The Senate

Legal and Constitutional Affairs Legislation Committee

Bankruptcy Legislation Amendment Bill 2009 [Provisions]

February 2010

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ABBREVIATIONS

ABA	Australian Bankers' Association
AFC	Australian Finance Conference
Act	*Bankruptcy Act 1966*
AICM	Australian Institute of Credit Management
Bill	Bankruptcy Legislation Amendment Bill 2009
CALC	Consumer Action Law Centre
CCLC	Consumer Credit Legal Centre (NSW)
Department	Attorney-General's Department
FCRC	Financial and Consumer Rights Council
IPA	Insolvency Practitioners Association
ITSA	Insolvency and Trustee Service Australia
Law Council	Law Council of Australia
NPII	National Personal Insolvency Index
PILCH	Public Interest Law Clearing House

RECOMMENDATIONS

Recommendation 1

3.53 The committee recommends that the Senate pass the Bill.

CHAPTER 1

Introduction

1.1 On 29 October 2009, the Senate referred the provisions of the Bankruptcy Legislation Amendment Bill 2009 (Bill) to the Legal and Constitutional Affairs Legislation Committee for inquiry and report by 2 February 2010. On 2 February 2010, the Senate agreed to extend the reporting date to 23 February 2010.

Purpose of the Bill

1.2 The Bill was introduced in the House of Representatives on 28 October 2009 by the Attorney-General, the Hon. Robert McClelland MP. The Bill amends the *Bankruptcy Act 1966* (Act) and aims to:

- provide a more streamlined process for fixing trustee remuneration and a more transparent process for reviewing that remuneration;
- strengthen the penalties for some offences and ensure these align with the penalties for similar offences;
- remove the outdated concept of 'bankruptcy districts' to provide more flexibility in personal insolvency administration;
- increase the minimum debt for a creditor's petition to reflect changes in the economic environment;
- increase the stay period that follows a declaration of intent to file a debtor's petition to allow debtors to better assess their options; and
- increase the debt, income and asset tests thresholds for debt agreements to ensure the thresholds keep pace with increasing wages and the increasing availability of credit.[1]

1.3 According to the Replacement Explanatory Memorandum (REM), the primary purpose of the Bill is to modernise the national personal insolvency scheme and to make it more efficient. In particular, the Bill includes amendments which recognise that the majority of bankruptcies relate to consumer debts and involve bankrupts with relatively few assets and little income.[2]

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1 Replacement Explanatory Memorandum, p. 1.

2 Replacement Explanatory Memorandum, p. 2.

Conduct of the inquiry

1.4 The committee advertised the inquiry in *The Australian* newspaper on 18 November 2009, 2 December 2009, 9 December 2009 and 27 January 2010. Details of the inquiry, the Bill and associated documents were placed on the committee's website. The committee also wrote to 30 organisations and individuals, inviting submissions by 25 November 2009.

1.5 The committee received 15 submissions which are listed at Appendix 1. Submissions were placed on the committee's website for ease of access by the public.

1.6 The committee held a public hearing in Sydney on 28 January 2010. A list of witnesses who appeared at the hearing is at Appendix 2, and copies of the Hansard transcript are available through the internet at http://www.aph.gov.au/hansard.

Acknowledgement

1.7 The committee thanks those organisations and individuals who made submissions and gave evidence at the public hearings.

Scope of the report

1.8 Chapter 2 provides a brief outline of the key provisions of the Bill, and Chapter 3 discusses the key issues raised in submissions and evidence.

Note on references

1.9 References in this report are to individual submissions as received by the committee, not to a bound volume. References to the committee Hansard are to the proof Hansard: page numbers may vary between the proof and the official Hansard transcript.

CHAPTER 2

Overview of the Bill

2.1 This chapter provides a brief overview of the purpose and key provisions of the Bill. The Bill comprises four schedules, which contain the following categories of amendments:

- remuneration of trustees of estates of bankrupts – Schedule 1;
- offence provisions – Schedule 2;
- removal of bankruptcy districts – Schedule 3; and
- other amendments – Parts 1 and 2 of Schedule 4.

2.2 A brief outline of these categories is provided below, with an emphasis on those provisions particularly examined during the course of the inquiry.

Remuneration of trustees of estates of bankrupts

2.3 Items 1 to 17 of Schedule 1 aim to provide a clearer regime for setting and reviewing the remuneration of trustees of estates of bankrupts by providing for:

- a more accessible and streamlined process for challenging a trustee's remuneration claim;
- enhanced oversight for the Inspector-General in Bankruptcy to ensure trustees are following the rules when claiming remuneration; and
- a streamlined process for claiming a basic amount of remuneration (set at $5,000) which reflects the essential tasks undertaken by every trustee.[1]

Offence provisions

2.4 Items 1 to 84 of Schedule 2 of the Bill:

- provide for the introduction of an infringement notice regime as an alternative to prosecution for offences of strict liability;
- ensure that the penalties for some offences (particularly those involving fraud) reflect the seriousness of the conduct and are consistent with penalties for similar offences in other federal, state and territory legislation;
- provide stronger powers to obtain a 'statement of affairs' from a bankrupt who fails to file this document as required; and

1 Replacement Explanatory Memorandum, p. 2.

- provide stronger powers for the Inspector-General in Bankruptcy to investigate possible offences under the Act.

Removal of Bankruptcy Districts

2.5 The overall purpose of Schedule 3 is to deliver a more efficient, national personal insolvency scheme. Essentially, the Bill seeks to achieve this objective by removing the concept of bankruptcy districts from the Act.

Other amendments

2.6 Schedule 4 of the Bill – comprising Parts 1 and 2 – relates to 'other amendments'. The three key amendments examined during the course of the inquiry are contained in Schedule 4 and are categorised by the REM as follows: increasing the minimum debt for a creditor's petition to $10,000; increasing the stay period that follows the declaration of intent to file a debtor's petition; and increasing the debt income and assets thresholds for eligibility for debt agreements. These amendments are described in detail below.

Increasing the minimum debt for a creditor's petition to $10,000

2.7 At present, the Act allows a creditor to petition for bankruptcy where the debtor owes at least $2,000. Similarly, a creditor can request that the Official Receiver issue a bankruptcy notice where the debtor owes at least the same amount. This amount has not increased since 1996. Item 1 of Schedule 4 would increase this amount to $10,000, and items 2 and 3 of Schedule 4 would do likewise in respect of filing a creditor's petition and an application for administration of a bankrupt estate. The REM explains the proposed changes as follows:

> It is wrong to set in motion all the machinery of bankruptcy for the purpose of winding up a debtor's estate when, as is often the case, one creditor has a debt due to him of an amount not much more than $2,000. Raising the amount of the petitioning creditor's debt will lessen the opportunity to use bankruptcy procedures as a debt collection process. It is an established principle of the law of bankruptcy that, when a creditor sets in motion proceedings in bankruptcy, they do so for the benefits of all the debtor's creditors. Moreover, there has been a significant change in the value of money and levels of individual indebtedness since 1996 when the Bankruptcy Act was last amended in this respect.[2]

2.8 The REM reports that, during 2008-09, of 1,953 sequestration orders made across Australia and matched by amounts in bankruptcy notices, 1,551 were for an amount greater than $10,000; 217 were for an amount between $5,001 and $10,000; and 174 were for an amount between $2,000 and $5,000.[3] However, the REM does

2 Replacement Explanatory Memorandum, pp 22–23.

3 Replacement Explanatory Memorandum, p. 23.

not explain why the new threshold would be set at $10,000: there is no indication of any assessment of acceptable debt levels.

Increasing the stay period that follows the declaration of intent to file a debtor's petition

2.9 The Act also currently allows a debtor to give the Official Receiver a declaration of intent to file a debtor's petition. Once the debtor's declaration of intent to file is given, creditors cannot take action to recover any debts for a stay period of seven days. Item 5 of Schedule 4 would increase the stay period from seven days to 28 days. The REM states that:

> A 7 day stay period does not give debtors enough time to assess their options. If a debtor is not fully informed about their options they may act precipitously. In any given 7 day period there will only be at most 5 working days (less when a public holiday falls during the seven day period). Given that most professional advisors that a debtor may wish to consult during the stay period are only open during normal working hours it would be very difficult for a debtor to obtain adequate advice during the 7 day stay period. If the 7 day stay period falls during the period leading up to the end of the financial year or during the Christmas period the debtor's difficulties in obtaining adequate advice during the stay period will be compounded. In addition, debtors typically owe money to a number of creditors and it can be difficult, at a time of financial stress, to achieve an outcome with each individual creditor within 7 days.[4]

2.10 Items 6-8 of Schedule 4 would also provide that a declaration of intent to file a debtor's petition must be accompanied by a statement of the debtor's affairs:

> The requirement to file a statement of affairs will mitigate the risk of the debtor dissipating assets during the stay period.[5]

Increasing the debt income and assets thresholds for eligibility for debt agreements

2.11 A debt agreement is a voluntary agreement between a debtor and creditors proposed by the debtor. It is principally aimed at consumer debtors with lower levels of income, assets and debts; consequently, there are statutory thresholds which determine eligibility.

2.12 At present, the Act provides for the threshold amount as being seven times the amount that, at a particular point in time, is specified in column 3, item 2, Table B, point 1064-B1, Pension Rate Calculator A, in the *Social Security Act 1991*.

2.13 Item 11 of Schedule 4 would increase the threshold amount for eligibility for debt agreements by increasing the multiplier from 7 to 8.4, translating into a 20 per

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4 Replacement Explanatory Memorandum, p. 23.

5 Replacement Explanatory Memorandum, p. 24.

cent increase. The present thresholds are: after tax income of less than $62,735.40; *or* unsecured debts, and assets, of less than $86,647.20. The REM explains:

> These thresholds were last revised in 2002 with the aim of making debt agreements more widely available. They were also considered in a review of debt agreements conducted prior to amendments which commenced on 1 July 2007. During that review, it was decided to retain the thresholds at their current levels until the next review of debt agreements scheduled for 2010. This was to allow time to evaluate the effectiveness of the 2007 amendments which were aimed at restoring creditor confidence in the system and addressing the unacceptably high failure rate. However, it is considered that a modest increase in the thresholds in advance of the 2010 review is consistent with current policy and merely recognizes the increases in debt, wealth and available income since the thresholds were last revised. Since the 2007 amendments, the termination rate has fallen to around 4% of debt agreements made since 1 July 2007. This compares with a termination rate of 35-40% under the previous rules. In addition, the rate of acceptance by creditors of debt agreement proposals has increased from less than 70% to over 85%. This demonstrates greater confidence by creditors in the system.[6]

6 Replacement Explanatory Memorandum, p. 24.

CHAPTER 3

Key issues

3.1 Submissions and witnesses expressed support for the overall objective of the Bill: that is, to modernise the national personal insolvency scheme and improve its efficiency. However, for some, this support did not extend to certain provisions of Schedule 4. The three key issues arising in relation to Schedule 4 are discussed in this chapter:

- the threshold for a creditor's petition;
- the increase in debt, income and asset thresholds for debt agreements; and
- the increase in the stay period following a declaration of intent to file a debtor's petition.

The threshold for a creditor's petition

3.2 The Australian Government has taken the view that bankruptcy tends to involve people who have fallen on hard times, rather than debtors seeking to escape payment of their debts. The Bill therefore introduces measures aimed at giving those in financial distress a more realistic opportunity to consider their options, reorganise their affairs, and, where possible, avoid bankruptcy.[1]

3.3 One such measure is contained in item 1 of Schedule 4, which proposes to increase the threshold for a creditor's petition from $2,000 to $10,000. Submitters and witnesses were divided on this issue, with some supporting the proposed new threshold and others expressing concern with the increase.

Support for the increased threshold

3.4 In general, those who supported the proposed new threshold did so on the grounds that a $10,000 threshold is more appropriate than the $2,000 threshold set in 1996; and, further, that a $10,000 threshold will prevent minor abuse of the bankruptcy system by some creditors.

3.5 The Consumer Action Law Centre (CALC), for example, submitted that the increased threshold would prevent the inappropriate use of bankruptcy laws by creditors seeking to recoup small debts. The CALC stated that a creditor's petition

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1 The Hon. Robert McClelland MP, Attorney-General, 'Reforms to personal bankruptcy laws', Media Release, 25 August 2009.

triggers a process which can significantly impact on debtors and their families. In its view, the bankruptcy process should never be used for the collection of small debts:

> It is the excessive cost and disproportionate impact of bankruptcy, combined with the existence of alternative debt collection processes that makes the use of bankruptcy to collect a debt under $10,000 so harsh, unfair and punitive to the debtor. [2]

3.6 The CALC, and others, referred particularly to Eastern Access Community Health's November 2007 report, *Homes at risk: using bankruptcy to collect small debts*, which noted:

> Mainstream creditors are currently paying more attention to the development and implementation of financial hardship policies for debtors in financial difficulty. Attention to responsible collection of debt beyond this stage would be welcomed by financial counsellors. Using the bankruptcy regime to collect small debts should be a last resort.[3]

3.7 In relation to a minimum debt amount, the CALC went on to submit that a $10,000 threshold is appropriate in view of the Consumer Price Index (CPI) and increases in personal debt levels since 1996:

> The [Eastern Access Community Health] report, which is the only detailed investigation into this issue, concluded that the minimum debt amount should be increased from $2,000 to $10,000. We agree that this is an appropriate level for 2009. The threshold amount was last raised from $1,500 to $2,000 in 1996, however, the original minimum debt amount was, in fact, set in 1966 at $500. This amount has not kept pace with inflation or other market changes, being raised only sporadically since that time. At current values, the $500 original threshold would equate to over $5,000 merely as a result of inflation. In addition, the consumer credit market has been transformed since 1966. Personal debt levels are increasing exponentially and considerably larger amounts of debt are now routinely carried by consumers. Forced bankruptcy in order to liquidate a person's home over a $5,000 debt is a manifestly disproportionate response to the size of such a debt.[4]

3.8 The views in paragraphs 3.5 to 3.7 were shared by the Homeless Persons' Legal Centre (a project of the Public Interest Law Clearing House (PILCH)), the

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2 Consumer Action Law Centre, *Submission 3*, pp 3-5.

3 J. Pentland, *Homes at risk: using bankruptcy to collect small debts*, Eastern Access Community Health, November 2007, p. 25. www.afccra.org/otherpublication%20documents/Homes%20at%20risk%208%20dec.pdf (accessed 12 February 2010).

4 Consumer Action Law Centre, *Submission 3*, p. 5.

Consumer Credit Legal Centre NSW (CCLC), the Financial and Consumer Rights Council (FCRC), and Legal Aid NSW.[5]

3.9 While supportive of the increased threshold, the CALC, and others, called for clarification of the threshold amount; that is, whether it relates to the original amount owing or the amount owed at the time the petition is presented, which could also include collection costs, late fees, and interest:

> We have seen several cases in which a creditor or debt collector owed a small debt below the minimum debt amount in the Act has simply waited until costs have accrued on the debt and, once the debt amount has passed the threshold, they have pursued bankruptcy proceedings.[6]

Opposition to the increased threshold

3.10 In contrast, other submitters and witnesses expressed concern with the Bill's proposal to increase the minimum threshold for a creditor's petition.[7] These concerns primarily focussed on a lack of evidence for the need to increase the threshold, and a perceived failure to attack the root causes of financial hardship.

3.11 The Australian Institute of Credit Management (AICM) argued that it was inaccurate to characterise the majority of bankrupts as having 'fallen on hard times'. In support of its position, the AICM drew on annual reports of the Inspector-General in Bankruptcy, which show that:

- more than half of bankruptcies in 2008-09 occurred in the over 35 age bracket; and
- the occupational profile of bankrupts discloses a four-fold increase since 2005 in the percentage of bankrupts who are managers or administrators, as well as a three-fold decrease in the percentage who are students, pensioners, retired or unemployed.[8]

3.12 Similarly, Bartier Perry submitted that the rationale for the increased threshold, and the statistics put forward by the Australian Government to support that

5 Financial and Consumer Rights Council, *Submission 5*, p. 4; Legal Aid NSW, *Submission 6*, p. 2; PILCH, *Submission 10*, p. 6; and Consumer Credit Legal Centre (NSW), *Submission 11*, p. 4.

6 Consumer Action Law Centre, *Submission 3*, p. 6. See also Financial and Consumer Rights Council, *Submission 5*, pp 1-5; and Consumer Credit Legal Centre (NSW), *Submission 11*, pp 3-4.

7 See, for example, Australian Institute of Credit Management, *Submission 1*, p. 1; PPB, *Submission 2*, p. 1; Bartier Perry, *Submission 4*, p. 1; and Insolvency Practitioners Association of Australia, *Submission 8*, pp 2–4.

8 Australian Institute of Credit Management, *Submission 1*, p. 3, citing Inspector-General in Bankruptcy, *Annual Report by the Inspector-General in Bankruptcy on the operation of the Bankruptcy Act 2007-2008*, Table 8.

change, are 'misconceived'.[9] This view was supported by the Insolvency Practitioners Association of Australia (IPAA). The IPAA told the committee:

> …if there is a case for the increase of that threshold, we do not think the case is made out in the information provided in the explanatory memorandum and elsewhere. We think that there should be clear statistical or other evidence that would show that, where a petitioning creditor's debt is under $10,000 or, let us say, close to $2,000, that results in a bankrupt estate of minimal assets and liabilities. That information, we feel, would be available, and we do not feel that the information that has been provided substantiates that.[10]

3.13 The committee asked the IPAA precisely what was wrong with the figures set out in the REM. In response, the IPAA described the figures as 'bald', and indicated that a further level of detail is required to determine whether the existing threshold is sufficient, that is, whether it is actually resulting in 'small bankruptcies':

> Sequestration orders made where the amount claimed was, in effect, below $10,000, do not seem to take the matter very far. Of those bankruptcies—and I am just speaking broadly—we would like to know to what extent they were very small bankruptcies in terms of number of debts and number of assets. That is not shown, and that is really the substance of what I think this whole issue is about…I suppose it is a matter of policy as to whether a person should be able to go bankrupt when their ultimate debt position is $4,000—they have got $4,000 worth of debts—and they have got $3,000 in the bank…I think that there is a feeling that is not appropriate and that person might be dealt with in another way.[11]

3.14 The IPAA went on to tell the committee that the Bill would also create an unjustifiable disparity between the personal and corporate insolvency regimes, where the latter does not appear to need an increase in its threshold amount:

> There has been no parallel move or comment or request for increase in corporate insolvency. One fundamental point about insolvency, in both personal and corporate, is that the debt upon which the petitioning creditor relies to trigger the insolvency is only a trigger amount.[12]

3.15 PPB Pty Ltd (PPB), an advisory firm practising in insolvency, separated bankrupts into two categories: unwilling debtors; and incapable debtors. While the

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9 Bartier Perry, *Submission 4*, p. 3.

10 Mr Michael Murray, Legal Director, Insolvency Practitioners Association of Australia, *Committee Hansard*, 28 January 2010, p. 2. See also Ms Del Cseti, National Training and Marketing Manager, Australian Institute of Credit Management, *Committee Hansard*, 28 January 2010, p. 2.

11 Mr Michael Murray, Legal Director, Insolvency Practitioners Association of Australia, *Committee Hansard*, 28 January 2010, pp 6-7.

12 Mr Michael Murray, Legal Director, Insolvency Practitioners Association of Australia, *Committee Hansard*, 28 January 2010, p. 3.

Australian Government has identified those in the latter category as in need of assistance, PPB considered that:

> Denying creditors access to the bankruptcy process does not encourage Incapable Debtors to deal with their debts. Instead it allows them to further defer dealing with their problems. The consequence is that debts will be allowed to increase to a less manageable level before the debtor is obliged to deal with the problem.[13]

3.16 Some submitters also took issue with the apparent assumption that creditors are not using alternate debt collection processes. Bartier Perry submitted that creditors are using all means at their disposal to recover debts owed to them:

> Individual creditors and small businesses are much less capable of in effect writing off debts under $10,000…It is, with respect, somewhat insulting to suggest that simply because they have debts less than $10,000 these creditors have 'other options' which they have somehow failed to explore and which would lead to a recalcitrant debtor complying with his or her obligations. There is no evidence whatsoever that these 'other options' are not being pursued.[14]

3.17 The AICM also submitted that seeking payment of debt through lodgement of a creditor's petition remains a relatively unpopular avenue for creditors, featuring in only nine per cent of bankruptcies:

> …the decision to pursue a debt through the provisions of the *Bankruptcy Act 1966 (Cth)* is only made when a thorough assessment of the debtor's situation has been undertaken. There is little purpose in seeking to exercise remedies under the *Bankruptcy Act* if the individual concerned has no assets and little or no income. Creditors' petitions are primarily utilised in situations where the individual has assets and income and is in a position to meet their obligations albeit reluctantly.[15]

3.18 At the public hearing, an AICM representative also suggested that there would be no real need for the new threshold or, implicitly, any other reforms proposed by the Bill, given the recent introduction of a number of significant legislative reforms (such as the *Personal Property Securities Act 2009*):

> …we feel that it would be preferable to let those reforms take place and become part of the financial and credit and debt recovery domain before this amendment proceeds, because we feel that at that stage you may find that it is actually not necessary.[16]

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13 PPB, *Submission 2*, p. 3.

14 Bartier Perry, *Submission 4*, p. 5.

15 Australian Institute of Credit Management, *Submission 1*, p. 4.

16 Ms Del Cseti, National Training and Marketing Manager, Australian Institute of Credit Management, *Committee Hansard*, 28 January 2010, p. 3.

What is an appropriate increase?

3.19 Submitters and witnesses differed in their views as to what would be an appropriate increase to the threshold amount. If there were to be any increase, some suggested that a $5,000 threshold would be sufficient.[17] However, for those in favour of the threshold proposed in the Bill, $5,000 was considered far too low.

3.20 The Australian Finance Conference (AFC) and the Australian Bankers' Association (ABA) both expressed a preference for a $5,000 threshold, on the basis that:

> It is unclear how the proposed threshold has been arrived at and [it] may operate as a disadvantage to small business operators who are generally owed debts of much smaller amounts.
>
> A change of this magnitude further signals to a debtor that a failure to pay far lesser amounts is unlikely to result in bankruptcy at the suit of a debtor's creditors and so dilute the importance to the debtor of the debtor's obligation to pay.
>
> Where a debtor's liabilities to pay accrue over time, for example a strata title owner's payments to their body corporate management company, it may take several years before enforcement action with the prospect of bankruptcy can be undertaken.[18]

3.21 The IPAA also considered $5,000 to be a more appropriate threshold amount for a creditor's petition, on the basis of a previous CPI assessment of the 1996 figure. However, the IPAA emphasised that the amount merely serves as a trigger:

> …there is a lot of focus on this figure which is not necessarily relevant…to what the extent of the insolvency may ultimately be. I think the figures are there to demonstrate it, but they just have not been extracted. For example, we do not know to what extent, for petitioners with $2,000 worth of debt, a bankruptcy results with that being the only debt or with the other debts even smaller than that totalling no more than $5,000. It really is, as I said, just a trigger point—a trigger debt. Insolvency law requires a creditor to show that the debtor against whom they are bringing the proceedings is insolvent. That insolvency is in effect demonstrated by the fact that that debtor cannot pay on the bankruptcy notice an amount of $2,000.[19]

3.22 Much of the evidence received by the committee focussed on the current threshold amount of $2,000 set in 1996, and what would have happened to that figure over time. Supporters of the proposed new threshold also claimed that making

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17 See, for example, Insolvency Practitioners Association of Australia, *Submission 8*, p. 5.

18 Australian Bankers' Association, *Submission 7*, p. 3; and Australian Finance Conference, *Submission 12*, p. 2.

19 Mr Michael Murray, Legal Director, Insolvency Practitioners Association of Australia, *Committee Hansard*, 28 January 2010, p. 4.

appropriate adjustments to the 1996 figure would not equate to a threshold amount of $5,000. For example, the CCLC contended:

> Five thousand dollars is clearly too low. There would be no point making this reform if this were the amount. It would not protect people, particularly given that solicitors' fees and legal costs have risen greatly since this has been put in. Worse, it would be less than the original amount of $500 set in 1966, adjusted for inflation—and that is not even taking into account the huge changes in personal debt since 1966…You do not make good policy by simply picking a number roughly in the status quo; you make sure it is appropriately chosen. The policy underlying the bankruptcy system needs to deal with genuine insolvency. It has not been created simply to provide another tool for debt collection.[20]

3.23 Similarly, the CALC questioned the basis for selecting $5,000 as the threshold amount, and intimated that this figure has been 'plucked out of the air' by businesses opposed to the threshold amount proposed in the Bill:

> …there is actually plenty of evidence to suggest that the amount should be raised to $10,000. The first time any other amount has been raised is during this process when they have tried to pick an amount in the middle because they do not like it being raised to $10,000.
>
> The only comprehensive report in this area is the *Homes at risk* report which had 25 case studies. It based its recommendation on an analysis of all of those case studies and the law in the area. It came up with the figure of $10,000. We know from the statistics that [Insolvency and Trustee Service Australia] provided in its submission and that are in the explanatory memorandum to the bill that it is only a small amount of creditors' petition initiated bankruptcies that are under the $10,000 limit again suggesting that is the correct amount and that it is only a small number of cases that it would affect. We have provided plenty of case studies in our submission and I know other groups did as well. These also suggest that $10,000 is the correct amount. The amount of $5,000 is patently too low.[21]

Department response

3.24 At the public hearing, officers from the Attorney-General's Department (Department) reiterated the view that a $10,000 creditor's petition threshold is appropriate. Officers told the committee that the Department had held stakeholder consultations and had adopted a balanced approach in the Bill:

> [The government] believes that that threshold is appropriate given the magnitude of the consequences that bankruptcy has for a debtor, the cost

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20 Ms Katherine Lane, Principal Solicitor, Consumer Credit Legal Centre (NSW), *Committee Hansard*, 28 January 2010, p. 9.

21 Ms Nicole Rich, Director, Policy and Campaigns, Consumer Action Law Centre, *Committee Hansard*, 28 January 2010, p. 12.

> and complexity of bankruptcy proceedings compared with other available debt collection methods, and the increase in levels of consumer debt.[22]

3.25 Departmental officers indicated that CPI changes to the 1996 amount were one factor taken into consideration by the government when determining the proposed new threshold.[23] When asked what CPI had done to the 1996 amount of $2,000, the Department advised that it would be $2,770 in 2009 dollars.[24]

3.26 Although some witnesses argued for indexation of the proposed threshold,[25] the Department confirmed that this approach is not favoured by the Australian Government:

> …this is a very significant trigger for a creditor to pull on somebody to make them bankrupt and…parliament in enacting legislation in this area is making a very significant decision about what that figure should be…In terms of indexing it, again, the change from $2,000 to $10,000 is about more than just changes in the value of money; it is about recognising the cost and complexity of bankruptcy, the overall shift in the demographics of bankruptcy and the level of debt that is owed. So we did not really think that indexation was the right approach to take, particularly when the government is already proposing to make a very significant increase on that basis.[26]

3.27 The committee also asked whether the Department had conducted any research into the asset and liability positions of debtors who were made bankrupt for debts of between $2,000 and $10,000. Departmental officers stated that no such investigations had taken place in relation to the Bill, because the information was not relevant to the policy intent:

> The policy intent here is to say to a creditor who is owed less than $10,000, 'We are taking away the right for you to commence bankruptcy proceedings.' It does not matter to that creditor what the overall indebtedness is.[27]

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22 Dr James Popple, First Assistant Secretary, Civil Law Division, AGD, *Committee Hansard*, 28 January 2010, p. 16.

23 Dr James Popple, First Assistant Secretary, Civil Law Division, AGD, *Committee Hansard*, 28 January 2010, p. 17.

24 AGD, Answer to Question on Notice, 29 January 2010 (8 February 2010), p. 1.

25 See, for example, Ms Katherine Lane, Principal Solicitor, Consumer Credit Legal Centre (NSW), *Committee Hansard*, 28 January 2010, p. 9; and Ms Del Cseti, National Training and Marketing Manager, Australian Institute of Credit Management, *Committee Hansard*, 28 January 2010, p. 8.

26 Mr David Bergman, Assistant Secretary, Bankruptcy Policy Branch, *Committee Hansard*, 28 January 2010, p. 18.

27 Mr David Bergman, Assistant Secretary, Bankruptcy Policy Branch, *Committee Hansard*, 28 January 2010, p. 26.

The increase in debt, income and asset thresholds for debt agreements

3.28 Item 11 of Schedule 4 of the Bill would raise by 20 per cent the eligibility threshold to enter into a debt agreement. This measure attracted support from a number of submitters, including the ABA and the IPAA.[28]

3.29 However, the CALC (and others) expressed 'major concerns' with the proposal, citing ongoing problems with the 'administration of such debt agreements and their appropriateness for many of the debtors to whom they are marketed and sold'.[29] Providing a number of case studies, the CALC went on to submit:

> …financial counsellors have reported that many of their clients have been lured into unrealistic and unsustainable debt agreements, and we are concerned that the large number of unsuccessful agreements is driven by the large fees retrievable by debt agreement administrators under the agreements. 11,353 debt agreements were proposed in the 2008-09 year and 8,599 of these proposed agreements were accepted by creditors but only 29 agreements were completed during the year…[A] 2005 report…found that many debtors failed to comply with their debt agreement after being unable to maintain payments that were unlikely to have been sustainable from the start.[30]

3.30 The committee heard from CCLC representatives that debt agreements are proving counterproductive, and are placing debtors in a worse situation than they would have been in had they been able to make an informed choice prior to entering into such an agreement:

> We see a whole lot of other people who have gone into a debt agreement and a little while down the track it has become apparent that they either cannot pay or their circumstances changed yet again, whereas if they had been bankrupt in the first place or had had an informal agreement in place with their creditor they might have been on the way to getting back on track by that stage. Instead, they have to go through the bankruptcy process at that later date and a lot of the money does not go through to the creditors anyway. There is a situation where people are actually in limbo—that is,

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28 Australian Bankers' Association, *Submission 7*, p. 4; and Insolvency Practitioners Association of Australia, *Submission 8*, p. 1.

29 Consumer Action Law Centre, *Submission 3*, p. 6.

30 Consumer Credit Legal Centre (NSW), *Submission 3*, p. 7 quoting Consumer Credit Legal Service (now Consumer Action) and Eastern Access Community Health, *Debt Agreements: Remedy or Racket?*, November 2005, p. iv. www.consumeraction.org.au/downloads/DebtAgreements-RemedyorRacket2005report.pdf (accessed 12 February 2010).

> where they are not bankrupt, they are not in their debt agreement anymore and they may or may not be being sued—and it is really a big mess.[31]

3.31 The FCRC also argued against an expansion of the eligibility criteria for debt agreements, and observed:

> It is also important to recognise that many debtors enter into debt agreements under the false belief that they will avoid the consequences associated with bankruptcy. For example, entering into a debt agreement will be recorded on a person's credit information file in a similar manner to bankruptcy and the person's name will be recorded permanently on the National Personal Insolvency Index. It is also generally considered an 'act of bankruptcy' under clauses in typical consumer lending arrangements such as mortgages, triggering default or foreclosure options for lenders.[32]

3.32 At the public hearing, witnesses commented on the extensive work of the Insolvency and Trustee Service Australia (ITSA), and its efforts to encourage people to consider all available options. The AICM also advised:

> …there is a document that is produced jointly by the [Australian Competition and Consumer Commission] and [Australian Securities and Investments Commission] on debt collection. There are two versions. There is one for creditors and one for debtors. They are incredibly useful guides to help people understand what their alternatives are from both sides of the picture. We feel that, coming out of the legislative reforms, in particular national consumer credit protection, more material of that sort in this easy, usable, friendly format is going to assist people.[33]

3.33 Both the CALC and the FCRC recommended that the Australian Government should review the recommendations of the Consumer Credit Legal Service and Eastern Access Community Health's 2005 report, *Debt Agreements: Remedy or Racket*, as well as the operation of debt agreements, prior to any amendment of the debt agreement eligibility requirements.[34] The CCLC also recommended that the threshold not be increased until a government review of the debt agreement regime is undertaken in 2010.[35]

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31 Ms Karen Cox, Coordinator, Consumer Credit Legal Centre (NSW), *Committee Hansard*, 28 January 2010, p. 10. See also Ms Katherine Lane, Principal Solicitor, Consumer Credit Legal Centre (NSW), *Committee Hansard*, 28 January 2010, p. 11; and Consumer Credit Legal Centre (NSW), *Submission 11*, pp 9-10.

32 Financial and Consumer Rights Council, *Submission 5*, p. 8.

33 Ms Del Cseti, National Training and Marketing Manager, Australian Institute of Credit Management, *Committee Hansard*, 28 January 2010, p. 6.

34 Consumer Action Law Centre, *Submission 3*, p. 7; and Financial and Consumer Rights Council, *Submission 5*, p. 8.

35 Consumer Credit Legal Centre (NSW), *Submission 11*, p. 10.

Department response

3.34 The Department explained the increased eligibility requirements for debt agreements on the bases that the reform will increase access to the arrangements, and that such arrangements provide greater returns than the bankruptcy system:

> This will give more debtors access to debt agreements. Debt agreements provide, on average, far superior returns to creditors than bankruptcy. In 2008-09, 60c in the dollar—this is dollars actually paid to creditors, contrary to what you have heard from witnesses earlier this afternoon—was paid for the agreement system. That compares with [$0.134] for all bankruptcies.[36]

3.35 Departmental officers also noted that creditors appear to have more confidence in the debt agreement system since reforms came into effect on 1 July 2007:

> The rate of acceptance of debt agreement proposals has increased from around 70 per cent to well over 80 per cent, and there has been a significant reduction in the termination rate, which is about six per cent down from well over 30 per cent for debt agreements made since the 2007 reforms.[37]

3.36 At the public hearing, the committee received conflicting evidence in relation to completion and failure rates for debt agreements. According to some witnesses, as little as 3.7 per cent of debt agreements were completed over the 2006-09 period.[38]

3.37 However, the Department contested this view. The Department indicated that the presentation of information in the Inspector-General in Bankruptcy's 2006-09 report is confusing as it covers debt agreements made both before and after the 1 July 2007 regulatory reforms. After much discussion concerning how debt agreements are tracked, a departmental officer concluded that completion rates have improved, and continue to improve:

> …when we did the review of debt agreements prior to the 2007 amendments, the formal termination rate was around a third, but only about a third of agreements were actually completed. There was this other group that just went off into limbo—people lost interest in them. So the actual termination rate was over 30 per cent. If you only look at debt agreements made under the new system, from 1 July 2007, until either the end of October or the end of November last year—so we are talking nearly 2½ years—6.1 per cent had been terminated…In our view, those numbers demonstrate that the failure rate has diminished very significantly. So the

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36 Dr James Popple, First Assistant Secretary, Civil Law Division, AGD, *Committee Hansard*, 28 January 2010, p. 17.

37 Dr James Popple, First Assistant Secretary, Civil Law Division, AGD, *Committee Hansard*, 28 January 2010, p. 17.

38 For example, see Ms Katherine Lane, Principal Solicitor, Consumer Credit Legal Centre (NSW), *Committee Hansard*, 28 January 2010, p. 9.

> way that the numbers are moving at the moment would suggest that, in a year or two, when we look at that table again and see what has happened to agreements that have been in place since July 2007—over four or five years—a much higher percentage of those will have been completed than had been under the old system.[39]

The increase in the stay period following a declaration of intent to file a debtor's petition

3.38 Item 5 of Schedule 4 of the Bill would increase the stay period following a declaration of intent to file a debtor's petition from seven days to 28 days. This measure attracted widespread support,[40] with some exceptions.[41]

3.39 Among the supporters was the Australian Financial Counselling and Credit Reform Association (AFCCRA). A representative of AFCCRA told the committee:

> …the whole point of…[the reform] is to give people an opportunity to seek some advice about their financial position. Seven days is just far too short a time to do that. You will not get an appointment with a financial counsellor, generally…[and] people are incredibly stressed in these circumstances. They need counselling and they need time. It certainly does not give you a chance to potentially negotiate with your creditors. So it has been an ineffective provision, other than allaying enforcement action, which is what happens.[42]

3.40 The CCLC agreed with this view, using similar reasoning to argue against the proposed requirement that a statement of affairs must be completed at the same time as a declaration of intent to file a debtor's petition:

> [Declarations of intent]…are a stopgap measure to try and save the situation so you can get your kids to school, you can get to work and things like that because you are genuinely insolvent and you just need time to see a financial counsellor. We should not add a statement of affairs to the burden of doing that in a desperately difficult situation where you basically have about 10 minutes, because the sheriff has told you he is coming—he or she…The idea that you are going to be carefully filling out a statement of

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39 Mr David Bergman, Assistant Secretary, Bankruptcy Policy Branch, *Committee Hansard*, 28 January 2010, p. 24. See also ITSA, Answer to Question on Notice, 11 February 2010 (11 February 2010), p. 1.

40 See, for example, Australian Institute of Credit Management, *Submission 1*, p. 5; Consumer Action Law Centre, *Submission 3*, p. 6; Financial and Consumer Rights Council, *Submission 5*, p. 6; Insolvency Practitioners Association of Australia, *Submission 13*, p. 1; and Consumer Credit Legal Centre (NSW), *Submission 11*, p. 6.

41 See, for example, Australian Finance Conference, *Submission 12*, pp 2-3; Australian Bankers' Association, *Submission 7*, p. 3; and Westpac, *Submission 9*, p. 2.

42 Ms Fiona Guthrie, Executive Director, Australian Financial Counselling and Credit Reform Association, *Committee Hansard*, 28 January 2010, p. 14.

affairs is absurd. Nobody has time to do anything except put your name, address, who you are and that you need one…

Anybody who then goes to see the financial counsellor is suddenly in this awful position where they have filled out one form in a mad rush, in absolute terror of something terrible happening to them, and then they go to fill out a form with the financial counsellor and they do not match.

Everybody, even the most literate people, will make mistakes in a rush.[43]

3.41 In contrast, opponents of a 28-day stay period argued that debtors would not necessarily use the additional time as envisaged by the government, and this leeway would be to the detriment of legitimate creditors. For example, the AFC submitted:

> Ideally, providing a longer period [than seven days] would encourage greater dialogue between debtors and creditors with a view to working out alternative arrangements to settle debts. In reality there are doubts that the 28 days would be used for that purpose. In the meantime, legitimate judgement debts cannot be enforced.[44]

3.42 The ABA agreed:

> …the ABA considers that the stay on creditors' rights of enforcement for 28 days is too long when taking into account the interests of creditors whose judgment debts cannot be enforced in that period and that 14 days would be a better balance with the need for the debtor to understand the implications of bankruptcy and other options that may be available.[45]

3.43 Westpac concurred, stating:

> The proposed 28 day moratorium is too long and likely to create an excessive delay in agreeing a customer solution.
>
> A 14 day moratorium strikes the right balance between the debtor and creditor(s), assisting in retaining a sense of urgency while providing a more reasonable timeframe for both parties to reach an appropriate outcome.[46]

Department response

3.44 The Department considered 28 days to be a 'happy medium', during which time debtors might be able to 'get themselves back on their feet'. Officers affirmed that the government does not support a shorter time period, on the basis that such a period would not give debtors sufficient time to make a considered decision:

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43 Ms Katherine Lane, Principal Solicitor, Consumer Credit Legal Centre (NSW), *Committee Hansard*, 28 January 2010, p. 14. For similar arguments, see also Legal Aid NSW, *Submission 6*, p. 3; and Consumer Credit Legal Centre (NSW), *Submission 11*, p. 6.

44 Australian Finance Conference, *Submission 12*, pp 2-3.

45 Australian Bankers' Association, *Submission 7*, p. 3.

46 Westpac, *Submission 9*, p. 2.

> There are long waiting lists for appointments with financial counsellors and if a person has multiple creditors it may take some time to negotiate with all of them. Creditors will also benefit from the new requirement that the official receiver must notify them when a declaration of intent is lodged. This allows creditors to be proactive in negotiating with debtors who can then possibly avoid bankruptcy. In addition, the requirement to file a simple statement of affairs with a declaration makes it more likely the debtors will have considered their situation and received advice before deciding what steps to take next. Of course, it will always be open to creditors and debtors to reach a negotiated agreement in less than 28 days.[47]

3.45 Departmental officers acknowledged the concern that some debtors might not use the extended stay period as intended. In this regard, officers stated that the requirement for a declaration of intent to be filed with a statement of affairs will assist in the tracking of any dissipated assets:

> If…[debtors] then proceed into bankruptcy, that act of bankruptcy which has occurred before they actually become bankrupt, as long as it occurs within the six months prior to bankruptcy, will be the start of their bankruptcy. Everything that happened from the day that they file this declaration will be undone if they do eventually become bankrupt, which is arguably more likely if they are using that period to defeat their creditors.[48]

3.46 Officers from the Department and ITSA also told the committee that the statement of affairs intended to be filed with a declaration of intent will be a simple three-page document, the sole purpose of which will be to serve as a record of assets and not as a forensic document.[49]

Committee's view

3.47 Based on the evidence presented throughout the inquiry, the committee considers that the Bill should be passed in its present form.

3.48 The committee notes that the purpose of the Bill is to modernise the national personal insolvency scheme and to make it more efficient. While the Bill contains numerous provisions to this effect, the inquiry focussed on the proposed measures to assist debtors who owe relatively small amounts. Those measures aim to improve opportunities to consider options, reorganise affairs, and, where possible, avoid bankruptcy.

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47 Dr James Popple, First Assistant Secretary, Civil Law Division, AGD, *Committee Hansard*, 28 January 2010, pp 16-17. See also Ms Giulia Inga, Official Receiver, ITSA, *Committee Hansard*, 28 January 2010, p. 20.

48 Mr David Bergman, Assistant Secretary, Bankruptcy Policy Branch, *Committee Hansard*, 28 January 2010, p. 21.

49 Mr David Bergman, Assistant Secretary, Bankruptcy Policy Branch, *Committee Hansard*, 28 January 2010, pp 19-20; and Ms Giulia Inga, Official Receiver, ITSA, *Committee Hansard*, 28 January 2010, p. 20.

3.49 In this context, the committee considers it appropriate to increase the existing $2,000 threshold for a creditor's petition to $10,000. The threshold should recognise significant changes in personal debt levels over the past 14 years, as well as the cost and complexity of bankruptcy proceedings (as compared with other available debt collection methods), and the magnitude of the consequences that bankruptcy has for a debtor. The committee adds that, in this day and age, it would be harsh and punitive to bankrupt an individual on the basis of a debt as low as $2,000. The committee accepts that $10,000 is an amount that appropriately balances the interests of all relevant parties.

3.50 In relation to debt agreements, the committee supports the proposal to increase the eligibility threshold by 20 per cent. The committee endorses the availability of debt agreements as an alternative to bankruptcy proceedings, and accepts the Department's evidence that debt agreements provide far superior returns to creditors than the bankruptcy system. While available statistics are somewhat confusing, they do suggest that debt agreements are fulfilling their purpose. The committee welcomes the Department's proposed review of the debt agreement regime later this year, and looks forward to the outcomes of that review.

3.51 As far as the stay period is concerned, the committee agrees that the period should be increased from seven to 28 days to allow debtors a greater opportunity to review and organise their affairs. The committee notes that there are existing mechanisms to deal with debtors who misuse the stay period by dissipating assets.

3.52 On a final note, the committee observes the numerous comments regarding the stress that financial hardship can place on debtors and their families. The Bill's objective is to seek to assist such people as much as possible. The committee concurs with this objective and suggests that, when the Bill comes into operation, the Australian Government take steps to better educate and inform debtors of their legal position and options available to them to avoid bankruptcy.

Recommendation 1

3.53 The committee recommends that the Senate pass the Bill.

Senator Trish Crossin

Chair

ADDITIONAL COMMENTS BY LIBERAL SENATORS

1.1 Liberal senators do not agree with the majority report's conclusions regarding the creditor's petition threshold, the increase in the stay period, or the increase in the eligibility threshold for debt agreements.

The creditor's petition threshold

1.2 Liberal senators acknowledge that the 1996 threshold for a creditor's petition is no longer realistic. However, the evidence received by the committee, including from the Department, did not clearly substantiate the need for a five-fold increase in the threshold. In particular, Liberal senators note that CPI changes would have increased the 1996 amount of $2,000 to $2,770 in 2009 dollars.[1] This is consistent with the change in the real value of money since 1996. It is also consistent with the concerns of small business whose position should not be unfairly prejudiced by this Bill. For these and other reasons, Liberal senators accept the evidence that a threshold of $5,000 would be more balanced, and therefore appropriate. This sum is also broadly in line with indexation.

Recommendation 1

1.3 Liberal senators recommend that items 1 to 3 of Part 1 of Schedule 4 of the Bill be amended to reflect a threshold amount of $5,000.

Increase in the stay period

1.4 In respect of the stay period, Liberal senators agree with the evidence stating that a 28-day stay period is too long. Liberal senators are of the view that a 14-day stay period would grant debtors sufficient opportunity to consult with financial advisors and reorganise their affairs, without unduly prejudicing the rights and interests of creditors.

Recommendation 2

1.5 Liberal senators recommend that item 5 of Part 2 of Schedule 4 of the Bill be amended to include a stay period of 14 days.

Increase in the eligibility threshold for debt agreements

1.6 Submitters and witnesses, such as the Consumer Action Law Centre, the Financial and Consumer Rights Council and the Consumer Credit Legal Centre

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1 AGD, Answer to Question on Notice, 29 January 2010 (8 February 2010), p. 1.

(NSW),[2] persuasively argued that the Bill should not seek to increase the eligibility threshold for debt agreements until the findings of past and future reviews of the debt agreement regime have been taken into account. In particular, reference was made to a departmental review to be undertaken in mid to late 2010. Liberal senators agree that it would be prudent to await the outcomes of the pending review of the debt agreement regime rather than attempting to address issues in a piecemeal, and perhaps counterproductive, fashion. To this end, Liberal senators do not support the Bill's current proposal to increase the eligibility threshold for debt agreements.

Recommendation 3

1.7 Liberal senators recommend that item 11 of Part 2 of Schedule 4 of the Bill be removed, pending the outcomes of the 2010 departmental review of the debt agreement regime.

Recommendation 4

1.8 Subject to the above recommendations, Liberal senators recommend that the Senate pass the Bill.

Senator Guy Barnett

Deputy Chair

Senator Mary Jo Fisher

2 Consumer Action Law Centre, *Submission 3*, p. 7; Financial and Consumer Rights Council, *Submission 5*, p. 8; and Consumer Credit Legal Centre (NSW), *Submission 11*, p. 10.

APPENDIX 1

SUBMISSIONS RECEIVED

Submission Number	Submitter
1	Australian Institute of Credit Management
2	PPB
3	Consumer Action Law Centre
4	Bartier Perry
5	Financial and Consumer Rights Council (FCRC)
6	Legal Aid NSW
7	Australian Bankers' Association
8	Insolvency Practitioners Association
8a	Insolvency Practitioners Association
9	Westpac Banking Corporation
10	PILCH Homeless Persons' Legal Clinic
11	Consumer Credit Legal Centre (NSW) Inc
12	Australian Finance Conference
13	Insolvency and Trustee Service Australia
14	Abacus - Australian Mutuals
15	Australian Financial Counselling and Credit Reform Association

ADDITIONAL INFORMATION RECEIVED

1. Answer to Question on Notice - Provided by Insolvency Practitioners Australia on Monday, 1 February 2010

2. Answer to Question on Notice - Provided by Attorney-General's Department on Monday, 8 February 2010

3. Answer to Question on Notice - Provided by Insolvency and Trustee Service Australia on Thursday, 11 February 2010

4. Document Tabled by Insolvency and Trustee Service Australia at a Public Hearing in Sydney on Thursday, 28 January 2010: 2009 December Quarter Provisional Personal Insolvency Statistics

APPENDIX 2

WITNESSES WHO APPEARED BEFORE THE COMMITTEE

Sydney, 28 January 2010

BERGMAN, Mr David, Assistant Secretary, Bankruptcy Policy Branch
Attorney-General's Department

COX, Ms Karen, Coordinator
Consumer Credit Legal Centre (NSW) Inc

CSETI, Ms Del, National Training and Marketing Manager
Australian Institute of Credit Management

GUTHRIE, Ms Fiona, Executive Director
Australian Financial Counselling and Credit Reform Association

INGA, Ms Giulia, Official Receiver
Insolvency and Trustee Service Australia

LANE, Ms Katherine, Principal Solicitor
Consumer Credit Legal Centre (NSW) Inc

MITRA, Mr Dipen, Assistant National Manager
Information Registry, Insolvency and Trustee Service Australia

MURRAY, Mr Michael Hugh, Legal Director
Insolvency Practitioners Association of Australia

POPPLE, Dr James, First Assistant Secretary, Civil Law Division
Attorney-General's Department

RICH, Ms Nicole, Director, Policy and Campaigns
Consumer Action Law Centre