of disclosure of genetic information, the author briefly raises the question: what is the harm? The harm is not the eventual development of a predisposed genetic condition but the harm that results from 'not being aware of the risk and therefore being unable to take steps to prevent' the condition.[89]

This leads to the next question which is how the risk of harm is categorised, and therefore also quantified, for the purposes of assessing the causative loss to the genetic relative. For example, if a genetic relative commenced a tortious action for the failure to advise of a genetic condition

[84] Skene, above n 14; ALRC and AHEC, above n 20, 556.
[85] And also, privacy laws.
[86] Keeling, above n 16, 252.
[87] Gary McAbee, Jack Sherman and Barbara Davidoff-Feldman, 'Physician's Duty to Warn Third Parties About the Risk of Genetic Diseases' (1998) 102(1) *Pediatrics* 140.
[88] Keeling, above n 16.
[89] Ibid 248.

which may or may not eventuate, the risk of harm might be insignificant if the condition does not eventuate. Does the genetic relative have to wait for a diagnosis of the genetic condition before an action can commence? Should the quantification of risk mirror the statutory requirements for disclosure, in other words, the risk has to be a 'serious threat to health' (which, again, comes back to clinical judgement); and does this suggest that statistical predictability, rather than the balance of probability test, applies?

Finally, if the harm does eventuate, what is the plaintiff's damage? If the genetic condition cannot be cured but can be ameliorated with appropriate treatment, does the plaintiff lose the opportunity to improve their health? Does the leading authority of *Tabet v Gett*[90] mean that these plaintiffs might not be able to commence a lost opportunity claim in any event, even if there is a positive legal duty owed? It is beyond the scope of this paper to consider these issues in any greater detail but they go some way to illustrate the complexity of the considerations to be applied in a common law duty to warn.

VI CONCLUSION

> The recognition that a health professional owes a duty of care to the relatives of a patient who has been diagnosed with a familial genetic condition finds support in medical ethics, and can be accommodated within the existing framework of the law. In particular it is apparent that the ethos of the law of negligence is not opposed to the recognition of such a duty of care.[91]

However, as above, we have seen that international and domestic courts have found it difficult to attribute tortious liability to healthcare providers for a failure to directly warn the third-party plaintiff.

Of most significance appears to be the balancing exercise of the duties already owed to a patient against a duty to an individual with whom the doctor does not necessarily have a therapeutic relationship. Yet statutory provision permits disclosure in what is arguably a discrete number of circumstances where appropriate clinical judgement dictates. This would seem to pave the way to a legal *Rogers v Whitaker* type duty to provide genetic relatives with the same level of information that a patient might require in order to make their own informed choices about testing and treatment.

VII ADDENDUM

Since the writing of this article, the appeal decision in the matter of *ABC v St George's Healthcare NSH Foundation Trust*[92] has been handed down. The original decision of the High Court to strike out the plaintiff's claim was overturned thereby allowing the plaintiff to continue her action to trial. As such, it remains to be seen whether the UK courts will extend the duty of care to this arguably 'novel' situation.

[90] (2010) 240 CLR 537
[91] Blake, above n 23, 592.
[92] [2017] EWCA Civ 336.

QUT Law Review ISSN: Online- 2201-7275
Volume 17, Issue 1, pp 160–173 DOI: 10.5204/qutlr.v17i1.686

THE UNFAIR CONTRACT TERM PROVISIONS: WHAT'S TRANSPARENCY GOT TO DO WITH IT?

PETER SISE*

Provisions in the Australian Consumer Law allow a court to declare an 'unfair' term in a 'consumer contract' or a 'small business contract' void. When determining whether a term is unfair, a court must consider the extent to which it is transparent. Transparency is important since it is one of only two factors that a court must consider when making this determination. This article will examine whether transparency is logically relevant to the legislative test for whether a term is unfair. It will argue that it is of limited relevance and hence should not be a mandatory consideration for determining unfairness. It will then consider several alternatives to making transparency a mandatory consideration.

I INTRODUCTION

The *Australian Securities and Investments Commission Act 2001* (Cth) ('ASIC Act') and *Australian Consumer Law* ('ACL') contain provisions addressing unfair contract terms ('UCT provisions') in standard form contracts. The ACL[1] requires a court to consider the extent to which a term is transparent when determining whether the term is unfair. Strangely, transparency has limited logical relevance to whether a term is unfair. This is due to the narrow test in the ACL for determining unfairness. If a broad test were used, such as 'the court must determine whether the term is unfair in all the circumstances', transparency may be of greater relevance, but that sort of test has not been adopted. This article will first examine the relevance of transparency to the test for whether a term is unfair and argue that it has limited relevance. It will then address how the ACL could be amended to account for this limited relevance.

Transparency is one of only two factors that a court must consider when determining whether a term is unfair. For this reason, transparency and its logical relevance to the test for whether a term is unfair are important.

II THE MEANING OF 'UNFAIR' AND 'TRANSPARENT'

A *The Meaning of Unfair*

Section 24(1) of the ACL states the test for whether a term 'unfair'. It provides as follows:

> (1) A term of a consumer contract is ***unfair*** if:
> (a) it would cause a significant imbalance in the parties' rights and obligations arising under the contract; and

* LLB (Hons) (The University of Melbourne). Senior Associate, Clayton Utz. The views expressed in this article are those of the author and not of Clayton Utz.

[1] For simplicity, this article will only refer to the UCT provisions contained in the ACL. Equivalent provisions exist in the ASIC Act but those provisions only relate to financial products and financial services.

(b) it is not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term; and
(c) it would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on.

The test for whether a term is unfair is quite specific. A term is only unfair if it fulfils each of the three requirements in s 24(1). The test is not cast in wide terms, such as a 'term will be unfair if it is unfair in all the circumstances'.

Section 24(2) provides that a court *may* take into account such matters as it thinks relevant when determining whether a term is unfair, but *must* take into account 'the extent to which the term is transparent' and the 'contract as a whole'. The second of these two mandatory considerations is unlikely to result in a court considering anything which it would not have considered in the absence of s 24(2). Due to s 24(1)(a), a term will not be unfair unless 'it would cause a significant imbalance in the parties' rights and obligations arising *under the contract*' [emphasis added]. In order to determine whether this requirement has been fulfilled, a court must surely consider the contract as a whole, since s 24(1)(a) is not limited to a consideration of the rights and obligations arising under the impugned term or some other discrete part of the contract.

The other mandatory consideration—'the extent to which the term is transparent'—is unlikely to be considered by a court in the absence of s 24(2), since it is not readily associated with any of the three requirements listed in s 24(1) and, as will be argued in this article, transparency is of limited relevance to these requirements.

B *Transparent*

'Transparent' is defined in s 24(3) of the ACL as follows:

(3) A term is ***transparent*** if the term is:
(a) expressed in reasonably plain language; and
(b) legible; and
(c) presented clearly; and
(d) readily available to any party affected by the term.

The elements of this definition will be considered later in greater detail. For now, it is worth noting that transparency is defined as an absolute concept. There are no degrees of transparency. A term is only transparent if it fulfils each of the four requirements listed in s 24(3) of the ACL. If it does not fulfil all these requirements, it is not transparent. Despite this, s 24(2) requires a court to consider 'the *extent* to which the term is transparent' [emphasis added]. It is difficult to reconcile this approach with the absolute terms in which transparency is defined. Any term which does not fulfil all four requirements of s 24(3) will fail to be transparent. Hence, the only way to assess the extent of transparency is to judge the extent to which a term fails to be transparent. This, however, is not considering 'the extent to which the term *is* transparent' because the term is actually not transparent according to s 24(3); rather, it is considering the extent to which a non-transparent term falls short of being transparent.

C *Case Law Concerning the UCT Provisions*

There are presently few decisions from the Federal Court of Australia or state or territory Supreme Courts considering the UCT provisions.[2] At the time of writing, there were four Federal Court decisions: *ACCC v CLA Trading Pty Ltd* ('*Europcar*'),[3] *ACCC v Chrisco Hampers Australia Limited* ('*Chrisco*'),[4] *ACCC v ACN 117 372 915 Pty Limited (in liq) (formerly Advanced Medical Institute Pty Limited*)[5] and *ACCC v Get Qualified Australia Pty Ltd (in liq) (No 2)*.[6] There was another matter, *ACCC v Bytecard Pty Ltd*,[7] but there are no published reasons for it since it was settled by consent orders. Similarly, *Europcar* was resolved by the parties submitting an agreed statement of facts and admissions whereby the respondent (which traded as Europcar) substantially admitted the allegations made by the ACCC. None the less, Gilmour J considered the law regarding UCT provisions in detail so as to be satisfied that he had the power to make the orders and declarations sought and that they were appropriate.[8] As a result, his Honour published detailed reasons.

There are decisions of the Federal Court, High Court and Supreme Court of Victoria concerning the unfair contract term provisions in the now repealed *Fair Trading Act 1999* (Vic) ('*Fair Trading Act*'). These are the Supreme Court decision of *Jetstar Airways Pty Ltd v Free* ('*Free*'),[9] the Federal Court decision of *Paciocco v Australia and New Zealand Banking Group Ltd*[10] ('*Paciocco*') and the Full Federal Court and High Court decisions concerning appeals from the *Paciocco* decision.[11] *Paciocco* considered s 32W of the *Fair Trading Act* for the period of 11 June 2009 to 1 July 2010[12] and *Free* considered it for the period of 9 October 2003 to 11 June 2009.[13] In *Paciocco*, s 32W was in the following form:

> A term in a consumer contract is to be regarded as unfair if, in all the circumstances, it causes a significant imbalance in the parties' rights and obligations arising under the contract to the detriment of the consumer.

In *Free*, s 32W was in the following form with underlining used to indicate how the provision is different from that considered in *Paciocco*:

> A term in a consumer contract is to be regarded as unfair if, contrary to the requirements of good faith and in all the circumstances, it causes a significant imbalance in the parties' rights and obligations arising under the contract to the detriment of the consumer.[14]

---

[2] Perhaps this is because, until 12 November 2016, the UCT provisions were limited to disputes concerning consumer contracts, which are more likely to be dealt with by administrative tribunals.
[3] (2016) ATPR 42-517; [2016] FCA 377.
[4] (2015) 239 FCR 33; [2015] FCA 1204.
[5] (2015) ATPR 42-498; [2015] FCA 368. The decision was upheld on appeal in *NRM Pty Corporation Pty Ltd v ACCC* (2016) ATPR 42-531; [2016] FCAFC 98.
[6] [2017] FCA 709.
[7] Proceeding number VID301 of 2013. See the orders made on 24 July 2013.
[8] *Europcar* [2016] FCA 377 [8]–[10].
[9] [2008] VSC 539.
[10] (2014) 309 ALR 249.
[11] (2015) 236 FCR 199 (Full Federal Court); and (2016) 333 ALR 569 (High Court).
[12] See *Paciocco* (2014) 309 ALR 249 [326]–[327] and [332]–[341].
[13] The impugned term in *Free* was entered into on 14 September 2006: see *Free* [2008] VSC 539 [5]. Section 32W of the *Fair Trading Act 1999* (Vic) was unchanged from 9 October 2003 to 11 June 2009.
[14] See *Free* [2008] VSC 539 [2].

It can be seen that the provisions considered in *Free* and *Paciocco* are different from the UCT provisions in the ACL. Further, the concept of transparency did not exist in the version of the *Fair Trading Act* considered in those cases. For these reasons, *Free* and *Paciocco* should be relied on with a degree of caution. However, in *Europcar*, Gilmour J referred to *Free* in detail and said it provided 'assistance in the interpretation and application' of the UCT provisions.[15]

III THE RELEVANCE OF 'TRANSPARENT' TO 'UNFAIRNESS'

It is submitted that transparency is defined in such a way that it is logically irrelevant to the second and third requirements of the definition of 'unfair' listed in s 24(1) of the ACL and of limited relevance to the first element. Each of the three requirements will be examined in turn below. For convenience, the party who is challenging an allegedly unfair term will be referred to as the 'plaintiff' and the party seeking to enforce it, the 'defendant'.

A *The First Requirement of 'Unfair': A Significant Imbalance in Rights and Obligations*

The first requirement for a term to be unfair is that it 'would cause a significant imbalance in the parties' rights and obligations arising under the contract'. This is stated in s 24(1)(a) of the ACL. Sirko Harder examined the role of transparency in the UCT provisions[16] and concluded:

> there is only one situation in which the requirements of unfairness set out in s 24(1) can easily accommodate considerations of transparency, and that is where the parties' rights and obligations directly depend upon the … [plaintiff] being aware of the term.[17]

Harder gave two examples of such a situation: first, a fixed-term contract which provides for its automatic extension unless one of the parties gives notice before the term expires and second, a contract for architectural work which prohibits the customer from making a claim for defective work unless they notify the architect of the defect within a certain time period.[18] In both of these examples, a time limit is being placed on the plaintiff's ability to exercise their rights. In the first example, the plaintiff's right to bring the contract to an end may be lost if notice is not given within a certain time while in the second example, the plaintiff's right to bring a claim is limited by a time bar.

1 *Situations Where the Parties' Rights and Obligations Depend on the Plaintiff Being Aware of the Term*

Situations 'where the parties' rights and obligations directly depend upon the … [plaintiff] being aware of the term'[19] can be broken into two categories. First, there are situations where a term limits a plaintiff's rights and second, situations where a term limits a plaintiff's ability to avoid an obligation. I will consider each in turn.

A plaintiff may be unaware of the limitation on their rights due to a lack of transparency in the term imposing the limitation. As a result, they may fail to abide by the limitation and lose a right. For example, as suggested above, a term could limit the time during which a plaintiff may

[15] *Europcar* [2016] FCA 377 [54].
[16] Sirko Harder, 'Problems in Interpreting the Unfair Contract Terms Provisions of the Australian Consumer Law' (2011) 34 *Australian Bar Review* 306.
[17] Ibid 319.
[18] Ibid 318.
[19] Ibid 319.

bring a claim for defective work. If the plaintiff is not aware of the term due to a lack of transparency, they may not bring a claim in time and hence lose their right to do so. This could cause 'a significant imbalance in the parties' rights and obligations arising under the contract' in two ways. First, the right may be lost, resulting to a situation where there is a significant imbalance. Second, the difficulty that the lack of transparency creates for the plaintiff in exercising their right may diminish the value of the right, leading to a significant imbalance. Returning to the example of a term concerning claims for defective work, the term may deprive the plaintiff of the right to bring an action, creating a situation where the defendant has a right to payment for the defective work and no obligation to repair it, while the plaintiff is obliged to pay for the defective work and has no right to have it repaired. This situation could amount to a 'a significant imbalance in the parties' rights and obligations arising under the contract', to quote s 24(1)(a). Alternatively, the limitation on the plaintiff's right to bring a claim for defective work could be viewed as devaluing the right, and leading to a significant imbalance. The transparency of the term is relevant to the significant imbalance in each scenario.

Dr Harder does not give an example of a situation where a term limits a plaintiff's ability to avoid an obligation, but one example would be a term that imposes a penalty on the plaintiff for breach or termination of the contract. Consider a situation where, due to the term lacking transparency, the plaintiff is unaware that it penalises them heavily for termination. The plaintiff terminates the contract believing they will only be liable for damages assessed at common law. Had they known they would be penalised, they would not have terminated. The plaintiff is now under an obligation to pay a significant penalty and has no right to receive the goods or services they contracted for from the defendant. By contrast, the defendant is under no obligation to provide the goods or services and has a right to be paid a windfall amount. Due to the plaintiff's ignorance of the term, resulting from a lack of transparency, a situation has arisen where there is a significant imbalance in the parties' rights and obligations. The same scenario could arise if the plaintiff were penalised for breach. It is important to note that in both cases the obligation of the plaintiff was contingent on an event, being termination or breach, and the plaintiff was able to avoid that event. Matters would be different if the plaintiff were unable to avoid the event and hence the significant imbalance would have arisen in any case. We will now consider the relevance of transparency in that situation.

2 *Terms Imposing Obligations*

Let us now consider a term which imposes an obligation which a plaintiff is unable to avoid through their own action. Such a situation would arise if, for example, a term imposed the evidentiary burden on the plaintiff for all matters in a proceeding arising from the contract.[20] Another example, may be a term that requires the plaintiff to indemnify the defendant for any loss suffered by the defendant whether the plaintiff contributed to that loss or not. It is submitted that in this situation, the transparency of the term is irrelevant to whether it would cause a significant imbalance in the parties' rights and obligations.

Due to a lack of transparency, a plaintiff may be unaware of an obligation prior to entering into a contract. Had they been aware of the obligation, they may have demanded an amendment to the contract so that the obligation was removed or lessened.[21] In this way, a lack of transparency has resulted in a term which imposes an obligation on the plaintiff being included in the

[20] Such a term is referred to in s 25(1) of the ACL which gives examples of terms that are potentially unfair.

[21] If the plaintiff is able to obtain an amendment to the contract, there may be an issue regarding whether the contract is a standard form contract, which is a requirement of the UCT provisions under s 23(1)(b).

contract. The existence of an obligation in itself will not result in a 'significant imbalance in the parties' rights and obligations arising under the contract'. Whether there is a significant imbalance will depend on an assessment of all the terms of the contract and their effect. A lack of transparency may provide an explanation as to why the plaintiff entered a contract containing an onerous obligation, but will have no bearing on whether there is in fact a significant imbalance. For this reason, it is submitted that transparency is irrelevant to whether a term imposing an obligation, which the plaintiff could not avoid, creates a significant imbalance.

This view is supported by case law which says the negotiation of a contract is irrelevant to whether there is a significant imbalance. In *Chrisco*, Edelman J clearly stated that he was proceeding 'on the basis that the lack of individual negotiation of the contracts' was irrelevant to determining whether there was a significant imbalance.[22] In *Free*, Cavanough J said 'individual negotiation of a term is not relevant to whether the term causes a significant imbalance'.[23] Cavanough J's view appears to have been endorsed in *Paciocco*.[24] The views regarding individual negotiation were expressed in *Free* and *Paciocco* notwithstanding that s 32X of the *Fair Trading Act* provided:

> Without limiting section 32W, in determining whether a term of a consumer contract is unfair, a court or the Tribunal may take into account, among other matters, whether the term was individually negotiated ….

A lack of transparency in a term imposing an obligation could be relevant in another way. Consider a situation where the term imposing the obligation is stated so vaguely that the defendant is able to lead the plaintiff to believe the obligation is more onerous than it actually is. The over-stated obligation may lead to a 'significant imbalance in the parties' rights and obligations arising under the contract'. This raises the question of whether the over-stated obligation is an obligation 'arising under the contract', as required by s 24(1)(a) of the ACL. On one view it is, since the over-stated obligation originated from a term in the contract and in that sense arose under the contract. On another view, the over-stated obligation did not arise under the contract but from a misinterpretation of the contract propounded by the defendant. Hence, it is the defendant's conduct and not the contract which is the source of the over-stated obligation. Depending on the answer to this question, the issue of whether transparency is relevant may not even arise because any significant imbalance in rights and obligations does not fall within s 24(1)(a) to begin with.

This scenario also raises a further question as to whether the term could fulfil the third requirement of unfairness, being that the term would cause detriment 'if it were to be applied or relied on'. The defendant would be *purporting* to rely on the term because they are actually relying on a misinterpretation of it. Due to the definition of 'rely on' in s 2 of the ACL, such purported reliance appears to be adequate. 'Rely on' is defined as including an 'attempt to exercise a right … *purportedly* conferred, by the term; [and to] assert the existence of a right … *purportedly* conferred, by the term' [emphasis added].

Regardless of how these two questions may be resolved, the above scenario is rather hypothetical for two reasons. First, if the term were challenged by the plaintiff, a court would determine the correct interpretation of the term. This would prevent the defendant from leading

[22] *Chrisco* (2015) 239 FCR 33 [50].
[23] *Free* [2008] VSC 539 [112].
[24] *Paciocco* (2014) 309 ALR 249 [331].

the plaintiff to believe they must comply with the over-stated obligation and hence there would be no need to resort to the UCT provisions. Second, it is more likely that a would-be defendant would draft a term that clearly imposes an obligation so as to avoid any need for exaggeration. A lack of transparency in a term imposing an obligation could be relevant as an indicator of a significant imbalance. This view appears to be propounded in the Explanatory Memorandum to the Trade Practices Amendment (Australian Consumer Law) Bill 2010 (No 2) ('Explanatory Memorandum'), which introduced the UCT provisions. It addresses transparency as follows:

> A lack of transparency in the terms of a consumer contract may be a *strong indication* of the existence of a significant imbalance in the rights and obligations of the parties under the contract.[25]

It is submitted transparency has little to no relevance as an indicator of whether a term creates a significant imbalance. The logic underlying the statement quoted above is somewhat unclear. Perhaps the logic is that if a term creates a significant imbalance, a defendant may try to conceal it from the plaintiff by not making it readily available to them or obscuring it with unclear drafting. This logic assumes the following:

- The defendant performed a proper construction of the contract and concluded that the term gave rise to a significant imbalance or might do;
- As a result of this conclusion, the defendant decided to obscure the term so that the plaintiff could not become aware of the significant imbalance; and
- In light of the defendant's conduct, the court should feel greater comfort in concluding that the term gives rise to a significant imbalance.

There are several problems with this logic. First, it assumes that the defendant is capable of performing a process of legal reasoning concerning whether a term creates a significant imbalance with such a level of precision that the court ought to give weight to it when performing its own reasoning. There is no basis for this assumption. In some circumstances, deliberate conduct by a defendant may be a reliable indication of whether a particular legal test has been fulfilled but not in the present case. For example, a court may more readily conclude that conduct was misleading or deceptive in breach of s 18 of the ACL if the defendant intended to mislead the plaintiff.[26] For misleading or deceptive conduct, there is a clear connection between someone intending to mislead and actually achieving that end, but there is no similar connection between concealing a term and that term causing a 'significant imbalance in the rights and obligations … under the contract'.

Second, the logic assumes that the defendant has deliberately deprived the term of transparency. The term may lack transparency due to careless drafting by the defendant, the defendant simply

[25] Explanatory Memorandum, Trade Practices Amendment (Australian Consumer Law) Bill 2010 (No 2) (Cth) [5.38] [emphasis added], quoted in *Chrisco* (2015) 239 FCR 33 [72].

[26] See *Campomar Sociedad, Limitada v Nike International Ltd* (2000) 202 CLR 45 [33], referred to subsequently in *National Exchange Pty Ltd v ASIC* (2004) 49 ACSR 369 [28] (Full Federal Court); *Veda Advantage Limited v Malouf Group Enterprises Pty Limited* [2016] FCA 255 [204]; *Verrocchi v Direct Chemist Outlet Pty Ltd* [2015] FCA 234 [91]; *Samsung Electronics Australia Pty Limited v LG Electronics Australia Pty Limited* [2015] FCA 227 [91]; *Telstra Corporation Limited v Phone Directories Company Pty Ltd* [2014] FCA 568 [489]; *Owston Nominees No 2 Pty Ltd, Clambake Pty Ltd* (2011) 248 FLR 193 [227] (WA Court of Appeal); *James Hardie Industries NV v Australian Securities and Investments Commission* 274 ALR 85 [245] (NSW Court of Appeal); and *National Exchange Pty Ltd v ASIC* (2004) 49 ACSR 369 [28] (Full Federal Court).

forgetting to make it available to the plaintiff or it being impossible to draft the term 'in reasonably plain language' due to the complexity of the subject matter it addresses.

Another way to look at how transparency may indicate a significant imbalance is to say that if a term is clearly disclosed to the plaintiff, it is unlikely to cause a significant imbalance because the plaintiff would presumably not accept a term which is significantly against their interests. This approach is also problematic. It assumes the plaintiff can perform a process of legal reasoning concerning whether a term creates a 'significant imbalance'. It also assumes that the plaintiff understood the term and made an entirely free choice to accept it.

3 *Terms Granting Rights*

Let us now consider a term which grants a right to the plaintiff. Due to a lack of transparency, a plaintiff may be unaware of a term granting them a right and hence be unable to exercise that right. If the right offsets an obligation imposed on the plaintiff by another term or a right granted to the defendant, the inability of the plaintiff to exercise the right may create a significant imbalance. For example, consider a term that allows the defendant to vary the contract unilaterally, and a second term that permits the plaintiff to strike out the variation provided they notify the defendant of their objection within a set time. If the plaintiff is unaware of the second term due to a lack of transparency, they will be unable to exercise their right to prevent the variation.

It is important to note that s 24(2)(a) does not mandate transparency as a consideration in this situation. Section 24(2)(a) requires the transparency of the allegedly unfair term to be considered, but *not* the transparency of another term which is *not* allegedly unfair.[27] The present example involves considering the transparency of an unchallenged term in order to determine whether a challenged term is unfair. However, a court may consider the transparency of a term granting a right even though it is not challenged by the plaintiff. This is because s 24(2) permits a court to 'take into account such matters as it thinks relevant' when determining whether the impugned term is unfair and requires it to consider the contract as a whole.

Let us now consider a term that grants a right to the defendant; for example, a right to unilaterally vary the contract, change the nature of the services or goods to be provided under the contract or terminate the contract without notice. This scenario is similar to that where a term imposes a heavy obligation on the plaintiff, which was considered above. A lack of transparency may explain why the plaintiff entered into a contract granting the defendant a far-reaching right, but will have no bearing on whether there is in fact a significant imbalance in rights and obligations. A slightly different scenario would be a term that grants a far-reaching right to the defendant but also grants the plaintiff the right to limit the defendant's exercise of the right: for example, a term that allows the defendant to vary the contract unilaterally but also allows the plaintiff to strike out the variation, provided they give the defendant notice of their objection within a set time. In that scenario, transparency would be relevant to whether there is a significant imbalance because the plaintiff cannot exercise their right unless they are aware of the term. This is much the same as the scenario considered above, where the plaintiff's right to bring a claim for defective work is subject to a time bar.

[27] *Chrisco* (2015) 239 FCR 33 [43].

B *The Second Requirement of 'Unfair': Protection of a Legitimate Interest*

The second requirement for a term to be unfair is that it is 'not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term'.[28] It is submitted that transparency is irrelevant to determining what the legitimate interests of the defendant are and irrelevant to whether the term is reasonably necessary to protect those interests. The legitimate interests of a party cannot be influenced by the clarity with which a term is drafted or its availability to another party. Those interests are determined by the nature of the party's business and the industry it operates in.

When determining whether a term is 'reasonably necessary in order to protect' a legitimate interest, the primary questions are (i) what rights and obligations does the term create, and (ii) are those rights and obligations reasonably necessary to protect the legitimate interest? It is submitted that transparency is irrelevant to answering these questions. As for the first question, the rights and obligations granted by the contract will be determined by a proper interpretation of the contract and not how clearly it is drafted. As for the second question, whether those rights and obligations go beyond protecting a legitimate interest will be determined by considering the scope of the rights and obligations, the scope of the legitimate interest and whether the rights and obligations go beyond protecting that interest.

There is perhaps a secondary matter to consider: if the term does protect a legitimate interest, has the term been *expressed* in a way that is reasonably necessary in order to protect that interest? To put things another way, could the term have been expressed more simply and still achieved the same end? Consider a situation where a defendant operates in a complex environment. In those circumstances, a term that protects its legitimate interests may need to be so complex that it is difficult or impossible to express in plain language. It is submitted that transparency is not relevant to determining whether the term could have been expressed more simply. That issue will be determined by the degree of complexity of the environment and how a drafter could respond to that complexity.

C *The Third Requirement of 'Unfair': Detriment*

The third requirement for a term to be unfair is that it 'would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on'.[29] It is difficult to conceive of a situation where transparency would be relevant to whether a term causes the plaintiff detriment. The consequences of a term being applied or relied on depend on the rights the term grants to the defendant and the obligations it imposes on the plaintiff. These matters are not affected by the clarity with which the term is expressed but by the proper interpretation of the term. A lack of clarity will not prevent a court from interpreting the term unless it is so vaguely expressed that it is void for uncertainty, in which case it will not be a source of rights or obligations for any party.

Transparency may at first appear to be relevant to detriment in two rather hypothetical situations, but on further analysis, it is submitted that it is not.

[28] ACL, s 24(1)(b).
[29] ACL, s 24(1)(c).

The first situation was identified by Harder who said that detriment could take the form of the plaintiff being surprised or angered on becoming aware of a non-transparent term.[30] He dismissed this argument for two reasons. First, the detriment must be caused by the defendant applying or relying on the term. The plaintiff would usually become aware of the term before it is relied on. Hence, the defendant's applying or relying on the term would not cause the surprise or anger, rather *the plaintiff's discovery* of the term would be the cause.[31] Second, for the purposes of s 24(1)(c), the detriment must result from the actual effect of the term and not the discovery of it.[32]

It is submitted that Harder is correct but some additional observations can be made. First, the primary cause of the plaintiff's surprise or anger upon discovering the term is its initial concealment by the defendant rather than the discovery of the term by the plaintiff, which is a secondary matter. As Dr Harder noted, it is the defendant's reliance or application of the term which must cause the detriment. The concealment by the defendant is a different act from relying on or applying the term. Second, the Explanatory Memorandum states that the detriment must be caused 'by the practical effect of the term'.[33] This supports Harder's second argument. It is submitted that the practical effect of the term is the effect it has on the parties' rights and obligations and not an incidental effect it may have on a party's emotions. Third, a situation where a plaintiff tries to rely on surprise or anger to fulfil the requirement of detriment is quite hypothetical. A plaintiff will need to suffer some non-emotional detriment if they are to establish that the term would cause a 'significant imbalance in the rights and obligations of the parties arising under the contract', as required by s 24(1)(a). The plaintiff is likely to rely on this non-emotional detriment to fulfil the requirement of s 24(1)(c) as well, rather than resort to relying on feelings of surprise or anger.

The second situation where transparency could be relevant to detriment is where the transparency of the term affects the *extent* of the detriment suffered by the plaintiff. As noted above, a vaguely drafted term may allow a defendant to over-state the plaintiff's obligations. In this way, transparency could affect the extent of the detriment. However, s 24(1)(c) is not concerned with the extent of detriment, only whether there is detriment. Hence, transparency could not be relevant in this way.

In light of the above, it is submitted that transparency is not relevant to whether a term 'would cause detriment … to a party if it were to be applied or relied on'.

D *Summary*

In summary, transparency is of limited relevance to the first requirement of the test for unfairness, being whether the term would cause 'a significant imbalance in the parties' rights and obligations arising under the contract'. It is irrelevant to the two remaining requirements of the test: whether the term is reasonably necessary to protect a legitimate interest of the defendant, and whether it would cause detriment to the plaintiff if it were relied on. For the first requirement, transparency is only relevant in situations where the plaintiff's rights and obligations depend on their knowledge of the allegedly unfair term. As explained above (see heading *Situations Where the Parties' Rights and Obligations Depend on the Plaintiff Being*

[30] Harder, above n 16, 319.
[31] Ibid.
[32] Ibid.
[33] Explanatory Memorandum [5.33]; see also [5.32].

Aware of the Term), such a situation will arise if (i) a term places a limitation on a right of the plaintiff and the plaintiff would be able to avoid that limitation, or (ii) a term imposes an obligation on the plaintiff, which is subject to the occurrence of an event that the plaintiff would be able to avoid. There will be many terms outside these scenarios such as terms that (i) impose an obligation on the plaintiff, which is not subject to the occurrence of an event, or (ii) grant a right to the defendant.

IV WHAT ROLE SHOULD TRANSPARENCY PLAY IN THE UCT PROVISIONS?

Given the limited relevance of transparency, what role should it play in the UCT provisions? It is submitted that transparency should not continue as a mandatory consideration for assessing unfairness because of its limited relevance. As a matter of logic, it is unsatisfactory to mandate a consideration which is largely irrelevant, but more importantly, it is practically undesirable. This is because (i) it is an inefficient use of the courts' and parties' resources to address a consideration that is largely irrelevant, and (ii) there is a risk that the consideration could lead to incorrect outcomes. The latter is of greater concern.

The Explanatory Memorandum clearly states that transparency is not determinative of unfairness:

> Transparency, on its own account, cannot overcome underlying unfairness in a contract term. Furthermore, the extent to which a term is not transparent is not, of itself, determinative of the unfairness of a term in a consumer contract and the nature and effect of the term will continue to be relevant.[34]

This was accepted in *Chrisco*.[35] However, there remains a real risk that the test for unfairness may be distorted by the inclusion of a largely irrelevant consideration. This is for two reasons. First, transparency is given greater weight in the ACL than it deserves, due to its being one of only two mandatory considerations. This is particularly so when the other mandatory consideration, being the requirement that a court consider the contract as a whole, is so trite that it adds little guidance. Further, the Explanatory Memorandum says that a 'lack of transparency may be a *strong indication* of the existence of a significant imbalance in the rights and obligations of the parties under the contract.[36] This statement was noted in *Chrisco*.[37]

Second, the test for transparency is more easily applied than the test for unfairness, and hence it is tempting for a decision maker to rely heavily upon it when determining unfairness. One of the requirements of the test for unfairness is whether the term causes a significant imbalance in the rights and obligations arising under the contract. Fair minds may easily differ on what amounts to a significant imbalance, but there is less likely to be a difference of views about transparency, since it turns on matters which are more objective, such as plainness of expression and the availability of the term. Hence, a conclusion regarding unfairness that is based largely on transparency is less likely to appear idiosyncratic.

If transparency is not a mandatory consideration for determining 'unfairness', what role should it play? There are four options.

---

[34] Explanatory Memorandum [5.39].
[35] *Chrisco* (2015) 239 FCR 33 [43].
[36] Explanatory Memorandum [5.38] [emphasis added].
[37] *Chrisco* (2015) 239 FCR 33 [72].

A *Add Transparency to the Test for 'Unfairness'*

The first option is to incorporate transparency into the test for unfairness in s 24(1) as a new fourth requirement so that a term is only unfair if it is not transparent. A term would still have to fulfil the existing three requirements to be unfair. If this option were adopted, it would be a substantial change to the test for 'unfairness'. Whether this is appropriate depends on what the test for unfairness is intended to achieve.

The Explanatory Memorandum states that the UCT provisions are based on the recommendations made by the Productivity Commission in its report *Review of Australia's Consumer Policy Framework* ('PC Report'),[38] suggesting the test for unfairness is intended to implement the recommendations of the Productivity Commission. The PC Report recommended that a term be declared unfair if (i) contrary to the requirements of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract and (ii) it would cause material detriment to consumers either individually or as a class.[39] It recommended that when deciding whether a term is unfair, a decision-maker must consider 'all of the circumstances of the contract' and take into account 'the broader interests of consumers, as well as the particular consumers affected.'[40] The recommendations did not mention transparency or a similar concept.

It is submitted that including transparency as a fourth requirement in the test of unfairness would depart from the Productivity Commission's recommendation, which was the foundation for the introduction for the UCT provisions. The PC Report is a comprehensive document devoting approximately 60 pages to the consideration of unfair contract terms. It was the culmination of over 16 months of work from the release of the terms of reference on 11 December 2006 to the release of the report on 30 April 2008. In preparing its Report, the Productivity Commission released a draft report for consultation, received over 250 written submissions, met with over 70 individuals and organisations within Australia, and met with governments, consumers and businesses in several other countries.[41] Hence, one should be slow to depart from its recommendations until an equally comprehensive review of consumer protection policy is undertaken.

The fact the PC Report did not mention transparency in its recommendation is a further reason for removing transparency as a mandatory consideration for determining unfairness in the ACL.

B *Specify Transparency as a Discretionary Consideration*

A second option is for transparency to be referred to in the ACL as a discretionary consideration for determining unfairness. Referring to transparency as a discretionary consideration is preferable to making it a mandatory consideration because then a court will only consider it when it is relevant. However, since transparency will be irrelevant on many occasions, there seems little point in giving it specific mention. If it is specifically mentioned, we might as well refer to various other matters that might be relevant on some occasion. Further, the list of

[38] Explanatory Memorandum [5.3].
[39] Productivity Commission, *Review of Australia's Consumer Policy Framework*, Report No 45, Vol 2, (2008) 168.
[40] Ibid.
[41] Ibid 14.

contractual terms which are potentially unfair, in s 25 of the ACL, already gives a court sufficient guidance on what may be unfair.

The ACL could make transparency a mandatory consideration for the element of the test for unfairness contained in s 24(1)(a)—whether there is a significant imbalance in the parties' rights and obligations. As noted above, transparency may be relevant to this element on some occasions. However, since it will be irrelevant on many other occasions, it is preferable that transparency is not a mandatory consideration.

C *Adopt a Broad Test for 'Unfair'*

As already noted, the test for whether a term is unfair in s 24(1) is quite specific. The test is not cast in broad terms, such as a 'term will be unfair if it is unfair in all the circumstances'. This can be contrasted with the prohibition on unconscionable conduct in s 21 of the ACL, which provides that a person must not 'engage in conduct that is, in all the circumstances, unconscionable'. The transparency of a term would be relevant to whether the term is unfair under a broad test. For example, a term could be judged unfair if it was so unclear that a plaintiff could not understand what it required of them.

A comprehensive analysis of whether a broad test for unfairness is desirable is beyond the scope of this paper, but a few points can be made. First, a broad test may give greater latitude to the subjective views of the decision-maker and hence create a risk of idiosyncratic decision-making. This could lead to greater uncertainty for contracting parties about whether terms in their contract will be enforceable. Even if idiosyncratic decision-making does not eventuate, the perception of such a risk could still create a sense of uncertainty among contracting parties. Second, the common law will not invalidate a term simply because it is unfair.[42] Hence, a broad test for unfairness would be a significant departure from common law principles. Third, a broad test for unfairness was not recommended by the PC Report.

D *Create a Separate Prohibition on Terms Lacking Transparency*

The PC Report does not address a specific prohibition on terms which lack transparency or are unclear by some other definition, although such a prohibition is not unprecedented. One previously existed in the now repealed *Fair Trading Act* and another currently exists in the *Consumer Rights Act 2015* (UK) (*Consumer Rights Act*).

Section 163 of the *Fair Trading Act* specified minimum requirements regarding clarity for a consumer contract. Unlike the UCT provisions, a consumer contract did not need to be a standard form contract for the purposes of s 163.[43] Section 163(3) required a consumer contract to be 'easily legible', use a font of no less than 10 points if it is printed or typed, and be 'clearly expressed'. Section 163(4) permitted the Director of Consumer Affairs Victoria to apply to the Victorian Civil and Administrative Tribunal or a court for an order that a provision did not comply with s 163(3).[44] If the Tribunal or court was satisfied that it did not comply, it could

[42] *Europcar* [2016] FCA 377 [47], citing *Biotechnology Australia Pty Ltd v Pace* (1988) 15 NSWLR 130, 132–3 (Kirby P); *Woolworths Ltd v Kelly* (1991) 22 NSWLR 189, 193–4; Elizabeth V Lanyon, 'Equity and the Doctrine of Penalties' (1996) 9 *Journal of Contract Law* 234, 250.

[43] See *Fair Trading Act* s 3.

[44] Originally, the application could only be made to the Tribunal but this was altered to include a court, with effect from 30 May 2007, by the *Fair Trading and Consumer Acts Amendment Act 2007* (Vic).

order that a supplier not use the provision in the same or similar terms in consumer contracts. There was no right for a person other than the Director to seek such an order.

Section 68 of the *Consumer Rights Act* requires a term in a consumer contract to be transparent, which is defined as 'expressed in plain and intelligible language' and 'legible'. If a term is not transparent, the regulator may apply for an injunction in relation to it.[45] Section 68 is clearly comparable to s 163 of the *Fair Trading Act*. However, the *Consumer Rights Act* contains another provision, in s 69, which does not have an equivalent in the *Fair Trading Act*. Section 69 of the *Consumer Rights Act* provides that if a term in a consume r contract 'could have different meanings, the meaning that is most favourable to the consumer is to prevail'. Unlike the UCT provisions, neither s 68 or s 69 is limited to standard form contracts.[46]

The main issue is whether there is a need for a provision akin to s 163 of the *Fair Trading Act* or s 68 of the *Consumer Rights Act* in the ACL. A comprehensive analysis of this issue is beyond the scope of this paper, but a few points can be made. First, s 163 existed from 27 May 2003 until 19 October 2010. In that seven-year period, it appears to have only been relied on seven times.[47] This suggests it may be unnecessary. Second, the PC Report did not contain a recommendation that such a provision be included in the ACL. Third, the risk of people being misled by unclear terms is already addressed to an extent by the prohibition in s 18 of the ACL on conduct that is likely to mislead.

V CONCLUSION

Section 24(2) of the ACL provides that when a court is determining whether a term is unfair it may take into account such matters as it thinks relevant, but *must* take into account the extent to which the term is transparent and the contract as a whole. It is submitted that s 24(2) should be removed. A court does not need to be told to consider such matters as it thinks relevant or the contract as a whole. Further, transparency should cease to be a mandatory consideration for three reasons. First, it is of limited relevance to determining whether a term is unfair. Second, the recommendation in the PC Report, which was the basis for the introduction of the UCT provisions, made no mention of transparency. Third, retaining transparency as a mandatory consideration is undesirable since it is logically unsatisfactory to mandate a consideration of limited relevance and practically undesirable because there is a risk that it could lead to incorrect outcomes when the test of unfairness is applied. Transparency could play some role in the ACL but this would require an amendment to the legislation. For example, transparency could be part of a new prohibition on unclear terms or it could be relevant if the test for unfairness was amended to a broad test instead of the narrow test that currently exists.

---

[45] *Consumer Rights Act* sch 3 cl 3.

[46] See *Consumer Rights Act* sub-ss 61(1) and (3).

[47] See *Director of Consumer Affairs Victoria v Australian Tourism Centre Pty Ltd* [2010] VSC 571; *Director of Consumer Affairs v Parking Patrols Vic Pty Ltd* [2012] VSC 137; *Director of Consumer Affairs v Palamara* [2012] VSC 311; *Director of Consumer Affairs v AAPT Ltd* [2006] VCAT 1493; *Director of Consumer Affairs Victoria v Craig Langley Pty Ltd & Matrix Pilates and Yoga Pty Ltd* [2008] VCAT 482 and [2008] VCAT 1332; *Director of Consumer Affairs Victoria v Trainstation Health Clubs Pty Ltd* [2008] VCAT 2092; and *Director of Consumer Affairs Victoria v Backloads.com Pty Ltd* [2009] VCAT 754. Section 163 has also been referred to in three proceedings brought by private litigants: *Braithwaite v GH Operations Pty Ltd* [2007] VCAT 415; *Elliott v Simonds Homes Pty Ltd* [2010] VCAT 1827; and *Worthing v Advance Heating & Cooling Pty Ltd* [2014] VCAT 1532, but, as noted, only the Director of Consumer Affairs can rely on s 163.

Editorial

Articles – Special Issue

Articles – General Issue