



Personal Insolvency Task Force

Groupe de travail sur l'insolvabilité personnelle

THE PURPOSE OF THIS PAPER

The purpose of this paper is to establish operating terms of reference for the Personal Insolvency Task Force (PITF).

In addition to the five year review planned for 2002, when the Office of the Superintendent of Bankruptcy (OSB) must report to Parliament on the 1997 Reforms, the single most important event giving rise to this task force is the rapid escalation in the number of personal bankruptcies over the years.

THE FUNDAMENTAL PURPOSE OF BANKRUPTCY LEGISLATION

The fundamental purpose of bankruptcy legislation is and remains that of protecting and maximizing the realization in an insolvent estate by liquidating the debtor's assets and by distributing its proceeds amongst his/her

creditors quickly and efficiently.

However, in today's society, where consumer debtors have no, or very little, assets to be liquidated the purpose of bankruptcy legislation takes on a new meaning. Personal insolvency and bankruptcy may be viewed more in socio-economic terms rather than strict legal terms.

BACKGROUND

A little history

The *Constitution Act* of 1867 conferred upon Parliament exclusive jurisdiction to enact laws in relation to "bankruptcy and insolvency". Canada's first insolvency Act, which only applied to traders, was adopted in 1869 and was replaced by a later Act in 1875.

The *1875 Act* was widely criticized and repealed in 1880. Between 1880 and 1919, Canada had no general bankruptcy legislation at all. In 1882, the federal government adopted winding up legislation for insolvent trading corporations and other corporate

enterprises¹. The first insolvency Bill was enacted in 1919. The *1919 Act* was heavily influenced by the *British Bankruptcy Act 1883*, and its general conceptual structure. In 1949, the *1919 Act* was extensively revised. A number of proposals for new revisions were presented by a federal Study Committee in 1970, yet despite the introduction of several bills between 1975 and 1984, the proposals were never adopted.

What's Been Done Thus Far...

\$ The 1992 Amendments

In 1992 a number of important amendments were made to streamline the process by removing from the judicial process the procedure for the handling of discharges for personal bankrupts by introducing the concept of *automatic* discharges for first-time bankrupts where no opposition was made by the trustee, the Superintendent or creditors. These amendments further recognized the need for debtor rehabilitation by introducing the concept of counselling. As well, the amendments afforded insolvent debtors an alternative to bankruptcy by introducing a separate regime for the making of consumer proposals.

\$ The 1997 Amendments

The 1997 amendments were primarily focused on making high-income debtors aware of their responsibilities by introducing significant changes to the treatment of consumer bankruptcies. Former section 68 of the *BIA* was repealed and replaced with new section 68 which requires high-income debtors, between the time of bankruptcy and the time of their discharge, to pay over their surplus income based on standards issued by the Superintendent of Bankruptcy. The concept of compelling high-income debtors to pay over their surplus income to the trustee was intended to provide a way of precluding an automatic discharge of such debtors in cases where they failed to comply with Section 68.

\$ The National Insolvency Forum Report

In May and June 1999, through a series of round table discussions held in six selected cities across Canada, primary stakeholders of the insolvency system were asked to voice their opinions on what works, what doesn't work and how the existing insolvency system could be streamlined to be more efficient and cost-effective. A summary of each round-table discussion was published in the fall of 1999, all of which are available by consulting our Web site at <http://osb-bsf.ic.gc.ca>. Some of the suggestions

1 Houlden & Morawetz, *Bankruptcy Law of*

Canada, Third Edition, Carswell, p.1-1

include:

❖improve compliance measures by addressing the lack of deterrent mechanisms for trustees who fail to maintain professional obligations (e.g., verifying the debtor's statement of affairs) and debtors who do not comply with their duties and obligations under the *BIA* (e.g., declaring all their assets);

❖simplify the procedure and requirements for Summary Administration Estates, making them less time-consuming and less expensive to comply with for debtors with few assets and no surplus income;

❖incorporate a hardship clause in paragraph 178(1)(g) which refers to student loans.

Where We Are Now...

Despite predictions made by government and economists to the effect that a strong economy would translate into a decrease in personal bankruptcies in the late 1990's, the actual rate of consumer bankruptcies in fact peaked in 1997 and has decreased only slightly since².

Overall, the number of bankruptcies has been increasing exponentially over the last 35 years. In 1966, business bankruptcies represented the majority of all bankruptcies reported in Canada (i.e., 59.3%), whereas consumer bankruptcies represented 41%. Five years later, in 1971, consumer bankruptcies accounted for 50.5% whereas business bankruptcies accounted for 49.5% of all bankruptcies reported. This trend has continued throughout the 70's, 80's and 90's with consumer bankruptcies reaching an all time high of 87.9% in 1999. Recent statistics reported by the Bank of Canada show that the debt-income-ratio (% total household debt/personal disposable income) was at 99.9% in 1999.

The current profiles of insolvencies reveal that consumer proposals are on the rise, whereas bankruptcies appear to remain stable in spite of the fluctuations in the economy. Statistics show that in 1999, 72,997 Canadians declared bankruptcy; 90% or more of consumer bankrupts declare total assets with less than \$10,000, thus qualifying the estate for summary administration; 85% or more have incomes at or below the prescribed low income cost of living at which they are required to make payments

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A number of studies conducted in 1998 and 1999 present various explanations and/or rationales for the rapid escalation in the number of consumer bankruptcies^B see *Symposium Consumer Bankruptcies in a Comparative Context*, Osgoode Hall Law

Journal, Volume 37, Numbers 1 & 2, Spring & Summer 1999.

to the trustees pursuant to section 68 of the *BIA*.

PITF's MANDATE

PITF has been established to review the provisions of the *Bankruptcy and Insolvency Act (BIA)* as it pertains to personal bankruptcies. Starting without preconceived notions, PITF will explore alternative models of personal insolvency processes better geared towards addressing the perceived weaknesses of our Canadian insolvency system. In doing so, PITF will also review expectations of both debtors and creditors while factoring in the general public interest.

PITF's OBJECTIVE

PITF's objective is to formulate recommendations for an alternative insolvency process and/or redress mechanisms to the existing process in order to ensure:

\$ that Canada's highly privatized bankruptcy system, which was designed for debtors with assets and/or income can nevertheless remain accessible to debtors with little or no assets and/or income;

\$ the appropriateness of low-income debtors paying even a modest fee to obtain a *fresh start* while being subject to the same procedural process as those

with high income and/or assets;

\$ that bench marking is incorporated into the recommendations and that best practices from other countries such as Australia, USA and UK are drawn on to improve the efficiency and effectiveness of Canada's insolvency system.

PITF will also identify the desirable legislative changes to the Canadian insolvency system and recommend appropriate mechanisms to ensure that:

low-income debtors are discharged in a fair and efficient manner, having regard to the legitimate and frequently competing interest of various stakeholders representing, in turn, various societal interests.

the issue of post-bankruptcy revenues is clarified and addressed in a cohesive manner in the *BIA*;

trustees are afforded appropriate and fair remuneration for their professional services;

stakeholders and practitioners are afforded electronic means of communications and *e-commerce*;

debtors' assets are evaluated in a just manner and their realization maximized in an insolvent estate;

all procedures in personal bankruptcies are streamlined and reduced without jeopardizing the integrity of the system;

bankrupts with no surplus income or seizable assets are dealt with as efficiently as possible.

PITF's CRITERIA

Criteria against which PITF must prioritize the issues to be examined and serve as the measure against which final recommendations must be gauged are:

Fairness: is a function of what the system appears to be to on-lookers, whether or not they are familiar with the system.

Accessibility: going bankrupt in Canada must be seen as a right, not a privilege.

Accordingly, access to the system must be simple, inexpensive and readily available throughout the country.

Predictability: debtors and creditors understand what the result of the process will be—consistency.

Efficiency: the social cost of the system and its economic cost are directly related to its efficiency. This raises questions about whether a trustee needs to be involved in every aspect of a personal insolvency and, more generally, whether the system as a whole is as efficient as it could or should be.

Responsibility: the system should encourage social and economic responsibility of both debtors and credit grantors.

Understandability: is the process itself, and are the results of the process, transparent and comprehensible to each of the debtor and the creditors?

Effectiveness: deals with whether the insolvency system is responsive to the perceived needs of its users and whether it is consistent with the rest of the socio-economic fabric of the country.

THE PITF TEAM

Structure

PITF is comprised of a broad base constituency of stakeholders with a strong interest in the subject matter; namely creditors and/or creditor representatives, debtor representatives, members of the judiciary, trustees, a member of the Canadian Insolvency Practitioners Association as well as a number of academic scholars in the field of Bankruptcy Law.

Meetings

A series of four or five meetings of the Task Force will be held over the course of the next year. In addition, five sub-groups have been created. These sub-groups will be called upon to deal with, and make recommendations to the Task Force, in specific subject areas.

Results

A comprehensive Report outlining strong rationales supporting recommendations for changes to the *BIA*, its *Rules* and *Directives*, including other relevant aspects of the insolvency system. In addition, the Report will also serve as a form of bench marking by positioning Canada and comparing the Canadian insolvency system with that of Australia, USA and the UK while respecting the fundamental policy and flavor which characterize the personal insolvency system in Canada. The final Report will be published to elicit further public discussion before final recommendations are made to the Minister.

Method of Payment of Members

Members of the task force will conduct their duties *pro bono*. Their expenses, however, will be paid by the OSB.