Consumer Credit
Legal Centre NSW

November 2009

Submission to the Senate Legal & Constitutional Affairs Committee

in response to the

BANKRUPTCY LEGISLATION AMENDMENT BILL 2009

Consumer Credit Legal Centre (NSW) Inc

Consumer Credit Legal Centre (NSW) Inc ("CCLC") is a community-based consumer advice, advocacy and education service specialising in personal credit, debt and banking law and practice. CCLC operates the Credit & Debt Hotline, which is the first port of call for NSW consumers experiencing financial difficulties. We provide legal advice and representation, financial counselling, information and strategies, and referral to face-to-face financial counselling services, and limited direct financial counselling. CCLC also operates the Insurance Law Service, a national service assisting consumers with disputes with their insurance company. CCLC took over 15,000 calls for advice or assistance during the 2008 financial year.

A significant part of CCLC's work is in advocating for improvements to advance the interests of consumers, by influencing developments in law, industry practice, dispute resolution processes, government enforcement action, and access to advice and assistance. CCLC also provides extensive web-based resources, other education resources, workshops, presentations and media comment.

Thank you for the opportunity to make submission in relation to this Bill. While CCLC is largely supportive of this Bill we have serious concerns about the extension of the availability of debt agreements prior to a review of the amendments in this area due to occur next year. Our concerns are detailed at section (f) commencing on page 7 below.

PROPOSED CHANGES TO THE BANKRUPTCY ACT 1966

(a) Item 11 – repeal of section 161B(2))

CCLC strongly supports the repeal of these sections for the reasons stated in the Explanatory Memorandum.

(b) Item 13 – appeal and replacement of section 167, review of remuneration and costs

CCLC supports this change. Trustee fees can be very high in proportion to the bankrupt's debts with punitive consequences. Examples of callers to CCLC who have been adversely affected include:

- Callers who are basically solvent but have been made bankrupt in their absence (for example while overseas or seriously ill) and wish to annul the bankruptcy, but are faced with high fees, often multiples of the amount of the original debt or debts;
- Callers who have entered bankruptcy as a result of poor advice and wish to annul the bankruptcy and face the same challenges;

- Callers who have been made bankrupt as a result of a relatively small unsecured debt (but larger than the proposed new threshold) and own or are purchasing their home – these debtors not only lose their homes, but potentially also considerable equity as a result of trustees fees.

We refer also to Case Studies 2 and 3 below.

While trustees are entitled to remuneration, the bankrupt should be entitled to a review these costs in appropriate circumstances to ensure they are reasonable. We particularly support that the review process will be free to the applicant. Further, we submit that the review should not be narrow and technically construed, but should consider the overall fees and costs claimed and whether they are reasonable in all the circumstances.

(c) Removal of bankruptcy districts

We have no comment on the removal of bankruptcy districts provided that:

- There is no impact on the collection, publication, and analysis of historical data on a State by State basis, for example;
- There is no adverse impact on debtors, such as requiring them to appear in courts to defend proceedings that are distant from their place of residence.

(d) Increase the minimum debt for a creditor's petition to $10,000.

CCLC strongly supports this change.

The size of consumer debts carried by consumers has increased significantly in recent years as a result of freely available consumer credit. A 2006 analysis of CCLC callers in relation to credit card debt revealed that 844 callers on government benefits alone owed over $3,000 on credit cards and store cards, 38 people on low incomes (under $26,000) owed over $33,000, and 192 callers (of varying income levels) owed over $40,000 in credit card debt.

There has also been an increase in the number of creditors using bankruptcy inappropriately as a means of enforcing payment on relatively small debts. There are other enforcement options available in the case of these smaller debts including garnishees and writs for levy of property in NSW (against both goods and real estate). CCLC has received calls from debtors who are facing bankruptcy, and all the attendant disadvantages of loss of their primary place of residence and possibly tens of thousands of dollars in trustee fees, over relatively small debts such as phone bills and credit card accounts. CCLC is aware of one bank, and a number of debt collectors who use bankruptcy proceedings, not as a last resort but instead without first exhausting other enforcement options. This is particularly harsh in the case of smaller debts, especially where the only asset is usually the debtor's home.

However, CCLC would suggest that the minimum debt amount relate to the original debt owed, not to the debt owing at the time the petition is presented (for Creditor's Petitions) or the debt owing under the final judgment or order (for Bankruptcy Notices). At a bare

minimum the debt for the purposes of the threshold must be exclusive of legal fees at the time of judgment. This would ensure that creditors must try other enforcement options to collect smaller debts, rather than simply wait until sufficient interest and legal fees have accumulated and use the punitive bankruptcy process.

The following case studies were collected by CCLC in the last few months in order to advocate for improvements in the rights of unit owners who need more time to pay their strata management fees/levies. These cases demonstrate both the punitive consequences of bankruptcy and the difficulties encountered by debtors seeking time to pay in order to avoid bankruptcy.

Case Study 1

Jock is 60 years old. He inherited an apartment from his family members. He has an intellectual impairment and was recently injured at work. Jock is awaiting a determination from Work Cover and currently has no income. He received a Bankruptcy Notice which provided him 21 days to pay a judgment debt relating to his strata fees. He contacted the CCLC as the Bankruptcy Notice was due to expire, and he did not know what to do. Jock was at serious risk of losing his home and thousands of dollars in equity.

Case Study 2

Marietta contacted CCLC for assistance after she was made bankrupt over an unpaid Strata Management levy. Her original unpaid debt was $2,500 but the amount claimed by the time of her call for advice was with enforcements costs and trustee fees $16,000. Her only other debt was a credit card debt of $2,500.

Case Study 3

John was made bankrupt on a $6,000 strata debt. He was unaware of the judgment and the bankruptcy proceedings as he travelled frequently and English was not his first language. Three months after the Sequestration Orders were made he annulled his bankruptcy by paying the original $6,000 and ***an additional $25,000 in trustee fees*** that had accrued.

After he annulled the bankruptcy the strata manager demanded an additional $3,000 in 'strata collection fees' of $250 per month for the months where John was bankrupt. The trustee and solicitor for the strata manager agreed that there was no fee outstanding, but the strata manager continued to demand payment.

The following case studies do not involve bankruptcy proceedings (yet) but reveal the difficulties encountered by debtors who attempt to use the legal processes available to them to avoid the risk of bankruptcy.

Case Study 4

Marina is 56 years old. She owns a flat in a strata title block. She has a $70,000 mortgage to Big Bank and her income is derived from a partial Disability Support Pension and paid employment. She budgets her annual income to pay her strata contributions.

In November 2007 she received a levy notice in relation to a special levy incurred when her building was required to upgrade their fire alarms. The levy notice was for $2000, which Marina was unable to pay in a lump sum. On the bottom of the special levy was written "If you have any financial difficulty please contact the Strata Management Company to organise a repayment arrangement". Marina contacted the Strata Management Company as suggested but was refused a repayment arrangement.

Marina contacted CCLC and was advised to ask for a repayment arrangement in writing. It was arranged for her to see a Financial Counsellor for assistance in determining what level of repayments she could afford and in negotiating with the Strata Management Company. The Financial Counsellor contacted the Strata Management Company several times on her behalf, but the repayment arrangement was never acknowledged by the Strata Management Company. Marina continued to receive invoices that included considerable interest and account management fees.

In December 2007 Marina lodged an application under s149 of the Strata Management Scheme for mediation in relation to varying her contribution payments on the grounds of hardship. The Strata Management Company did not attend the mediation, and the matter was referred to an Adjudicator. Marina made written submissions in relation to her financial situation that were sent to each member of the Strata Complex. These were put on display in the noticeboard in the foyer of the building. This humiliated and frustrated Marina who still had no resolution to her levy difficulty.

In January 2008, Marina was issued a Statement of Claim in relation to the Strata Levy even though the matter is still before the Adjudicator in the Consumer Trader and Tenancy Tribunal. Marina is very dissatisfied with the legal process, and her debt is increasing due to the debt recovery action that continues as she attempts to defend the Local Court matter and attend to the CTTT Adjudication.

Case Study 5

Brendon is 50 years old. He is on Centrelink unemployment benefits after losing his job. He had been on a repayment arrangement of $150 per fortnight, covering his strata arrears and the payments as the new levies fell due. When he lost his job he missed a repayment and was unable to catch up. He tried to re-negotiate the payment plan. He did not receive a response from the strata manager.

He received a statement of claim. He went to Office of Trading for help negotiating, but they were unable to assist as legal proceedings had commenced.

He contacted the Credit and Debt Hotline, and one of the Centre solicitors gave him legal advice about responding to the statement of claim. Section 149 of the Strata Schemes Management Act is not a defence or a positive right. Based on the advice provided Brendon decided to lodge a Notice of Motion to Pay by Instalments as he had no defence, and his repayment arrangement was accepted by the Local Court. However the strata manager lodged an objection. A hearing was set down before a Magistrate.

Brendon attended the hearing by himself after an appointment with a Legal Aid solicitor and his instalment application was rejected as he had not filled in the form correctly as he had missed filling in one of the values. The Magistrate ordered that Brendon had to pay $200 in costs as the other side was represented at the hearing. The Magistrate gave Brendon 7 days to file another instalment application.

Brendon filed his Notice of Motion within the seven days, with the figure included as directed by the Magistrate. The Registrar rejected the instalment as it was the same as the first. Brendon tried to explain that the first was rejected due to an omission of a figure. Brendon with the help of the Centre solicitor and a Centre financial counsellor was able to provide a written explanation of the reasons and include a budget showing he could afford to repay the outstanding amount in a reasonable time. His instalment application was accepted by the Local Court.

However, a further objection was made by the strata manager. The Centre solicitor agreed to represent Brendon at the hearing and negotiate on his behalf. An agreement was entered into for Brendon to pay $150 per fortnight. The solicitors for the strata manager charged $1500 in enforcement expenses that has added to Brendon's original debt of $4,500.

(e) Introduction of a 28 day moratorium on payment.

The current time frame of the Debtors Intent to File for Bankruptcy is seven days. This prevents creditors from continuing and enforcing any debt recovery action during this period. In CCLC's experience as the key referral point for financial counselling in NSW, and an experienced advocate in negotiating hardship arrangements, the seven day period from the time of the Debtors Intent being approved does not allow adequate time to:

(1) Secure an appointment with a financial counsellor or other insolvency practitioner
(2) Contact creditors for payment options.

We therefore strongly support the extension of this period to 28 days.

We are concerned however about the proposed amendment to Section 54A to require a Statement of Affairs to be filed with the declaration of intent, albeit in a simpler form. CCLC advises all callers contemplating bankruptcy to seek assistance from a financial counsellor covering the following:

- The consequences of bankruptcy in the debtor's particular circumstances;
- The alternatives that may be available; and
- Assistance with completion of the Statement of Affairs.

Many callers to our service struggle with the completion of the Statement of Affairs. Even fairly literate clients can find the complexity of the document confusing and it is important, given the consequences of inaccurate completion, that appropriate assistance is sought. We submit that the requirement to lodge a Statement of Affairs with the notice of intent may defeat the purpose of the extended period in which to seek advice, as many debtors will need advice to complete the form itself.

(f) Increase the debt, income and asset thresholds for eligibility for debt agreements by 20%.

CCLC continues to hold serious concerns in relation to Part IX Debt Agreements. CCLC raised these concerns previously in the last review of the relevant provisions in 2007, and in our submission to the Productivity Commission. Whereas some problems may have been partially addressed by the 2007 changes in regulation, many problems persist.

Part IX Debt Agreements are sold by private administrators (and brokers) with a view to making a profit from consumers whose essential problem is that they are already in serious financial difficulty and cannot meet their commitments to existing creditors. This business model makes its profit by diverting some of the limited funds available to pay existing creditors to the debt agreement administrator. While this may have some net benefit for the community (but not necessarily the debtor) if every debtor who entered a Part IX Agreement would have otherwise gone bankrupt, CCLC's experience, however, suggests that this is far from reality (some CCLC clients do not appear to have even been insolvent at the point of entering a Debt Agreement).

Debt Agreements have grown rapidly in Australia since their inception in late 1996 from 300-500 in the first few years to 8,567 in the financial year to June 30 2009. Fox Symes, a company managing 54% of all debt agreements in Australia recently reported an increase in after tax profit of 229% to $8.84 million.[1] While the returns on Debt Agreements reported by Attorney-General McClelland are compelling on their face (76 cents in the dollar compared to 1.6 cents in the dollar for bankruptcies), CCLC urges the Government to look carefully behind these figures before drawing any conclusions.

In CCLC's experience, those consumers seeking to enter voluntary bankruptcy are usually those with minimal assets (usually household furniture and a modest vehicle), and low to medium income. In recent years, an increasing number of inquiries about bankruptcy is coming from home buyers with nil or negative equity and a large amount of unsecured personal debt. Clearly the returns from such bankruptcies will be minimal.

Debt Agreements on the other hand are embraced by debtors seeking to freeze interest and consolidate their debts into one payment. Arguably such debtors are sometimes solvent. Certainly, anecdotal evidence from callers to the Credit and Debt Hotline suggests that many would never have considered entering voluntary Bankruptcy, had a Part IX Debt Agreement not been available. In other words, they were not contemplating Bankruptcy and opted instead for a Part IX Agreement, they were simply struggling financially and saw a Part IX Debt Agreement as a possible way of easing the pain. In many of these cases, the debtors concerned are clearly in financial difficulty, but may have been better off in the long run with a hardship variation, or informal debt arrangement, from their lender (or lenders). Certainly, such an arrangement would have less long term ramifications for their financial rehabilitation, and would have ensured that all available funds were sent directly to creditors.

[1] Bryce, J, Fox Symes looks forward to better outcomes, *The Sheet*,3 September 2009, viewed at http://www.thesheet.com/nl06_news_selected.php?act=2&nav=1&selkey=8811&utm_source=daily+email&utm_medium=email&utm_campaign=Daily+Email+Article+Link

The promotion of Debt Agreements is highly effective, evidenced not only by the significant numbers of people entering such agreements, but also by the fact that the CCLC Credit and Debt Hotline gets as many referrals from private debt agreement administrators as from the Government's official legal referral service, Law Access. Such referrals are usually given to debtors on very low incomes, often government benefits, who could very clearly not meet the obligations under a Part IX Debt Agreement or pay the fee to propose such an agreement. CCLC also receives such referrals where debtors are seeking a further loan or consolidation (not a matter with CCLC can assist). In addition, CCLC receives calls from:

- Debtors contemplating debt agreements as a result of advertising who are clearly misinformed as to their nature and consequences, or who have simply embraced the idea of a debt agreement without exploring other options because it is the first "solution" that has come to their attention;
- Debtors who have paid to propose a debt agreement only to find they are in a worse situation when the proposal is rejected and they are further out of pocket *and* behind in their payments; and
- Debtors who are unable to meet their commitments under a debt agreement and are now in limbo, unsure what they should do.

Case Study 6

Elaine contacted the Credit and Debt Hotline in November 2008. She was in financial difficulty due to being injured at work. She contacted a Debt Agreement Administrator she saw advertised on the internet. She was told not to make any payments towards her debts for 6 weeks or more pending a decision on a Part IX Debt Agreement proposal. She was also told the proposal would not affect her credit reference file. Her proposal was rejected, she was further behind in her debts, her creditors have now rejected an application for hardship based on her poor recent repayment history, and she has default listings on her credit report.

Case Study 7

Bianca's boyfriend contacted the Credit and Debt Hotline in January 2009 when she fell into trouble with her small business and had $70,000 outstanding on credit cards, a mixture of personal and business related debt. She paid $2,000 to a Debt Agreement Administrator to make a Part IX Debt Agreement proposal and stopped making any payments as directed. Now there seems to be a problem with the proposal and all the creditors are figuratively screaming for payment.

Case Study 8

Stephen rang the Credit and Debt Hotline in June 2009 when he was sued by a creditor for a debt that had been included in a Part IX Debt Agreement in January 2009. He contacted Debt Agreement Administrator who suggested he "ask for a waiver" and wished him luck.

Case Study 9

Jillian entered a Debt Agreement several years ago. After paying for the best part of five years, she lost her job and applied to the Debt Agreement Administrator to reduce her repayments. She was told this was fine. However, it appears that this information was never agreed to, or even communicated to, the creditors who have now terminated the agreement. She called the Credit and Debt Hotline because one creditor is now pursuing her for $3,000, which she believes can't possibly be right given the amount she has paid over the last five years. She also wants to lodge a complaint about the Debt Agreement Administrator for telling her that reducing her repayments was not a problem.

Case Study 10

Christie and partner contacted the Credit and Debt Hotline for advice in July this year. Christie had entered a Debt Agreement last November. She received a Statement of Claim from one of her creditors in March. She contacted the Debt Agreement Administrators who said they would "sort it". In July she received an Examination Summons. Further enquiry of the creditor revealed that they were suing her partner and joint debtor, and that she was named as a second defendant. She was advised that as the Debt Agreement was in her name only it did not cover her husband's joint and several liability for the debt. Both she and her partner said they had been given the opposite advice by the Debt Agreement Administrators.

Case Study 11

Henry called the Credit and Debt Hotline in 2009 seeking a referral to a financial counsellor so that he could get assistance to go bankrupt. He had sometime previously applied for a Part IX Debt Agreement and stopped paying his creditors as advised. The application was ultimately rejected and he found himself worse off as a result of not paying in the meantime. He tried to complain to the Debt Agreement Administrator but they said they had no record of him, his proposal or the actual person he spoke to.

Despite the new regulatory framework applied to Debt Agreement Administrators in July 2007, CCLC suggests that Debt Agreements are:

- Increasing the amount of bankruptcy activity in Australia, thereby diverting funds from creditors to Debt Agreement Administrators as a result of their highly visible and effective promotion;
- Undermining the financial hardship initiatives undertaken by Government and Creditors[2] (debtors applying for debt agreements are advised to stop all payments

[2] Media Release by the Treasurer**,** *Relieving Mortgage Stress***:** *The Principles: A Common Approach for Assisting Borrowers Facing Financial Hardship,* 5 April 2009
Media Release by the Treasurer, *Building Societies, Credit Unions and Retail Banks Sign Up to Help Borrowers in Distress*, 21 June 2009

and cease contact with creditors, effectively denying creditors the opportunity to resolve the issue directly with their customer)

- Exacerbating financial difficulties for borrowers who are rejected after being advised to cease all payments, or who are unable to complete their Debt Agreement due to it being unsustainable, or as a result of a further change of circumstances.

We strongly urge the Government to refrain from increasing the potential for further significant growth in Debt Agreements by increasing the relevant thresholds until the regulatory framework introduced in 2007 is subject to the more thorough review due to occur in 2010.

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