Bankruptcy Legislation Amendment Bill 2001
Bankruptcy Legislation Amendment Bill 2001

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Law and Bills Digest Group
25 July 2001
Bankruptcy Legislation Amendment Bill 2001

Date Introduced: 7 June 2001
House: House of Representatives
Portfolio: Attorney-General

Commencement: On Proclamation or 6 months after Royal Assent, whichever is the earlier. The commencement of a few items relating to the change from the Administrative Appeals Tribunal to the Administrative Review Tribunal is deferred, reflecting the delay in the passage of the Administrative Review Tribunal Bill 2000.

Purpose

To make a number of significant changes to the Bankruptcy Act 1966 which, it is hoped, will encourage debtors to seriously consider using alternatives to bankruptcy where possible, and will make bankruptcy less of an ‘easy option’.

Background

The Commonwealth has power, pursuant to section 51(xvii) of the Constitution, to regulate bankruptcy and insolvency. Under this power, it has enacted the Bankruptcy Act 1966, which applies to an individual who is unable to pay his or her debts. Company insolvency matters are regulated separately by the Corporations Law. Although sometimes the words ‘bankruptcy’ and ‘insolvency’ are used interchangeably, ‘insolvency’ is a broader term. It refers to the inability to satisfy creditors or discharge liabilities, whereas technically ‘bankruptcy’ refers only to the formal process of being adjudged insolvent by a court.

The administration of personal bankruptcy matters (but not company insolvencies) is carried out by the Insolvency and Trustee Service Australia (ITSA) which is an executive agency within the Attorney-General's portfolio. Prior to 1 July 2000, ITSA was a part of the Attorney-General’s Department. The administrative head of ITSA is the Inspector-General in Bankruptcy.

The Official Trustee in Bankruptcy is a body corporate established under section 18 of the Bankruptcy Act 1966. Official Receivers act on behalf of the Official Trustee in

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Bankruptcy. There is one Official Receiver appointed for every bankruptcy district in Australia, that is, for each State and each of the Northern Territory and the ACT.

Basic overview of bankruptcy

The primary purposes of modern bankruptcy law are twofold. First, it enables proceedings to be taken to recover most kinds of property from a person who is unable to pay his or her accumulated debts, and use that property to pay the creditors in proportion to the amounts each is owed. Secondly, once a debtor’s property has been distributed among creditors, bankruptcy law enables the debtor to make a fresh start free from the burden of accumulated debts. In earlier times (commencing at the end of the 13th century in England), debtors could be imprisoned for non-payment of their debts.

The first step in the bankruptcy process is usually when a person petitions an Official Receiver for his or her own bankruptcy. In 1999-2000 approximately 95 per cent of all bankruptcies resulted from a debtor's petition. The other 5 per cent of bankruptcies resulted from a creditor’s petition. This is an application by a creditor to either the Federal Court or the Federal Magistrates’ Court for a sequestration order, where a debtor owes a debt of at least $2000 (or debts totalling at least $2000), and has committed an ‘act of bankruptcy’. Once a sequestration order is made, the debtor becomes bankrupt.

When an individual becomes bankrupt his or her property and finances are placed in the hands of a trustee in bankruptcy. In approximately 94 per cent of all bankruptcies, the trustee is the Official Trustee. In the remaining 6 per cent of cases, the trustee in bankruptcy is a private ‘registered trustee’, an accountant who must be registered under the Bankruptcy Act 1966.

The trustee collects and realises all the debtor’s available property. The trustee then calls for detailed claims from creditors as to what debts the debtor owes them. These are known as ‘proofs of debt’. The trustee then distributes the proceeds of the sale to the creditors in order of priority. If the trustee cannot pay a class of creditors in full, they are paid in proportion to the debts owed to each.

Most of a debtor’s property is available to pay creditors, but certain property – including basic household furniture and effects, certain tools of trade or property used to earn a living, and a car up to a certain value – is exempt. In addition, certain transactions entered into prior to the petition for bankruptcy (in some cases dating back as far as 5 years) are rendered void, and the money or property must be handed over to the trustee for distribution to creditors. A bankrupt who earns income during the period of bankruptcy must also contribute some of his or her income above a threshold amount to the estate, to be divided among the creditors.

After three years, a bankrupt is automatically discharged from bankruptcy, unless the trustee or Official Receiver objects, in which case the discharge is postponed for either two or five years, depending on the ground of objection. A person is also eligible to

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apply for early discharge of bankruptcy at any time after 6 months in certain circumstances.\textsuperscript{15} Discharge of bankruptcy releases a person from any future obligation to pay the portion of debts which may remain unpaid after the bankruptcy period has ended. However, certain debts remain payable, such as child maintenance and bail bonds.\textsuperscript{16} There is also currently a bill before Parliament which proposes excluding any accumulated HECS debt or semester debt from cancellation on discharge from bankruptcy.\textsuperscript{17}

There are three alternatives to actual bankruptcy provided for in Part X of the \textit{Bankruptcy Act 1966}, which are entering into a \textit{deed of assignment},\textsuperscript{18} a \textit{deed of arrangement}\textsuperscript{19} or a \textit{composition} with creditors.\textsuperscript{20} There are a number of specific formal procedures applicable to Part X arrangements, including procedures for meetings of creditors. Since 1996, there has also been a simplified, low cost alternative procedure, a \textit{debt agreement} under Part IX,\textsuperscript{21} which is designed for debtors with relatively low levels of debt, low income and few assets.

**Increase in incidence of bankruptcy and need for reform**

Bankruptcies have increased threefold over the past ten years to a level of 23,298 in 1999-2000, compared with 8,493 in 1989-1990. The clear majority of bankruptcies are not business-related. In the financial year 1999-2000 there were 3,899 (16.7\%) business-related bankruptcies\textsuperscript{22} and 19,399 (83.3\%) non-business bankruptcies. The proportion of business-related bankruptcies has halved in the last 10 years, from 34.7 per cent in 1989-1990.\textsuperscript{23}

There were also 801 Part IX debt agreements accepted by creditors in 1999-2000.\textsuperscript{24} The use of debt agreements has increased exponentially since they were first introduced in 1996. There were 47 debt agreements in 1996-1997, 369 in 1997-1998, and 480 in 1998-1999.\textsuperscript{25}

In contrast to bankruptcy and other alternatives to bankruptcy, the use of Part X arrangements has declined significantly. In 1999-2000, only 453 arrangements, assignments and compositions under Part X were accepted,\textsuperscript{26} compared with approximately 800 a decade ago.\textsuperscript{27} This decline is not solely attributable to the introduction of the alternative Part IX debt agreements, as it began several years prior to 1996.

Commenting on the general increase in the incidence of bankruptcy, Terry Gallagher, the Inspector-General in Bankruptcy, has stated that:\textsuperscript{28}

> While it is no easier to go bankrupt now than it has been for many years it is likely that excessive borrowing prompted by ready credit availability, perceptions of attainable living standards and a lessening of the stigma of bankruptcy have contributed to this increase.
There has been significant controversy in recent times over revelations that several Sydney barristers, including high-ranking Queen’s Counsel, were using bankruptcy as a means of avoiding paying substantial amounts of tax. The Attorney-General is reported to have denied that the present amendments are a response to these revelations.\textsuperscript{29} Other, non-legislative, measures have been introduced to address this problem,\textsuperscript{30} and State and Territory governments are encouraged to deal legislatively with the issue. New South Wales has recently introduced legislation to make it clear that certain acts of bankruptcy constitute professional misconduct and render a barrister or solicitor liable to be struck off unless he or she can give a satisfactory explanation.\textsuperscript{31}

Although some of the amendments proposed in the Bill will increase the powers of regulatory bodies to deal with high-income earners who are using bankruptcy to avoid their debts, the majority of the amendments appear to have arisen out of concern at the general increase in the number of bankruptcies. The clear majority of bankrupts are in fact low income earners\textsuperscript{32} who owe creditors relatively small amounts of money,\textsuperscript{33} rather than high-profile bankrupts. In this context, many of the amendments are targeted at consumers who ‘overspend on their credit cards or run up debts with small businesses’, and divorcees who use bankruptcy to avoid sharing property with a former spouse.\textsuperscript{34} The Government has proposed the present reform package in the hope that the amendments will counter community perceptions that it is ‘too easy’ to become bankrupt\textsuperscript{35} by encouraging ‘people contemplating bankruptcy to consider the seriousness of the step they are about to take and to try alternatives to bankruptcy,’\textsuperscript{36} as well as restoring community confidence in the bankruptcy system, by ‘clamp[ing] down on those who use bankruptcy in a mischievous or improper way’.\textsuperscript{37}

The major reforms proposed are:

- the introduction of a mandatory 30 day cooling-off period to encourage debtors to enter into a settlement with creditors
- giving the Official Receiver a discretion to reject a debtor’s petition which appears to be an abuse of the bankruptcy process
- the abolition of early discharge provisions
- strengthening trustees’ power to make objections to discharge
- strengthening the Court’s power to annul bankruptcy, and
- doubling the income threshold for debt agreements.

An explanation of each of the main reform proposals is provided separately in the Main Provisions section. The Bill also proposes a large number of other amendments to the Bankruptcy Act, including changes to the trustee registration scheme, changes to the voting procedures for meetings of creditors, and changes consequential on ITSA becoming an executive agency separate from the Attorney-General’s department.
Exposure drafts of the Bill and its companion, the Bankruptcy (Estate Charges) Amendment Bill 2001, were circulated in early 2001, after drafting notes were circulated in December 2000. Briefing sessions and consultation forums with industry groups including members of the Bankruptcy Reform Consultative Forum and groups of registered trustees, legal practitioners and financial counsellors in each State were held in February 2001.38 As a result of these consultations, the Government agreed to some changes to the original proposal.

The Bills have now been referred to the Senate Legal and Constitutional Committee for report by 7 August 2001.

**Main Provisions**

The six major reform proposals fall into three main groups, provisions aimed at making bankruptcy more difficult, those which encourage use of alternatives to bankruptcy, and those which address abuses of the bankruptcy system.

**Provisions aimed at making bankruptcy more difficult**

**Abolition of early discharge provisions**

Currently, the standard period of bankruptcy is three years.39 After three years, bankruptcy is automatically discharged unless an objection to discharge is lodged. However, a bankrupt is eligible for early discharge of bankruptcy at any time after 6 months, if he or she satisfies certain criteria. Early discharge is only available for those on a low income who are unable to pay their creditors at all, or who are unable to pay the trustee’s remuneration and expenses in full.40 However, a person may not apply for early discharge if his or her debts exceed 150 per cent of his or her income, or he or she is otherwise disqualified.41

Under the current law, about 60 per cent of all bankrupts are eligible for early discharge, and about half of these actually seek to be discharged early.42 The Bill proposes to abolish the early discharge provisions altogether (item 154).43 Now, the minimum period of bankruptcy will be three years and there will be no exceptions. It was earlier proposed to reduce the standard period of bankruptcy to two years rather than three,44 as a trade-off for removing the early discharge, but this proposal has not been carried through.

The former Minister for Justice and Customs, Senator Amanda Vanstone, explained the abolition of early discharge provisions by saying: ‘many creditors feel that the possibility of being released from bankruptcy after six months does not reflect the serious nature of the decision to become bankrupt.’45 It was also felt that early discharge provisions ‘discourage debtors from trying to enter formal or informal arrangements with their
creditors to settle debts, and provide little opportunity for debtors to become better financial managers’.46

Other justifications advanced by the Government for the abolition of the early discharge provisions are:47

- they were initially intended to apply to those who became bankrupt out of misfortune (those with few assets and low incomes) rather than misdeed, but it seems inappropriate to thus imply that all those with some assets or income have been guilty of incurring debts in bad faith, and

- they apply in a discriminatory way, by excluding women who have joint debts with, and generally a lower income than, their spouse, and thus are disqualified by the 150% rule.

Provisions encouraging use of alternatives to bankruptcy

Doubling the income threshold for debt agreements

As described above, Part IX debt agreements are intended to provide a simple, low cost alternative to the various Part X arrangements. They are currently only available to debtors whose annual after-tax income is less than $30 530. This relatively low threshold has been criticised as denying a considerable number of debtors ‘any realistic alternative to bankruptcy’.48

The Bill proposes to double the after-tax income threshold for eligibility to enter into debt agreements, to approximately $61 000 (item 177), which will ensure a much wider group of debtors has access to Part IX debt agreement arrangements.

In future, the Official Receivers rather than the Official Trustee will have responsibility for the functions relating to debt agreements (items 171-176, 178, 180, 182-193).

Mandatory 30 day cooling-off period

Currently, there is effectively an optional 7 day cooling-off period in the Bankruptcy Act 1966. This arises because a debtor has a choice to simply present a debtor’s petition for bankruptcy, or to first present a declaration of intention to present a debtor’s petition. If a debtor lodges a declaration of intention, a 7 day stay period applies during which most debts (excepting secured debts and child maintenance obligations) are frozen and cannot be enforced by creditors.49 At the end of this period, the protection is removed, and the debts become enforceable again. A debtor may, but does not have to, present a debtor’s petition after lodging a declaration of intention.

The Bill repeals the provisions dealing with a declaration of intention and the 7 day stay period (item 38)50 because it proposes the introduction of a mandatory 30 day cooling-off period after a debtor’s petition is presented (new subsections 55(4B) and 57(5A)). This

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means that debtors will not become bankrupt until 30 days after presenting their petition. This is designed to give debtors who may have acted hastily an opportunity to reconsider whether bankruptcy is the best option, as well as to give creditors an opportunity to negotiate an alternative arrangement with the debtor.\(^{51}\)

However, under new subsections 55(4B) and 57(5A) the cooling off period will not be available in a number of circumstances, including:

- where the debtor has already unsuccessfully attempted an alternative to bankruptcy (such as a Part IX debt agreement or a Part X arrangement) in the preceding 12 months,
- the debtor was carrying on a business during the 30 days prior to presenting a petition, or
- where a creditor’s petition or other legal proceeding for recovery of a debt of at least $2000 is already pending against the debtor.

The Official Receiver also has a discretion to determine that the cooling-off period does not apply, if it is likely to result in a reduction of the dividend to creditors (new subsections 55(4C) and 57(5B)). The cooling-off period also does not apply where a debtor lodges a debtor’s petition as a member of a partnership (items 50 and 51), or in the case of deceased estates. If the cooling-off period does not apply for any of these reasons, then the debtor becomes bankrupt immediately on the presentation of the petition (new subsections 55(4D) and 57(5C)).

If the cooling-off period applies, then the debtor can withdraw the petition at any time within the 30 days, and avoid bankruptcy (new subsections 55(4E) and (4F) and 57(5D) and (5E)).\(^{52}\) If the petition is not withdrawn, the debtor becomes bankrupt after 30 days (new subsection 55(4G) and 57(5F)).

During the cooling-off period, most of the debtor’s debts are frozen and cannot be enforced by creditors (new sections 55A and 57AA). This does not apply to new debts incurred during the cooling-off period. However, a creditor may apply for a court order under new section 55B or 57AB directing a trustee to take control of the debtor’s property during the cooling-off period. A court must grant this order if it would be in the interests of creditors.

Provisions targetted at abuses of the bankruptcy system

**Official Receiver's discretion to reject a debtor's petition**

Currently, an Official Receiver has only limited power to reject a debtor’s petition. He or she has a discretion to reject a debtor's petition only if the petition does not comply substantially with the approved form, the petition is not accompanied by a statement of
affairs, or if he or she thinks that the statement of affairs accompanying the petition is inadequate.53

The Bill proposes that, in addition to these reasons, Official Receivers be given a discretion to reject a debtor’s petition where it appears that the debtor would be likely to be able to pay all of his or her debts in a reasonable time, and one of the following applies:

- the debtor appears unwilling to pay one or more creditors, or
- the debtor has been bankrupt on his or her own initiative at least three previous times, or
- the debtor has previously been bankrupt on his or her own initiative in the last 5 years (items 40 and 60).

This amendment is directed at abuses of the bankruptcy system by people with a capacity to pay their debts who have either singled out a particular creditor for non-payment (such as the Australian Tax Office) or who are multiple bankrupts.54

The Official Receiver does not have to make use of this power, and any decision to refuse a debtor’s petition on this ground is subject to review by the Administrative Appeals Tribunal.

In addition, an Official Receiver must reject a debtor’s petition where the debtor (or each debtor in the case of joint debtors) does not have a connection with Australia, either through residency or carrying on a business here.55 This restriction already applies to bankruptcies on a creditor’s petition.56

**Strengthening the Court’s power to annul bankruptcy**

Currently, the Federal Court and the Federal Magistrates’ Court have power to annul a bankruptcy if the sequestration order (in the case of a creditor’s petition) or the petition (in the case of a debtor’s petition) ‘ought not to have been’ made.57 This power has been interpreted as being limited to situations where the debtor is ineligible for bankruptcy, for example, the debtor is in fact solvent, or where the bankruptcy is an abuse of process or a fraud on the court. Commentators suggest that it is generally not possible to annul a bankruptcy where the debtor is insolvent.58

The Bill proposes an amendment to make it clear that in the case of a debtor’s petition, the Court will have power to annul a bankruptcy which ‘ought not to have been’ made even where the debtor is insolvent (item 156). The *Explanatory Memorandum* notes that this power is intended to apply in the case of high income bankrupts who are technically insolvent but could make arrangements to pay their debts (including their tax liabilities), although ‘they choose not to while maintaining an expensive lifestyle’. These situations could be considered by a court to be an abuse of the bankruptcy process, leading the Court to annul the debtor’s petition.59
Strengthening of objections to discharge

As noted, most bankruptcies are automatically discharged after the expiry of three years. However, if an objection to discharge is made, the period of bankruptcy may be extended for another two or five years, depending on the ground of objection.\(^{60}\)

Currently, the trustee or an Official Receiver may lodge an objection to discharge. The Bill proposes to remove the Official Receiver’s power to object (items 133, 134, 141-146,\(^{61}\) 148, 151), on the basis that this is more appropriately a function for the trustee.

The Government believes that it is difficult for trustees to successfully sustain objections to bankruptcy. This is because of two main factors. First, in addition to identifying a ground of objection (something in the bankrupt’s conduct), a trustee must give a reason for objecting to discharge. This may be to advance the administration of the bankrupt estate, or to force the bankrupt to discharge a duty he or she has not discharged. However, it is not a permissible reason to punish the bankrupt for failure to cooperate with the trustee.\(^{62}\)

Secondly, objections by trustees are frequently cancelled on review by the Inspector-General, the Administrative Appeals Tribunal or the Federal Court. Often this occurs when a bankrupt has been uncooperative in refusing to provide information, and just before or even during a review hearing the bankrupt finally provides the information requested by the trustee.\(^{63}\) The Government considers these provisions do not encourage bankrupts to cooperate with trustees in the administration of their bankruptcy. The Government proposes to strengthen the objection-to-discharge provisions where a ‘special ground’ exists, by removing the need for the trustee to give a reason for objecting to discharge, and making it more difficult for review bodies to cancel an objection to discharge.

‘Special grounds’

The Bill identifies a list of grounds, to be known as ‘special grounds’, which will be sufficient to found an objection to discharge. If an objection to discharge is made on a special ground, the bankruptcy will be extended by five years (item 130). Many of the existing grounds which would result in an extension of the bankruptcy period by five years will become special grounds, including:

- failing to return to Australia when requested to by the trustee
- failing to provide information about property, income or expected income to the trustee on request
- failing to provide particulars of income or expected income
- failing to pay an income contribution to the trustee during the bankruptcy period, and
- failing to explain to the trustee a disposal of property or expenditure of money during the 5 years preceding the bankruptcy.
One ground which currently extends a bankruptcy by two years will be classified as a special ground. This is refusal or failure to sign a document when required to do so by the trustee. The Bill additionally proposes four new special grounds:

- transfer of property with the intention of defeating creditors (item 136)
- intentionally providing false or misleading information to the trustee after becoming bankrupt (item 137)
- intentionally failing to disclose a liability (item 138), or
- intentionally failing to disclose a beneficial interest in property (item 140).

Failing to disclose a liability or a beneficial interest in property are already, and will continue to be, grounds which result in a two year extension of bankruptcy, whether or not the failure to disclose was intentional. They will constitute ‘special grounds’ resulting in an extra five years of bankruptcy only where there has been an intentional failure to disclose.

‘Special grounds’ are significant for two reasons. First, the trustee will not have to provide a reason for objecting to a bankrupt’s discharge if at least one special ground is present (item 135). This means that the sole purpose of the objection may be to punish the bankrupt for non-cooperation, the objection need not further the administration by the trustee in any way.

Secondly, an objection which specifies at least one special ground must not be cancelled by a review body if there is sufficient evidence to support the ground and the bankrupt fails to provide a reasonable excuse for his or her conduct (new subsection 149N(1A)). Additionally, review bodies must not take into account any conduct of the bankrupt after the ground first commenced to exist (new subsection 149N(1B)).

Ordinary grounds of objection

If an objection to discharge is made on an ordinary ground, the bankruptcy period will be extended by two years (item 130). Three grounds which currently increase a bankruptcy period by five years will not be classified as ‘special grounds’, and in future will result in an increase in the period of bankruptcy of only two years. One of these is engaging in misleading conduct after the date of bankruptcy concerning amounts totalling in excess of $3000. From the bankrupt’s perspective, the culpability involved in misleading conduct seems broadly comparable to the ‘special ground’ of providing false or misleading information, although the latter affects the trustee in his or her conduct of the administration whereas the former affects potential future creditors of the bankrupt.

Grounds which will extend the period of bankruptcy for two years include:

- failing to disclose a liability or a beneficial interest in property
• failing to attend a meeting of creditors or a bankruptcy examination without excuse, and

• failing to notify the trustee of change of name, address or daytime telephone number.

In addition, the Bill puts forward two new ordinary grounds of objection:

• transfer of property at an undervalue or for no consideration, or to give preference to one creditor over others (item 136), and

• failure to notify the trustee of any material change in the bankrupt’s circumstances (items 86 and 139).

If a trustee objects to discharge of bankruptcy on one of these grounds, he or she will have to provide a reason for his or her objection to discharge. Further, the bankrupt’s conduct after the objection arose will continue to be relevant in review proceedings seeking to have the objection cancelled. This is to be contrasted with objections based on a ‘special ground’, for which no reason needs to be given, and in relation to which any post-objection conduct of the bankrupt is to be disregarded.

Other amendments

The Bill makes a number of other amendments of a minor or machinery nature. The majority of these are succinctly summarised in a description of the bankruptcy reforms package prepared by Don Costello of ITSA.66

A number of items remove references to the ‘Department’ or the ‘Secretary’ of the Department, and substitute references to ITSA and the Minister (items 8, 10, 13, 17, 18, 19, 103, 157, 162, 164, 168). This is because ITSA is now an APS executive agency separate from the Attorney-General’s Department. Although the Inspector-General and all the Official Receivers will now be appointed directly by the Minister rather than by the Secretary of the Department, the current appointments will continue in force (items 229 and 230).

Concluding Comments

The majority of the reforms proposed do not appear to have generated significant opposition. In part, this may be a function of the consultation process which was undertaken prior to the Bill being introduced, which gave interest groups an opportunity to comment on the reform proposal, as a result of which the Government subsequently altered some of the details of the measures. Some concerns exist in relation to objections to discharge, and alternatives to bankruptcy.
Concerns about bankruptcy alternatives

Consumer advocates have welcomed the expansion of eligibility for debt agreements, which will allow many middle income earners to access this alternative to bankruptcy. At the same time, however, Virginia Noonan of the Financial Consumer Rights Council is concerned that this could result in low-income debtors entering into private arrangements with creditors which they are unable to fulfil, because they are unlikely to be able to afford an accountant to negotiate on their behalf the terms of a debt agreement with creditors. A similar concern arises in relation to the mandatory 30 day cooling off period, which will give creditors time to approach debtors with alternative repayment options. The difficulty is not so much with the Bill, which merely provides the option of bankruptcy alternatives, but with the difference in bargaining power between some debtors and creditors, which may lead debtors to agree to terms or arrangements which they are unable to meet.

Concerns about the strengthening of objections to discharge

The amendments proposed in the Bill will make it easier where a ‘special ground’ exists for a trustee to sustain an objection to discharge of bankruptcy at the end of the three year period, and harder for a bankrupt to have an objection cancelled. The Attorney-General noted that the ‘special grounds’ ‘will apply to deliberate actions by bankrupts which frustrate trustees, and add unnecessarily to the costs of administrations.’ The four new special grounds proposed in the Bill all cover intentional actions by the bankrupt. However, none of the six existing grounds which will be classified as special grounds need necessarily be deliberate actions. The word ‘failure’ contained in each of those grounds has been interpreted in the context of bankruptcy as imposing a strict liability on the bankrupt, whether the relevant conduct was intentional or non-intentional. For example, a bankrupt may fail to provide information, or may fail to return from overseas when requested, either because he deliberately intends not to cooperate with the trustee, or because he has been unavoidably absent by reason of family circumstances.

Yet the mere existence of any of these grounds, including a ground based on non-intentional conduct, will be sufficient to extend the period of bankruptcy by a further five years on top of the initial three year standard period of bankruptcy. This is a serious sanction, which may be justifiable in cases where a bankrupt is deliberately being non-cooperative with a trustee, but seems excessive in other circumstances.

Additionally, it seems incongruous that no reason needs to be given when a trustee objects on a ‘special ground’, when the consequence of such an objection is five additional years of bankruptcy, whereas the trustee must provide a reason for pursuing an objection relating to non-intentional conduct leading to only two extra years of bankruptcy.

A further difficulty is posed by the removal of the power of review bodies to cancel an objection based on conduct of the bankrupt after the objection is lodged but prior to
review. The Bill would permit a review body to cancel a trustee’s objection on a special ground where the bankrupt is able to demonstrate a ‘reasonable excuse’. This seems intended to safeguard bankrupts whose conduct was not intended to frustrate the trustee. However, it may be difficult for bankrupts to prove a reasonable excuse if, as the Bill provides, their subsequent conduct (for example, in providing an explanation to the trustee as to why they belatedly complied with his or her request) may not be taken into account.

It is true that the trustee retains a discretion not to file an objection in most cases, or to withdraw an objection at any time. It may be that trustees confronted with genuine cases of hardship will not pursue an extension of the bankruptcy period. However, the Bill on its face would permit them to maintain their objection, as it does not require them to give a reason justifying their decision to object. It is of concern that the new provisions are framed to give this power to the trustee, and to remove avenues of review from the various review bodies, particularly when the consequence of establishing a special ground is serious.

Typographical error

The reference in new paragraph 149N(1A)(c) (item 149) to paragraph 149D(1)(h) may be a typographical error, and should be a reference to paragraph 149D(1)(f).

Will the Bill achieve its aims?

The Bill contains two proposals which will better equip the regulatory authorities to deal with abuse of the bankruptcy system by debtors with high incomes, such as the recently publicised barristers using bankruptcy to avoid paying tax. These are the power to reject a debtor’s petition which is an abuse of process, and the power to annul a bankruptcy even where the debtor is technically insolvent. Strengthening the trustee’s power to object to discharge of bankruptcy is directed at any, whether high or low income earners.

The other major proposals appear to be targetted predominantly at low income earners, who constitute the majority of bankrupts. Doubling the income threshold for eligibility to enter into a debt agreement, and enforcing a mandatory 30 day cooling off period prior to bankruptcy commencing are both proposals aimed to encourage debtors to consider alternatives to bankruptcy. Consonant with this, the Bill intends to make the bankruptcy process more difficult and hence less attractive to debtors, by abolishing the opportunity for early discharge, and by introducing new powers to object to discharge and lengthen the period of bankruptcy in cases where bankrupts fail to cooperate with their trustees.

Despite these intentions, it is unclear whether the changes made by the Bill will have the desired effect of making bankruptcy more difficult. Terry Gallagher, the Inspector-General in Bankruptcy, is reported to have admitted that while the proposed reforms are important in terms of curbing abuses of the bankruptcy system, he does not expect they will result in a huge dent in bankruptcy numbers.
The Bill also does not deal specifically with other ongoing bankruptcy-related problems, such as the ability of debtors to put assets beyond the reach of creditors (for example, by transferring or acquiring assets in other people’s names), or the interaction of bankruptcy law with family law issues. A Sydney Morning Herald editorial commented ‘these changes to the bankruptcy law, though welcome, hardly begin to deal with the larger, more complicated problem.’

Endnotes

1 Subsection 18(8) of the Bankruptcy Act 1966.

2 The Jervis Bay Territory is included within the Bankruptcy District of New South Wales, and Christmas Island and Cocos (Keeling) Islands are within the Bankruptcy District of Western Australia. See proclamation of Bankruptcy Districts on 15 September 1993, Gazette GN38 on 29 September 1993, reprinted in McDonald, Henry and Meek, Australian Bankruptcy Law and Practice, (1996, revised 5th ed), Vol 1, at [13.0.10].


4 Section 55 of the Bankruptcy Act 1966.


6 The Federal Court and the Federal Magistrates’ Court have concurrent jurisdiction in bankruptcy, under section 27 of the Bankruptcy Act 1966.

7 See sections 42, 43 and 44 of the Bankruptcy Act 1966. There are a number of ‘acts of bankruptcy’ listed in section 40 of the Bankruptcy Act 1966, including assignment of property for creditors’ benefit, departure from Australia or from the debtor’s usual place of business with intent to defeat creditors, failure to pay a debt where a final judgment order has been made, and admission of insolvency at a meeting of creditors followed by failure to voluntarily lodge a debtor’s petition for bankruptcy within 7 days of the meeting.


9 See Part VIII Division 1 of the Bankruptcy Act 1966.

10 Section 116 of the Bankruptcy Act 1966.

11 These include transfers of property for no consideration or at less than market value any time in the last five years, section 120 of the Bankruptcy Act 1966.

12 These include transfers to defeat creditors, section 121 of the Bankruptcy Act 1966, or transfers in favour of a certain creditor or creditors to give them preference over other creditors, section 122 of the Bankruptcy Act 1966.


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14 Subsection 149(4) of the Bankruptcy Act 1966.
15 Sections 149S and 149T of the Bankruptcy Act 1966.
16 Section 153 of the Bankruptcy Act 1966.
17 The Higher Education Funding Amendment Bill 2001.
18 Under a deed of assignment, a debtor hands over all his or her divisible property to a trustee who divides the property for the benefit of the creditors, subsection 187(1) of the Bankruptcy Act 1966. Entry into a deed of assignment releases the debtor from those debts which would otherwise have comprised his or her bankruptcy, section 230 of the Bankruptcy Act 1966.
19 Under a deed of arrangement, a debtor's financial affairs are administered for him or her, subsection 187(1) of the Bankruptcy Act 1966. This may include running the debtor's business or assigning future income. A deed of arrangement does not release the debtor from all his or her debts unless the deed specifically so provides, section 234 of the Bankruptcy Act 1966.
20 Under a composition, creditors accept less than the full amount of the debt as full satisfaction, or agree to a schedule of instalments, subsection 187(1) of the Bankruptcy Act 1966.
21 The debtor makes a debt agreement proposal – which may involve payment of less than the full amount of the debts or periodic payments or a moratorium on payments – to the Official Trustee, and creditors decide whether or not to accept it.
22 A business related bankruptcy is defined as being one in which an individual's bankruptcy is directly related to his or her proprietary interest in a business or company: Insolvency and Trustee Service Australia, Annual Report 1999-2000, Table 2.2, p. 8.
27 Although there were only 561 Part X arrangements in 1989-1990, this figure was unusually low, as the figures for the preceding and following years were 795 and 805 respectively. This increased to 953 in 1991-1992, before beginning a steady decline. See ITSA, Quarterly Bankruptcy Statistics – Part X Administrations, http://law.gov.au/aghome/commaff/itsa/stats/Qtr_Pt_X.pdf (accessed 4 July 2001).
30 ‘Procedures will be introduced to ensure that Commonwealth departments and agencies do not engage barristers who use bankruptcy as a means of avoiding tax.’ The Hon Daryl

31 The Legal Profession Amendment (Disciplinary Provisions) Bill 2001 was introduced in the Legislative Assembly on 22 June 2001, and passed the Legislative Assembly on 26 June 2001. It was amended in the Legislative Council on 2 July 2001, and the amendment is currently before the Legislative Assembly for consideration.

32 The single biggest group by occupation in 1999-2000 was unemployed persons, with 5208 bankrupts, followed by pensioners with 2112, and housewives/househusbands with 2088. Tradespersons and labourers experienced many more bankruptcies than did managers and professionals. ITSA, Annual Report 1999-2000, Table 14, p. 29.

33 It is reported that half of all bankrupts owe unsecured creditors less than $14,000: Mary Byrne, ‘Why bankruptcy is the latest craze’, Financial Review, 28 March 2001.

34 The Hon Daryl Williams MP, Answer to Question without Notice: Bankruptcy, House of Representatives, Hansard, 6 June 2001, p. 26233.


38 Terry Gallagher, Inspector-General in Bankruptcy, ITSA, Reforms to the Bankruptcy Act.

39 Section 149 of the Bankruptcy Act 1966.

40 Section 149T of the Bankruptcy Act 1966.

41 Section 149Y of the Bankruptcy Act 1966. Other disqualifications include previous bankruptcy, or failure to disclose a number of matters, including beneficial interests in property, existing liabilities, or projected income.


43 Items 33, 46, 52, 65, 129, 132, 215 and 216 repeal other references to the early discharge provisions.


45 ibid.


Warning:
This Digest was prepared for debate. It reflects the legislation as introduced and does not canvass subsequent amendments.

This Digest does not have any official legal status. Other sources should be consulted to determine the subsequent official status of the Bill.

48 *Explanatory Memorandum*, p. 11.

49 See Division 2A of Part IV of the *Bankruptcy Act 1966*.

50 *Items 4, 5, 6, 7, 11 and 27* repeal other references to the declaration of intention provisions.


52 The only exception is that a debtor cannot withdraw a petition if a creditor has obtained a court order under *new section 55B or new section 57AB* directing a trustee to take control of the debtor’s property.

53 Subsection 55(3) of the *Bankruptcy Act 1966*.


55 *New subsection 55(2A)*, inserted by *item 39*, and *new subsection 57(2A)*, inserted by *item 59*.

56 Paragraph 43(1)(b) of the *Bankruptcy Act 1966*.

57 Technically, section 153B of the *Bankruptcy Act 1966* provides for annulment of bankruptcy if a sequestration order ought not to have been made or a debtor's petition ought not to have been presented or ought not to have been accepted by the Official Receiver. For simplicity, the text uses the phrase ‘ought not to have been’ made to cover all three.


59 *Explanatory Memorandum*, p. 35.

60 Section 149A of the *Bankruptcy Act 1966*.

61 *Item 141* also removes reference to a right of review before the Administrative Appeals Tribunal. Henceforth, the bankrupt must request internal review by the Inspector-General prior to seeking external review by the Administrative Appeals Tribunal (*item 152*). See also *item 124*.


64 Paragraph 149D(1)(c) of the *Bankruptcy Act 1966*. The other grounds are leaving Australia and not returning, and continuing to manage a corporation without leave while bankrupt, paragraphs 149D(1)(a) and (b) of the *Bankruptcy Act 1966*.
The grounds are set out in paragraphs 149D(1)(i), (j), (l), (m) and (n) of the Bankruptcy Act 1966.


ibid.


In Re Woodman and Inspector-General in Bankruptcy (1996) 40 ALD 800, the Administrative Appeals Tribunal held that the bankrupt had ‘failed’ to provide information when requested by the trustee, and thus the trustee was entitled to sustain an objection under paragraph 149D(1)(d) of the Bankruptcy Act 1966. It did not matter that the bankrupt’s failure was not deliberate, but the consequence of a heavy workload he had undertaken in an attempt to rehabilitate himself. However, the tribunal was able to cancel the trustee’s objection on the basis that the bankrupt had subsequently complied with the request and extension of bankruptcy would have adverse consequences for him. This flexibility will not be available where a ‘special ground’ exists.

Under subsection 149B(2) of the Bankruptcy Act 1966 a trustee must lodge an objection if the trustee believes there is no other way to force the bankrupt to discharge a duty which he or she has failed to discharge. In all other cases, the choice whether or not to lodge an objection is in the hands of the trustee.

Section 149J of the Bankruptcy Act 1966.

New paragraph 149N(1A)(c) provides that where a bankrupt can demonstrate a ‘reasonable excuse’, a review body may cancel a trustee’s objection to discharge, except where the objection is founded on paragraph 149D(1)(h). That paragraph contains the ground of failing to return to Australia when requested by the trustee. However, the discussion in the Explanatory Memorandum refers to the ground of non-payment of assessed contributions, Explanatory Memorandum, p. 34. This seems to suggest that the reference should be to paragraph 149D(1)(f), which contains the ground of non-payment of assessed contributions.
