

BANKRUPTCY FOR THE POOR?[©]

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The conventional wisdom is that the poor are not heavy users of the insolvency system, because creditors are unwilling to take risks on the poor and because many of the poor are judgment-proof.

However, credit is now widely available across the spectrum of income groups. In addition, poverty is often a temporary state for many Canadians; therefore, being judgment-proof is likewise temporary. Some of those who are poor at any point in time are in fact in need of bankruptcy protection. They have debts that they are unable to pay and little likelihood of being able to repay in the near future.

We begin by presenting evidence on indebtedness among families in the lower income deciles. We then turn to the main question: should the Canadian bankruptcy process be more readily available to poor debtors? Following a comparative analysis (considering the United States, Australia, New Zealand, and the United Kingdom) and analysis of interviews with Canadian bankruptcy trustees and other insolvency professionals, we offer six recommendations for reform.

La sagesse traditionnelle veut que les pauvres ne soient pas d'importants usagers du système d'insolvabilité car les créanciers ne désirent pas prendre de risques à leur égard, étant donné qu'un grand nombre d'entre eux font preuve de manque de jugement.

Toutefois, le crédit est actuellement largement disponible pour une vaste fourchette de groupes de revenus. En outre, la pauvreté est souvent un état temporaire pour nombre de Canadiens, ce qui indique que le manque de discernement est également temporaire. Certains de ceux qui sont pauvres à un moment donné ont en réalité besoin d'une protection contre la faillite. Ils sont endettés, mais incapables de payer, et il est peu probable qu'ils soient en mesure de rembourser dans un avenir proche.

À la suite d'une analyse comparative (qui examine les États-Unis, l'Australie, la Nouvelle-Zélande et le Royaume-Uni) et d'une analyse des entrevues menées auprès de syndicats de faillite canadiens et d'autres professionnels du domaine de l'insolvabilité, nous offrons six recommandations pour entreprendre une réforme.

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The research for this article was funded by the Industry Canada Office of the Superintendent of Bankruptcy Insolvency Research Initiative. Val Culp provided excellent research assistance. We would like to thank Jamie Cameron, Iain Ramsay, Mike Norris, John Pottow, Tom Telfer, Adrian Walters, Donna Skene, Jacob Ziegel, Tony Duggan, Catherine Dupont, Stephanie Cavanagh, and Dave Stewart and Steve Joannis of the Office of the Superintendent in Bankruptcy for their comments and assistance at various stages of this article. We would especially like to thank the bankruptcy trustees, members of the insolvency community, and the former bankrupt whom we interviewed. All errors remain our own.

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I. INTRODUCTION

Bankruptcy need not be synonymous with poverty. Indeed, in North America, consumer bankruptcy is a middle-class phenomenon, with debtors filing for bankruptcy from a wide array of occupations and income levels. Filing for bankruptcy requires a few thousand dollars in out-of-pocket costs in Canada and the United States. Most of those considering bankruptcy can afford to pay, drawing upon either their earnings or their friends and family.

Our concern here is with debtors who need bankruptcy but who cannot afford to pay the required costs of filing. We will call them “poor debtors,” and the first task is to define what we mean by this term. As part of the research for this article, we conducted semi-structured interviews with a number of Canadian bankruptcy trustees.¹ We asked each of these

¹ Information on the interviewees can be found in Appendix I. Bankruptcy trustees in Canada are the private intermediaries (often accountants) who are regulated and licensed by the Office of the Superintendent of Bankruptcy (OSB) and serve as gatekeepers to the consumer bankruptcy process. Given the ethical, privacy, and cost restrictions, we chose to interview trustees instead of “poor debtors” for the purposes of this study. Future work may involve more in-depth interviews with “poor debtors.”

trustees to characterize those who could not pay their normal fees, and found that the trustees shared a common vision. As one trustee put it: “These are people who live a marginal existence, on social assistance, living in government-subsidized housing and with no prospects for changing this around.”² That same trustee stated that such debtors have “no income, no friends, no family” and are “by themselves and at the end of their rope.” Others spoke of debtors with physical or cognitive disabilities,³ or of lone mothers who are immigrants with limited ability to speak English or French.⁴ Women seem to figure prominently among “poor debtors,” most likely reflecting the feminization of poverty that has occurred in recent decades.

In our view, the defining characteristic of “poor debtors” is the strong likelihood that they will experience *persistent* poverty, with or without their debts. They are not using the bankruptcy system to discharge their debts and then move on to a comfortable middle-class existence. We use the term “poor debtors” to refer to debtors seeking bankruptcy who cannot pay the fees associated with filing and who seem unlikely to attain anything but a low income for the foreseeable future.

Poor debtors should be distinguished from so-called no-income, no-asset (NINA) debtors.⁵ In the Canadian context, NINA debtors have no non-exempt assets to liquidate and no income above the Low Income Cut-offs (LICOs) calculated by Statistics Canada.⁶ Estimates suggest that 70 to 80% of bankruptcies in Canada are filed by NINA debtors. Most of these debtors, however, are able to pay the normal trustee fees. They have financial difficulties, but the depth of their poverty is far less than that of the debtors described above.

In this article, we address several questions concerning the situation of poor debtors in the Canadian context. First, how common is

² Interview with Trustee 4, 15 September 2006.

³ Interview with Trustee 5, 20 September 2006.

⁴ Interview with Trustee 1, 18 August 2006.

⁵ In the deliberations of the OSB’s Personal Insolvency Task Force some five years ago, there was substantial discussion on the idea of creating a new and simpler insolvency procedure for NINA debtors. In the end, it was decided that a streamlined version of the existing summary administration procedure would adequately address the issue.

⁶ Discussions about NINA debtors in Canada often refer not to those with incomes below the LICO but to those with income below the Surplus Income guidelines issued by the OSB. See *e.g.* the 2007 guidelines: Canada, OSB, Directive No. 11R, “Surplus Income” (27 January 2007), online: <<http://strategis.ic.gc.ca/epic/site/bsf-osb.nsf/en/br01055e.html#appA>>. Bankrupts with incomes higher than these guidelines are deemed to have “surplus income” and must make extra payments to their creditors. The Surplus Income guidelines, however, are based on the LICO calculated by Statistics Canada. See Ivan P. Fellegi (Chief Statistician of Canada), “On poverty and low income,” September 1997, online: Statistics Canada <<http://www.statcan.ca/english/research/13F0027XIE/13F0027XIE1999001.htm>>.

it for low-income Canadians to have significant debts? If the poor cannot easily borrow, it is unlikely that they will accumulate enough debt to warrant bankruptcy. Second, do poor debtors need bankruptcy? Many will be judgment-proof, facing no real prospect that a court would allow their creditors to take any action against them. And third, do existing procedures provide sufficient access to bankruptcy for poor debtors? A Canadian government program called the Bankruptcy Assistance Program (BAP) is available to those who cannot afford the required fees and, as we will see, private efforts also aid such debtors.

We draw on three sources to shed light on these questions: (1) an analysis of the *1999 Survey of Financial Security*, a wealth survey conducted by Statistics Canada;⁷ (2) the findings of our trustee interviews; and (3) a comparative analysis of approaches adopted in the United States, Australia, New Zealand, and the United Kingdom.

These research questions go to the heart of the long-standing debate about the ease with which debtors should be able to obtain a full discharge of their debts through the bankruptcy process. On one side of the debate are those who believe that the vast majority of debtors filing bankruptcy are honest but unfortunate and seek relief from their debts only as a distasteful last resort. Those on the other side of the debate believe that many who file for bankruptcy could repay their debts if only they were more diligent in their work habits and more careful in their spending habits. These two views lead to different conclusions about any initiative that makes bankruptcy more accessible. Those adhering to the first view believe that greater accessibility will not dramatically increase the numbers of debtors who file for bankruptcy, as bankruptcy is sought only as a last resort. Those who hold to the second view believe that the barriers to bankruptcy, both monetary and non-monetary, must be kept high in order to discourage large numbers of debtors from seeking bankruptcy. As we will see, this general debate spills over into the narrower debate about the subset of debtors who have so little income that they cannot pay the usual fees associated with bankruptcy.

Our conclusions are easily stated. We believe that the poor now have wide access to credit, fuelled by the easy availability of credit cards, by the ease with which consumer durables can be bought on credit and, for some, by government-subsidized student loans. When the poor find

⁷ Statistics Canada, *Survey of Financial Security* (March 2001) prepared by Karen Maser & Johanne Pineau, 13-595-XIE [*1999 Survey of Financial Security*].

themselves unable to meet their repayment obligations, they are often subject to intense and invasive collection efforts, even if they are judgment-proof. Despite the efforts of some trustees in some cities to provide bankruptcy at a reduced price,⁸ an unknown number of poor debtors remain without access to bankruptcy. Moreover, the Office of the Superintendent of Bankruptcy's (OSB) BAP is poorly designed, poorly understood, and in great need of modernization.

II. DO THE POOR NEED BANKRUPTCY?

In the context of consumer bankruptcy, the poor are not only insolvent at the time of filing for bankruptcy, but are likely to have been poor for some time and are likely to remain in poverty for the foreseeable future. Their earning prospects are dim and their life circumstances are such that significant barriers will impede any upward economic mobility.

However, for one of two reasons, some might question whether the poor need bankruptcy. The first reason has already been discussed. Many of the poor are judgment-proof and, in principle, can simply refuse to respond to collection efforts. Nonetheless, avoiding collection efforts is more difficult than one might think and judgment-proof debtors frequently appear in trustees' offices seeking bankruptcy protection.

The second reason for believing that the poor do not need bankruptcy is the idea that the poor do not accumulate very large debts and therefore have little need for bankruptcy protection. In this section, we use the *1999 Survey of Financial Security* to illustrate that the so-called "democratization of credit"—the extension of credit throughout the income distribution—has proceeded to the point where even families in the lowest deciles of family income have significant debts.

Tables 1 and 2 show the distribution of various kinds of debt across the deciles of family income. Families in the bottom three deciles almost certainly have incomes that are lower than the relevant Statistics Canada LICO and therefore might qualify as poor by our definition.⁹

Table 1 makes clear that significant proportions of the poor have debts in each of the categories listed. To be sure, families in the lowest

⁸ See Part III(A), below.

⁹ There is an important difference between the poor families in Tables 1 and 2 and poor families as we think of them in the context of bankruptcy. In our conception, poor families seeking bankruptcy protection are not only poor at a single point in time but are likely to remain poor for the near future. Because there is considerable mobility in and out of poverty in Canada, a significant minority of families in the lowest deciles of family income in Tables 1 and 2 are likely to move out of poverty in future years.

three deciles are *less* likely to have various types of debts than those in the higher deciles, but one in four has credit card debt (*e.g.*, 25% in the lowest decile) and one in six (*e.g.*, 17% in the lowest decile) has other debts. Since bankruptcy is a situation facing only a minority of debtors, these proportions are large enough to suggest that a significant minority of poor families will have significant debts coming due at a time when their income is low. The amounts shown in Table 2 are averages only for those who have positive amounts of debt in each category, but their size once again suggests that poor families may acquire significant debts, especially in relation to their low income. For example, among those in the lowest decile with credit card debt, the average amount owed was \$2,064.

We note in passing that student loan debts are an important type of debt held by the poor, both in terms of frequency and size, and that student loans are not dischargeable through bankruptcy. We see that the families in the lowest decile are the *most* likely to hold student loans, partly because those loans are directed to students from low-income families, and partly because there is a correlation between the incomes of parents and children.¹⁰ If the debts of a poor family become overwhelming, it may make sense to file for bankruptcy in order to discharge those debts that are dischargeable, and then to focus on repaying the student loans that are not dischargeable.

Table 1: Percentage of Families with Various Types of Debt¹¹

Deciles of Family Income	Mortgage	Vehicle Loans	Credit Cards	Student Loans	Other Debts	Families with Debt
Less than 12,250	7	6	25	13	17	50
12,250-18,000	9	9	24	9	15	47
18,000-24,700	14	14	32	10	20	57
24,700-31,850	22	19	39	10	24	65
31,850-40,000	32	24	42	12	27	72
40,000-49,000	41	28	46	10	32	78
49,000-60,850	45	31	47	11	35	81
60,850-76,800	53	34	48	12	40	84
76,800-105,300	52	34	45	10	39	83
More than 105,300	47	23	30	5	39	76

¹⁰ See *e.g.* Jere R. Behrman & Paul Taubman, "The Intergenerational Correlation Between Children's Adult Earnings and Their Parents' Income: Results from the Michigan Panel Survey of Income Dynamics" (1990) 36 *Rev. Income & Wealth* 115.

¹¹ 1999 *Survey of Financial Security*, *supra* note 7, unweighted. See also Saul Schwartz & S. Baum, "How Much Debt is Too Much? Benchmarks for Manageable Debt in Canada and the United States" (Paper presented to the Universities and the Powering of Knowledge: Policy, Regulation, and Innovation conference, School of Public Policy and Administration, Carleton University, Ottawa, 19 October 2007) [unpublished]. Note: All debts are reported for the family as a whole.

Table 2: Dollar Amount of Debt Outstanding for Families with Non-negative Debt¹²

Deciles of Family Income	Mortgage	Vehicle Loans	Credit Cards	Student Loans	Other Debts	Debt Per Family
Less than \$12,250	62,260	6,968	2,064	11,961	6,562	19,430
12,250-18,000	52,348	8,338	1,957	12,013	8,601	19,875
18,000-24,700	51,815	8,113	2,233	9,983	6,307	23,651
24,700-31,850	51,783	9,393	2,551	11,593	8,171	29,248
31,850-40,000	58,804	9,835	2,696	10,611	9,021	39,202
40,000-49,000	65,158	10,897	2,998	10,093	9,126	48,871
49,000-60,850	70,281	11,005	3,186	9,619	11,740	58,561
60,850-76,800	75,093	12,054	3,479	9,979	14,589	69,382
76,800-105,300	80,899	14,469	3,786	9,769	17,632	77,080
More than 105,300	117,558	16,108	4,721	12,354	33,266	109,512
No. of Families	5,098	3,506	5,993	1,615	4,592	10,543

III. OVERVIEW OF THE CANADIAN SYSTEM

One option facing poor but heavily indebted Canadians is to do nothing. Whatever threats might be made by collectors, and regardless of the persistence of their calls and visits, such individuals are likely to be judgment-proof and the threats and calls will eventually stop. However, when faced with persistent and threatening collection calls, “doing nothing” is easier said than done. Few know the law well enough to know that the threats are empty and that the calls will stop sooner rather than later. For those who seek to resolve their debt situations, bankruptcy can be the best option. The other major option—credit counselling as currently practiced in Canada—is unlikely to be successful because poor debtors lack the financial resources to make the payments required by a debt management plan. “Doing nothing” also leaves the outstanding debts in place, waiting for the person should he or she ever find a way out of poverty and thus lose judgment-proof status.

Since private-sector trustees administer bankruptcies, a poor debtor seeking bankruptcy protection must find a trustee who is willing to handle such a file. Not surprisingly, trustees consider whether they are likely to be paid for their efforts before they agree to take on a case. Trustees are paid from the money that they collect on behalf of the creditors; this money defines the estate of the debtor. Rule 128(1) of the *Bankruptcy and Insolvency Act*¹³ sets out the method by which trustees calculate the maximum fees. Essentially, the maximum fees are a function of the amount of receipts coming into the estate. At most, a trustee can

¹² Schwartz & Baum, *ibid.*

¹³ R.S.C. 1985, c. B-3 [BIA]. See Appendix III for the text of Rule 128(1) of the BIA.

collect the first \$975 of receipts, plus 35% of the next \$1,025, plus 50% of everything above \$2,000, to a maximum of \$10,000. In practice, it seems that trustees try to realize at least \$1,500 to \$1,700 on each file. Of course, they are free to take less if they so choose.

Two major sources of receipts for the estate, and thus for trustee fees, are selling the debtor's non-exempt assets and filing the debtor's tax refunds. In many cases, however, debtors have no non-exempt assets and the amounts that can be expected from their tax returns are not enough to bring the receipts of the estate up to an acceptable level. In such cases, trustees are allowed to ask the debtors to make voluntary payments to the estate over the course of the nine months of the bankruptcy.¹⁴ In a significant minority of bankruptcies, these voluntary payments comprise the bulk of the receipts of the estate.¹⁵

The problem for the poor debtors is that trustees may decide, rightly or wrongly, that the receipts of the estate, including any voluntary payments that the debtor can afford, are not likely to reach an acceptable level. If so, the trustee need not accept the case.

In our interviews with trustees, we realized that a poor debtor who decides to seek bankruptcy in Canada but unable to afford the voluntary payments required by most trustees has two options. First, the debtor may try to find a trustee who will handle the file at a lower-than-normal price. Second, the debtor might seek help from the BAP, operated by the OSB.

A. *Relying on Local Trustees*

Conceivably, a debtor who seeks help from local trustees might be turned away by all of them. However, none of the trustees that we

¹⁴ Though there is case law in Canada suggesting that such fee agreements are not allowed, recent legislation amends the *BIA* to reverse the case law and reinstate these agreements. See Bill C-55, *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, 1st Sess., 38th Parl., 2005, (assented to on 25 November 2005; not currently in force), S.C. 2005, c.47, online: Parliament of Canada <http://www2.parl.gc.ca/content/hoc/Bills/381/Government/C-55/C-55_4/C-55_4.PDF> [Statute c. 47]. See also *BIA*, *ibid.*, s. 156.1.

¹⁵ For the 2006 summary administration bankruptcies described in Appendix III, the proportion of receipts consisting of voluntary payments by the debtor can be estimated. Voluntary payments were made in 77% of the cases. Such payments made up more than 50% of the receipts in 49% of the cases and were more than 75% of the receipts of the estate in 25% of the cases. A controversial issue here is that the voluntary payments that trustees are allowed to ask of debtors become part of the estate and cannot be returned to the debtor should actual receipts turn out to be unexpectedly large. If trustees expect that receipts from the sale of non-exempt assets or from tax refunds will cover trustees' usual fees, they will presumably lower or eliminate the voluntary payments. The only mechanism driving trustees to lower their fees in such cases, however, is potential competition from other trustees.

interviewed believed that large numbers of poor debtors were being turned away due to their inability to pay trustees' fees. Even if some area firms were unwilling to accept the files, the trustees thought that poor debtors would be able to find at least one trustee who would be flexible in the fees that he or she asked. The majority of the trustees we interviewed indicated that they themselves would never turn away a debtor seeking bankruptcy if they thought that the only obstacle to bankruptcy was the level of their fees. Most would agree with one trustee's statement that she "would never refuse someone who cannot afford the fee."¹⁶ However, the decision to be flexible on fees is not automatic; the trustees described the decision as one that is made on a case-by-case basis, and is dependent upon the information gleaned during initial interviews with the debtor.

The trustees were willing to go beyond personal experience to suggest that such flexibility is quite common among trustees. While this flexibility may be common, it may not be universal. One trustee said that the national firms in her location did not lower their fees if the debtor could not pay.¹⁷ Another trustee (from a national firm) said that firms that were busy were unlikely to be flexible in their fees.¹⁸

In some cities, area trustees have gotten together and decided to handle the cases of poor debtors according to an agreed-upon formula. Such voluntary plans are not new. In 1969, the *Globe and Mail* reported: "A newly formed group of Ontario bankruptcy trustees [have] agreed to negotiate a plan for reduced-cost services to debtors who cannot afford the usual \$500 fee for personal bankrupts."¹⁹ The plan was aimed at "... the honest debtor who deserves the benefit of the bankruptcy but can't finance it himself."²⁰

In 1994, trustees in the Halifax region agreed that, as a group, they would handle the bankruptcies of anyone who needed the service

¹⁶ Interview with Trustee 1, *supra* note 4.

¹⁷ Interview with Trustee 2, 8 September 2006.

¹⁸ Interview with Trustee 9, 29 November 2006.

¹⁹ Loren Lind, "New service offered to lower costs of bankruptcy" *Globe and Mail* (6 February 1969) 4th: 35. It is important to note that in that era the summary tariff was a flat \$450 fee plus \$50 for disbursements. This was the maximum fee possible for such files regardless of the amount of work performed. At that time, the vast majority of trustees required that the \$500 had to be paid up front before the bankruptcy would be filed. Given an average annual inflation rate of 4.68, the equivalent of the \$500 fee in 2007 would be \$2,840. Inflation based on Bank of Canada's *Inflation Calculator*, online: <<http://www.bankofcanada.ca/en/rates/inflationcalc.html>> [Bank of Canada, *Inflation Calculator*].

²⁰ Lind, *ibid.*, quoting Keral Jerabek, then-president of the Ontario Association of Trustees in Bankruptcy.

and could not afford it.²¹ That agreement has persisted over time, and today poor debtors are asked to pay only \$250.²² Similarly, trustees in Edmonton agreed in 1999 to a similar arrangement for dealing with what are now known as “450 cases” because the out-of-pocket costs (and therefore the fee charged) at the time amounted to \$450.²³

Apart from the reports of trustees, however, there is no way to determine precisely how many debtors are simply turned away, who do not approach trustees because they think they will be unable to afford the normal fees, or who cannot afford upfront payments of \$250–\$450.²⁴

B. *The Bankruptcy Assistance Program*

The OSB administers the little-used BAP.²⁵ Trustees first agree to be part of the program, and those who do so are placed on a list of available trustees. The program then assigns listed trustees to administer the files of debtors who have approached at least two trustees to handle their bankruptcies and who have been turned away because of their inability to pay the normal fees.

Very few cases are actually filed under the BAP. Of the roughly thirty thousand summary administration cases described in Appendix III, only 304 (about 1%) were BAP cases.²⁶ Our interviews illustrate, however, that it would be a mistake to assume that the number of BAP cases is equal to the number of poor debtors. For example, in the cities where an agreement exists among trustees to handle poor debtors in a certain way, trustees will often not refer poor debtors to the BAP program, but will simply administer the cases themselves. Perhaps a better measure of the number of poor debtors is the number of cases in which receipts are less than \$500; of the non-BAP summary administration bankruptcies in our data set, receipts were less than \$500 in 1,056, or about 3.5%, of the files.

²¹ Interview with Trustee 6, 20 September 2006.

²² The fee is still \$250 in Halifax even though out-of-pocket costs are now higher. *Ibid.*

²³ Interview with Trustee 3, 8 September 2006. Given an average annual inflation rate of 2.35, the equivalent of the \$450 fee in 2007 would be \$542. Bank of Canada, *Inflation Calculator*, *supra* note 19.

²⁴ We note that this is a common situation in evaluating program participation; since information on non-participants is rarely collected, there is no effective way to estimate their number apart from anecdotal evidence from practitioners.

²⁵ The statutory source for the BAP is a directive known as “Directive No. 11” made pursuant to the *BIA*, *supra* note 13. Section 5(4)(b) to (e) of the *BIA* provides the OSB with the power to make directives. Canada, OSB, Directive No. 11, “Bankruptcy Assistance Program,” (23 October 1986), online: Strategis <<http://strategis.ic.gc.ca/epic/site/bsf-osb.nsf/en/br01331e.html>> [“Directive No. 11”].

²⁶ Calculations by the Business Intelligence Centre of the OSB.

There is no set fee charged by trustees for BAP cases. As in all summary administration cases, the trustee collects GST refunds and any tax refund arising from the pre-bankruptcy tax return. For poor debtors, these sources might yield only a small amount of money. In such cases, most of the trustees that we interviewed ask that the debtor pay for the \$75 filing fee and the \$180 cost of the two mandatory counselling sessions up front, allowing the debtor to make any remaining voluntary payments that may be required by the trustee with small payments over the nine months of the bankruptcy.

One trustee told us, however, that BAP cases in her area were often almost as remunerative as non-BAP cases, with the trustee realizing fees close to the usual amount charged.²⁷ The Edmonton trustee that we interviewed stated that the GST refunds usually cover the out-of-pocket costs and that she had only lost money on two of the “450 cases” that she has handled since 1999.²⁸ Another trustee informed us that he averages \$1,000 to \$1,200 on a BAP case, as opposed to the \$1,200 to \$1,500 that he charges for a typical summary administration.²⁹

Looking at the receipts and disbursements for the 304 BAP cases in our data set, we see that the average trustee fee in these cases was \$1,500, with a standard deviation of \$986. This average seemed surprisingly high and we thought it might be influenced by a handful of cases in which the receipts of the estate (and thus the trustee’s fee) were inflated by unusual circumstances. For example, one BAP debtor received a \$39,000 inheritance during his bankruptcy. However, the median trustee fee is \$1,594, suggesting that the few cases with large receipts were not the main factor underlying the high mean. Voluntary payments from the debtors were not common; such payments were made in only 61 of the 304 cases.

Even though the average fees on BAP cases seem high to us, one trustee felt that there was no unmet need for bankruptcy in his area. He thought that all those who sought help in his area were being served and, furthermore, extensive advertising by trustees meant that no needy debtors were unaware of the option of filing.³⁰ Another trustee observed that, because the ability of trustees to oppose the bankrupt’s discharge

²⁷ Interview with Trustee 3, *supra* note 23.

²⁸ *Ibid.*

²⁹ Interview with Trustee 5, *supra* note 3.

³⁰ *Ibid.*

for unpaid fees provided security that their fees would be paid, few debtors were turned away. The same trustee, however, also observed that the costs of attending at court for the discharge hearing might be excessive for a trustee operating on his or her own.³¹

C. *Discussion*

We believe that the lack of uniform treatment of poor debtors is a major impediment to equal access to bankruptcy. In effect, their bankruptcies are handled in a way similar to how paupers received aid before the advent of modern social assistance systems, when local charities, local churches, or municipal governments took up the task of providing for the destitute. As a result, the nature of the assistance that the poor received varied widely across Canada. Some received the assistance that they required, while others did not. Similarly, some poor debtors have low-cost access to bankruptcy, while others do not.

A broad assessment of the situation suggests that most of those who seek bankruptcy are able to file. The cost of filing varies across the country, however, so the extent to which *low-cost* access is available is unknown.

Debtors who cannot afford to pay trustee fees can use the BAP program, but few do. Instead, some individual trustees and groups of trustees take it upon themselves to provide service to poor debtors. The Halifax and Edmonton agreements discussed in Part III(A), above, are examples of collective action of the sort that local charities might have undertaken to help the poor in the nineteenth century.

While the analogy to nineteenth-century social assistance is apt in some ways, it is less appropriate in others. For trustees specializing in consumer bankruptcies, fee flexibility is sometimes a good business decision rather than pro bono work. Most small businesses need to maintain a steady volume of cases in order to keep the staff busy. During periods when full-price cases are scarce, servicing poor debtors “keeps the lights on” even if the profit on such cases may turn out to be low or non-existent.³² The idea is that “anything is a contribution to overhead.”³³ The marginal cost of such cases is very small since the staff is already on site and may be underemployed during slow periods. Thus, the files of poor debtors may

³¹ Interview with Trustee 9, *supra* note 18.

³² Interview with Trustee 3, *supra* note 23.

³³ Interview with Trustee 5, *supra* note 3.

have a positive effect on the economic viability of trustees' businesses, helping them cover overhead during slow periods. Two of the interviewed trustees even thought that removing the files of poor debtors might endanger the economic viability of trustees who specialize in consumer bankruptcy.³⁴ The trustee from the large firm also noted this phenomenon when he said that he did *not* have to worry about cash flow and therefore did not need to take on the files of poor debtors for that reason.

IV. SHOULD POOR DEBTORS HAVE FINANCIALLY ACCESSIBLE OPTIONS FOR BANKRUPTCY?

A. *The American In Forma Pauperis Experience*

The American academic literature has tackled the issue of whether poor debtors should be allowed to file *in forma pauperis* petitions in bankruptcy. In the United States, the authority to proceed *in forma pauperis* is granted by statute, and is meant to provide indigent litigants with meaningful access to the federal courts, equivalent to the access available to those who can afford to pay.³⁵ When an individual successfully petitions to proceed *in forma pauperis*, certain costs and fees are waived.³⁶ Those who argue against allowing *in forma pauperis* proceedings in bankruptcy stress the cost implications of waiving fees: that the amount of fees collected by the system will decrease.³⁷ Furthermore, critics assert, nearly everyone who files for bankruptcy relief will ask that fees be waived, requiring screening mechanisms to be introduced.³⁸ Opponents further suggest that a fee-waiver system will encourage unnecessary and improper bankruptcy cases.³⁹ Individuals will file for bankruptcy even when there is no benefit in doing so, because debtors who cannot afford the filing fee are typically judgment-proof.⁴⁰ Such a system may also be subject to abuse

³⁴ Interview with Trustee 3, *supra* note 23; Interview with Trustee 6, *supra* note 21.

³⁵ Michael C. Markham & Bethann Scharrer, "In Forma Pauperis: An Unnecessary Privilege in Bankruptcy" (1994) 2 Am. Bankr. Inst. L. Rev. 73 at 77.

³⁶ *Ibid.* at 78. In the United States, some costs and fees are not waived. For example, witness fees and expenses are not among the fees and costs waived.

³⁷ *Ibid.* at 90.

³⁸ *Ibid.*

³⁹ *Ibid.*

⁴⁰ US Federal Judicial Centre, "Implementing and Evaluating the Chapter 7 Filing Fee Waiver Program: Report to the Committee on the Administration of the Bankruptcy System of the

or fraud; critics argue, for example, that a fee-waiver system will increase the number of people who file to benefit from an automatic stay, with no intention of following through to a discharge.⁴¹

In the American context, some commentators assert that a fee-waiver system is unnecessary because the filing fees can be paid in instalments, and as such, access to the system is denied only in rare circumstances.⁴² Otis B. Grant argues that the filing fee must be retained because of the easy availability of discharge: if a debtor believes that discharge is costless, Grant asserts, he or she will be more likely to use it.⁴³ Bankruptcy must have a cost, he states, because otherwise creditors will shift the cost of bankruptcy to the buyers of goods.⁴⁴ Lastly, Michael Markham and Bethann Scharrer argue that proceeding in a bankruptcy case is “nothing more than a privilege,” and thus “it seems logical that proceeding in forma pauperis in bankruptcy is also only a privilege.”⁴⁵

In the Canadian context, the suggestion coming out of the American commentary that a low or non-existent filing fee coupled with an easy discharge would have a significant impact on the bankruptcy rate can be challenged. The two existing empirical studies that bear on the abuse assumption in Canada suggest that the majority of existing Canadian bankrupts fall into the “can’t pay” rather than the “won’t pay” category.⁴⁶ While it is possible that the costs associated with bankruptcy played a role in these findings, it is unlikely that the composition of bankrupts would be significantly altered if “poor debtors” were given access to the system. This prediction is supported by our findings from the interviews with trustees, who suggested that as long as they continue to be the intermediaries in this process they would continue to play a

Judicial Conference of the United States” by Elizabeth C. Wiggins *et al.*, (Federal Judicial Center, 1998) at 21, online: <http://www.fjc.gov/library/fjc_catalog.nsf/autoframepage!openform?url=/library/fjccatalog.nsf/Publication!openform&parentunid=76FF032DF9BA521B85256CA300688AE3>.

⁴¹ *Ibid.* at 22.

⁴² *Ibid.*

⁴³ Otis B. Grant, “Are the Indigent Too Poor for Bankruptcy? A Critical Legal Interpretation of the Theory of Fresh Start within a Law and Economics Paradigm” (2002) 33 *Univ. Toledo L. Rev.* 773 at 792.

⁴⁴ *Ibid.* at 793.

⁴⁵ Markham & Scharrer, *supra* note 35 at 83.

⁴⁶ See Saul Schwartz, “The Empirical Dimensions of Consumer Bankruptcy: Results from a Survey of Canadian Bankrupts” (1999) 37 *Osgoode Hall L.J.* 83; Iain D.C. Ramsay, “Individual Bankruptcy: Preliminary Findings of a Socio-Legal Analysis Symposium on Consumer Bankruptcies” (1999) 37 *Osgoode Hall L.J.* 15.

“gate-keeping” function. That is, trustees will restrict access to “won’t pay” debtors. In addition, unlike the American system, the Canadian system continues to include a judicial discharge process that allows for the possibility of opposing the discharge of an “abusive” bankruptcy.⁴⁷

Henry J. Sommer succinctly states the argument in favour of being able to proceed *in forma pauperis* in bankruptcy filings: “Equal justice under the law.”⁴⁸ His response to the argument that the filing fee is low enough, and can be paid in instalments, is that “... those who make [the argument] must be shockingly unfamiliar with the plight of those in poverty in this country.”⁴⁹ Sommer notes that people file for bankruptcy for other reasons than to protect assets, for instance, to prevent a utility shutoff, to protect a driver’s licence, to participate in a government program, to prevent garnishment of wages (which is allowed in some states), or to fend off harassing or abusive calls from creditors or collection agencies.⁵⁰ Sommer’s statements reflect the findings on the need for bankruptcy for the poor from our interviews of Canadian bankruptcy trustees. Like Sommers, who considers the fears of overburdening the system with more paperwork to be overstated,⁵¹ we agree that the solution to abuse is not to restrict access to the system but to address the problem directly: the possibility that some might abuse the system is not a reason to reject a proposed reform.⁵²

V. MODELS FOR REFORM

A number of jurisdictions have acted on concerns such as those expressed by Sommer and the trustees we interviewed, and, recognizing that it can be difficult for poor debtors to file for bankruptcy due to the associated costs, we have identified forms of relief that can assist poor debtors in obtaining a fresh start. The following section documents the

⁴⁷ See *BIA*, *supra* note 13, s. 168.1(1).

⁴⁸ Henry J. Sommer, “In Forma Pauperis in Bankruptcy: The Time has Long since Come” (1994) 2 *Am. Bankr. Inst. L. Rev.* 93 at 97.

⁴⁹ *Ibid.* at 100.

⁵⁰ *Ibid.* at 103-04. See also Susan D. Kovac, “Judgment-Proof Debtors in Bankruptcy” (1991) 65 *Am. Bankr. L.J.* 675 at 678-81 for a discussion of the benefits and costs of bankruptcy for judgment-proof debtors; and Nathaniel C. Nichols, “The Poor Need Not Apply: Moralistic Barriers to Bankruptcy’s Fresh Start (1993-1994) 25 *Rutgers L.J.* 329 at 351-53, where he points out that filing for bankruptcy is an effective way for a poor family to prevent the stoppage of a utility service, while providing for a fresh beginning with the utility service.

⁵¹ Sommer, *supra* note 48 at 105.

⁵² *Ibid.* at 107.

available and proposed bankruptcy services for the poor in the United States, Australia, New Zealand, and the United Kingdom.

A. *United States*

Title 28 of the United States Code (U.S.C.) represents the American *in forma pauperis* statute, which allows an individual to file civil actions in federal courts without paying the requisite filing fee.⁵³ A person seeking to proceed *in forma pauperis* must file an affidavit showing an inability to pay the associated costs.⁵⁴ Section 1930 governs the payment of fees in bankruptcy courts. As the statute was previously worded, bankruptcy courts did not fall under the definition of a “court of the United States,” and therefore had no authority to allow *in forma pauperis* proceedings.⁵⁵ A 1973 decision of the US Supreme Court held that there was no constitutional right to obtain a discharge of one’s debts in bankruptcy, and concluded that the fee provisions of the *Bankruptcy Code* at the time were not an unconstitutional denial of due process rights.⁵⁶ Thus, the legislation and jurisprudence previously precluded the application of Title 28 to the initial filing fee for a bankruptcy petition.⁵⁷

Under section 418 of the *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* (and codified at Title 28 of the U.S.C.), however, individual Chapter 7⁵⁸ applicants may now seek a waiver of the filing fee at the time they file the bankruptcy petition.⁵⁹ Under the new legislation, a district or bankruptcy court may waive the filing fee for an individual debtor who (a) has income less than 150% of the poverty

⁵³ Markham & Scharrer, *supra* note 35 at 73. Note that the current fee for a Chapter 7 filing is US\$299, effective as of 9 April 2006: United States, Administrative Office of the US Courts, “Bankruptcy Filing Fees” in *US Bankruptcy Courts*, online: US Courts <<http://www.uscourts.gov/bankruptcycourts/fees.html>>. Given an exchange rate of 1.0654 (for 1 July 2007) the equivalent of the US\$299 fee in Canadian dollars would be \$319. The exchange rate is based on Bank of Canada’s *Daily noon rates: 10-year lookup*, online: <<http://www.bank-banque-canada.ca/en/rates/exchange-look.html>> [Bank of Canada, *Daily noon rates*].

⁵⁴ Markham & Scharrer, *ibid.* at 77.

⁵⁵ See *ibid.* at 80 for an overview of the decisions which have held that bankruptcy courts are not courts of the United States.

⁵⁶ *Ibid.* at 74-75. See also *United States v. Kras*, 409 U.S. 434 (1973) [*Kras*].

⁵⁷ Sommer, *supra* note 48 at 95.

⁵⁸ So-called because Chapter 7 of Title 11 (“Bankruptcy”) of the U.S.C. governs liquidations, the most common form of US bankruptcy.

⁵⁹ *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 119 Stat. 27, s. 418, codified at 28 U.S.C. § 1930(f)(1-3).

guidelines last established by the US Department of Health and Human Services,⁶⁰ and (b) is unable to pay that fee in instalments.⁶¹ For individual debtors whose filing fees have been waived, the bankruptcy or district court may also waive other fees.⁶² In addition, the U.S.C. allows for the payment of the filing fee in instalments.⁶³

Congress implemented a pilot program in 1994 in six judicial districts to study the effect of waiving the US\$175⁶⁴ filing fee for individual Chapter 7 debtors who were unable to pay the fee in instalments.⁶⁵ The study found that an application for waiver of the filing fee was filed in 3.4% of all non-business Chapter 7 cases, and granted in 2.9% of the cases.⁶⁶ The report concluded that the fee-waiver program might make the bankruptcy system more accessible to low-income debtors: almost 11% of the successful fee-waiver applicants stated that they would not have filed for bankruptcy had there been no fee-waiver program.⁶⁷ In particular, the “committee concluded that the fee-waiver program may have enhanced access to the bankruptcy system for indigent single women.”⁶⁸ Debtors whose filing fees were waived “were more likely to obtain a discharge compared to debtors whose applications were

⁶⁰ See United States, Department of Health and Human Services, “THE 2007 HHS POVERTY GUIDELINES” (24 January 2007), online: <<http://aspe.hhs.gov/poverty/07poverty.shtml>>.

⁶¹ United States, Judicial Conference, “Interim Procedures Regarding the Chapter 7 Fee Waiver Provisions of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005” (11 August 2005), in *US Bankruptcy Courts*, online: US Courts <<http://www.uscourts.gov/bankruptcycourts/jcusguidelines.html>>.

⁶² 28 U.S.C. § 1930(f)(2). The fees that may be waived are those prescribed under §§ 1930(b) and (c).

⁶³ Fed. Bankr. Rule 1006; *ibid.*, § 1930(a). Upon petition,

the court may ... grant leave to pay in installments and fix the number, amount and dates of payment. The number of installments shall not exceed four, and the final installment shall be payable not later than 120 days after filing the petition. For cause shown, the court may extend the time of any installment, provided the last installment is paid not later than 180 days after filing the petition.

See Fed. Bankr. Rule 1006(b)(2).

⁶⁴ Given an exchange rate of 1.3825 (as of 1 July 2007) and an average annual inflation rate of 2.10, the equivalent of the 1994 US\$175 fee in 2007 Canadian dollars would be \$317. Exchange rate: Werner Antweiler, “Database Retrieval System (v.2.12),” Pacific Exchange Rate Service, University of British Columbia, online: <<http://fx.sauder.ubc.ca/data.html>>; inflation: Bank of Canada, *Inflation Calculator*, *supra* note 19.

⁶⁵ See Wiggins *et al.*, *supra* note 40.

⁶⁶ *Ibid.* at 1.

⁶⁷ *Ibid.* at 4.

⁶⁸ *Ibid.*

denied.”⁶⁹ The report noted that there was an increase overall in Chapter 7 and Chapter 13⁷⁰ filings during the period of study, thereby complicating the assessment of whether the program increased Chapter 7 filings. The study concluded, however, that only a “small fraction” of the increased filings were due to the program.⁷¹ Assuming that applications would be filed and granted at the same rate as occurred in the pilot program, the study predicted that a national fee-waiver program would cost approximately US\$4.7 million in lost filing fees, US\$74,000 in waived miscellaneous fees for *in forma pauperis* debtors, and US\$1.5 million in salary for additional office clerk personnel (a total cost of approximately US\$6.3 million).⁷² To fund the program, the study recommended that Congress increase the judiciary’s appropriation by this amount,⁷³ or request authorization for a portion of the US Treasury share of the filing fee to cover the cost.⁷⁴

In addition to filing fees, American debtors often are confronted with legal fees as they navigate the complex bankruptcy process. As Kerry Heydel Ducey notes, it is unlikely that a no-asset Chapter 7 filer can afford to pay a bankruptcy attorney up front.⁷⁵ Without a retainer, a bankruptcy attorney is unlikely to pay the requisite filing fees or perform other pre-petition services because the debtor’s obligation to pay for these services are likely to be discharged in the bankruptcy proceeding.⁷⁶ Most courts have held that pre-petition attorney fees are dischargeable, forcing bankruptcy attorneys to “get creative” if they wish to be paid.⁷⁷ In addition, a debtor’s attorney cannot be paid out of funds of the estate in a Chapter 7 proceeding, which has heightened access to justice issues

⁶⁹ *Ibid.*

⁷⁰ So-called because Chapter 13 of Title 11 (“Bankruptcy”) of the U.S.C. governs reorganization.

⁷¹ *Ibid.* at 6.

⁷² *Ibid.* at 12. The study did indicate that the cost might rise significantly if fee waivers were automatically based on a bright-line income standard.

⁷³ This represented two tenths of one per cent of the judiciary’s total fiscal appropriation for 1997. *Ibid.* at 13.

⁷⁴ *Ibid.* Given an exchange rate of 1.3825 and an average annual inflation rate of 2.10, the equivalent of the 1994 US\$6.3 million cost fee in 2007 Canadian dollars would be \$11,412,424. Exchange rate: Antweiler, *supra* note 64; inflation: Bank of Canada, *Inflation Calculator*, *supra* note 19.

⁷⁵ Kerry Heydel Ducey, “Bankruptcy, Just for the Rich? An Analysis of Popular Fee Arrangements for Pre-petition Legal Fees and a Call to Amend” (2001) 54 Vand. L. Rev. 1665 at 1667.

⁷⁶ *Ibid.*

⁷⁷ *Ibid.* at 1671.

because the debtor's attorney must be paid in cash up front, or else the attorney cannot participate in the estate.⁷⁸ Accordingly, Haydel Ducey recommends exempting pre-petition bankruptcy attorney fees from discharge, which would in turn encourage counsel to represent "even the poorest of debtors" by removing the risks of representing those who may be unable to pay their legal fees in advance.⁷⁹ Under 28 U.S.C. § 1915(e)(1), the court may request an attorney to represent someone who is unable to afford counsel, although most bankruptcy judges have decided that they do not have the authority to do so.⁸⁰

Given that both the American consumer credit market and bankruptcy system have much in common with the Canadian market and bankruptcy system, the American model for dealing with "poor debtors" merits serious consideration. In particular, the experience of the American pilot project undertaken in the mid-1990s suggests that the number of bankruptcy filings will not increase significantly with the availability of a fee-waiver system, thus laying to rest some of the fears associated with abuse of the system as well as the costs of implementing such a system.

B. *Australia*

The vast majority of bankruptcies in Australia are administered by official receivers, who work as representatives of the Official Trustee of the Insolvency and Trustee Service Australia (ITSA). Trustees from the private sector do, however, administer some bankruptcies.⁸¹ Australia's bankruptcy regime provides three alternative bankruptcy

⁷⁸ *Lamie v. US Trustee*, 540 U.S. 526 (2004). 11 U.S.C. § 330(a)(1) does not list a debtor's attorney as someone eligible for compensation from the bankruptcy estate. We thank John Pottow for drawing this case to our attention. Note also that much controversy has erupted over the new 11 U.S.C. § 524(a)(4)'s prohibition on advising clients to incur more debt before bankruptcy, which implies that attorneys cannot advise their clients to file for bankruptcy if to do so would require the debtor to borrow money to pay for filing or counsel fees. Pottow indicates that most courts that have considered this provision have struck it down as unconstitutional.

⁷⁹ Heydel Ducey, *supra* note 75 at 1672.

⁸⁰ Richard H.W. Maloy, "Should Bankruptcy Be Reserved for People Who Have Money? Or is the Bankruptcy Court a Court of the United States?" (1997) 7 J. Bankr. L. & Prac. 3 at 28. The courts have generally found that, due to the *Kras* decision (*supra* note 56), the section is inapplicable to bankruptcy proceedings.

⁸¹ Rosalind Mason, "Consumer Bankruptcies: An Australian Perspective" (1999) 37 Osgoode Hall L.J. 449 at 453. The Official Trustee in Australia is a person who administers statutory functions under the *Bankruptcy Act 1966* for the Australian government.

options, one of which is accessible to low-income debtors. First, under section 55 of the *Bankruptcy Act 1966*,⁸² a debtor may apply for bankruptcy without the need for court involvement. A debtor may become bankrupt by presenting a petition and statement of financial affairs to an official receiver. If the documents are in correct form and there is no creditor's petition pending, the official receiver must accept the petition. The individual becomes bankrupt on the day the petition is accepted, and the official receiver automatically becomes the trustee unless the individual nominates a privately registered trustee. In most cases, the bankrupt will be automatically discharged after three years.⁸³ The vast majority of bankruptcy cases in Australia proceed through the Official Trustee's office, and in cases where the bankrupt does not have money in his or her estate, there is no payment made to the Official Trustee.⁸⁴ Thus, for the poor, bankruptcy is effectively subsidized by the public, because no funding comes from their estates.

Second, bankruptcy is available under Part X of the *Bankruptcy Act*—a more expensive, more sophisticated process involving lawyers. Third, debt agreements under Part IX of the *Bankruptcy Act* are available to represent a low-cost alternative to bankruptcy for those who can afford to make some payments; however, they are not likely to be viable for poor debtors.⁸⁵

Under the Australian government's cost-recovery policy, the ITSA has adopted a formal cost-recovery regime in respect of fees and charges payable under the *Bankruptcy Act 1966* and related legislation. In 2004, the ITSA undertook a review of its fees and charges, identifying which services should be cost recovered, the type of charge to apply, who should pay, and which services would be more appropriately

⁸² (Cth) as amended, s. 55 [*Bankruptcy Act 1966*].

⁸³ See *Bankruptcy Act 1966*, *ibid.*, ss. 149-149Q. The bankrupt will be automatically discharged after three years, unless (i) an early discharge from bankruptcy has been granted by the trustee (only applies to bankruptcies in existence prior to 5 May 2003, since the amendments of *Bankruptcy Legislation Amendment Act 2002* (Cth.)), (ii) an objection to discharge has been filed by the trustee, or (iii) the bankruptcy has been annulled. See ITSA, "Bankruptcy—Long Version," online: <<http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/bankruptcy-%3Ebankruptcy+-+long+version>>.

⁸⁴ Tony Duggan, "Consumer Bankruptcy in Canada and Australia: A Comparative Overview" in Janis Sarra, ed., *Annual Review of Insolvency Law 2006* (Carswell: Toronto, 2007) 857.

⁸⁵ See ITSA, "Part IX Debt Agreements," online: <<http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/debt+agreements-%3Epart+ix+debt+agreements>>. See also ITSA & Attorney General, "Report on the Review of Debt Agreements Under Part IX of the Bankruptcy Act 1966," online: <http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/Reform-%3EAmendments%20documents/%FILE/debt-agreement_review_report.pdf> [Review of Debt Agreements].

covered through general taxation.⁸⁶ The new fees and charges are effective from 1 July 2006. There is no fee for processing section 55 debtor petitions or debt agreement proposals.⁸⁷

The ITSA's "Cost Recovery Impact Statement" indicated that an AUS\$250 fee would have to be charged to recover the processing costs of debtors' section 55 petitions.⁸⁸ The ITSA deemed, however, that this fee would not be consistent with broader bankruptcy objectives in providing a broad community benefit and not just relief for debtors.⁸⁹ During the consultation process, proponents of the fee argued that debtors receive a direct benefit, and given that debtors would not have the same debt servicing burdens once their petition is accepted, they should be able to afford the fee.⁹⁰ Critics argued that it would be counter-intuitive to subject debtors facing financial hardship to the fee, and that its imposition would deny many debtors access to the system.⁹¹ Creditors noted that ultimately they would end up paying the fee in many cases, as debtors would choose not to pay certain bills, or would acquire additional credit to pay the processing fee.⁹²

While the Australian debate on the issue of filing fees for bankruptcy appears to have been settled in a similar fashion as the most recent American debates, there remains a key difference. The Australian discharge provisions under section 55 are more onerous than those in either the United States or Canada. For example, a three-year period is required before discharge under the Australian model, in comparison to the typical nine-month period in Canada. Presumably, the result is that higher-income debtors will opt for one of the two alternative bankruptcy options, meaning that a different and less attractive form of fresh start is

⁸⁶ *Bankruptcy Legislation (Fees and Charges) Bill 2006*, Bills Digest no. 110 2005-06, online: Parliament of Australia <<http://www.aph.gov.au/LIBRARY/pubs/BD/2005-06/06bd110.htm>>.

⁸⁷ See ITSA, "ITSA Fees and Charges" (effective 1 July 2007), online: <[http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/Bankruptcy-%3EPamphlets%20and%20Fact%20Sheet%20Documents/\\$FILE/Fees_and_charges.pdf](http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/Bankruptcy-%3EPamphlets%20and%20Fact%20Sheet%20Documents/$FILE/Fees_and_charges.pdf)>.

⁸⁸ ITSA, "Cost Recovery Impact Statement," (February 2005), online: <[http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/About%20Us-%3ECost%20Recovery-%3ECost%20Recovery%20Documents/\\$FILE/CRIS_230205.pdf](http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/About%20Us-%3ECost%20Recovery-%3ECost%20Recovery%20Documents/$FILE/CRIS_230205.pdf)> [ITSA, "Cost Recovery"] at 3. Given an exchange rate of 0.9029 (for 1 July 2007), the equivalent of the AUS\$250 fee in Canadian dollars would be \$226. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53.

⁸⁹ ITSA, "Cost Recovery," *ibid.*

⁹⁰ *Ibid.* at 17-18.

⁹¹ *Ibid.* at 18.

⁹² *Ibid.*

offered to poor debtors. This aspect of the Australian model runs counter to the goal of equality under the law as it applies to the bankruptcy system. As such, it replicates characteristics of the existing Canadian system, which we find troubling.

C. *New Zealand*

The New Zealand government has recently introduced the *Insolvency Act 2006*, which includes a “no income no asset procedure” as an alternative to bankruptcy as it exists in New Zealand.⁹³ The reforms expand the role of the Official Assignee, as all debtors will have to consult with an Official Assignee before invoking any of the proceedings; this will make bankruptcy an administrative procedure.⁹⁴ Under the new regime, a debtor will be required to file a financial statement of affairs with the Official Assignee before pursuing bankruptcy or the no asset procedure option.⁹⁵ The Official Assignee will not only provide advice and information, Thomas Telfer notes, but also render substantive decisions on the options pursued.⁹⁶ Telfer cautiously suggests that the retention of the Official Assignees’ monopoly over bankruptcy administration may avoid some of the problems associated with a private trustee system, such as Canada’s, where private trustees face potential conflicts of interest. However, Telfer draws attention to the multiple roles the Official Assignee will have to play under the proposed reforms and the potential for conflicts.⁹⁷

The New Zealand Ministry of Economic Development describes the no-asset procedure as providing “... an alternative to bankruptcy for insolvent debtors with nominal debts, no assets and no means to repay the debt.”⁹⁸ Part 5, subpart 4 of the bill sets out the rules relating to the no-

⁹³ *Insolvency Act 2006* (NZ), 2006/55 [*Insolvency Act 2006*].

⁹⁴ David Brown & Thomas G.W. Telfer, *Personal and Corporate Insolvency Legislation* (Wellington: LexisNexis, 2007) at 7; Thomas G.W. Telfer, “New Zealand Bankruptcy Law Reform: The New Role of the Official Assignee and the Prospects for a No-Asset Regime” in *Consumer Bankruptcy in Global Perspective*, Johanna Niemi-Kiesilainen, Iain Ramsay & William C. Whitford, eds. (Oxford and Portland: Hart Publishing, 2003) 247 at 248 [Telfer, “New Zealand Bankruptcy Law Reform”]. The Official Assignee is a statutory position created by the *Insolvency Act 1967* (NZ) 1967/54, ss. 15-18. When an Official Assignee is appointed to act in respect of a bankruptcy, he or she acts as an officer of the court.

⁹⁵ Telfer, “New Zealand Bankruptcy Law Reform,” *ibid.* at 257; Explanatory Note, General Policy Statement, Bill 14-1, *Insolvency Law Reform Bill* (NZ), 48th Parl., 2005, online: New Zealand Parliament <http://www.parliament.nz/NR/rdonlyres/4C0A36B5-EDED-41EC-BBD1-255243CCD29D/47166/DBHOHBILL_71631229992.pdf> [Explanatory Note to Bill 14-1].

⁹⁶ Telfer, *ibid.*

⁹⁷ *Ibid.* at 258-59.

asset procedure. The starting point is the same for proceeding in bankruptcy: furnishing a statement of the debtor's affairs. Based on the statement of affairs, the Assignee will decide whether the debtor qualifies for entry to the no-asset procedure.⁹⁹ The bill outlines criteria for entry to the no-asset procedure: no assets, total debts between NZ\$1,000 and NZ\$40,000,¹⁰⁰ no means to repay any amount, and a clean financial record (namely, not previously bankrupt, not previously admitted to the no-asset procedure).¹⁰¹ Once admitted to the no-asset procedure, the debtor enjoys a moratorium—with some exceptions, their debts cannot be enforced while the debtor is in the no-asset procedure. After twelve months, the debtor is discharged and the debts are cancelled.¹⁰² However, if the no-asset procedure terminates at any time before the twelve-month period has elapsed, the debtor's debts will become enforceable.¹⁰³

The Assignee will have a limited role in the process because the debtor by definition has no assets; the Assignee must ensure that an applicant is qualified for entry, provide creditors with an opportunity to object to a debtor being admitted to the no-asset procedure, ensure that a debtor who has been admitted improperly is removed, and terminate the no-asset procedure at the request of the debtor if the Assignee is satisfied that the debtor, through changed circumstances, can make payment towards his or her debts.¹⁰⁴ The benefit of the no-asset procedure is that an individual's debts are cancelled on discharge. Telfer notes that the Official Assignee will have to play a gate-keeping function through the control of access to the regime.¹⁰⁵ He argues that if the no-asset procedure adopted by Parliament incorporates a number of subjective standards (such as entry criteria to determine who may access the procedure), the benefits of a streamlined

⁹⁸ New Zealand, Ministry of Economic Development, Statement of Feasible Options to Achieve the Desired Objectives," *Bankruptcy Administration: No Asset Procedure and Insolvency Act Changes—Regulatory Impact Statement* (1 December 2003), online: Ministry of Economic Development (New Zealand) <<http://www.med.govt.nz/templates/MultipageDocumentPage6252.aspx>>.

⁹⁹ Explanatory Note to Bill 14-1, *supra* note 95, cited in Brown & Telfer, *supra* note 94 at 28.

¹⁰⁰ Given an exchange rate of 0.8219 (for 1 July 2007) the equivalent of the NZ\$1,000-40,000 range in Canadian dollars would be \$822-32,876. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53.

¹⁰¹ See Explanatory Note to Bill 14-1, *supra* note 95; *Insolvency Act 2006*, *supra* note 93, s. 363.

¹⁰² *Insolvency Act 2006*, *ibid.*, s. 377.

¹⁰³ *Ibid.*, s. 375. For example, if the debtor no longer meets the qualification requirements.

¹⁰⁴ *Ibid.*, ss. 363-65, 370, 372-76. See also Explanatory Note to Bill 14-1, *supra* note 95.

¹⁰⁵ Telfer, "New Zealand Bankruptcy Law Reform," *supra* note 94 at 265; Brown & Telfer, *supra* note 94 at 30.

no-fault bankruptcy procedure will be lost; the final legislation includes both fixed rules and general standards, but Telfer and David Brown note that it is not yet clear how well the criteria adopted will work in practice.¹⁰⁶

Under the system previously in place in New Zealand, a debtor could apply to a District Court for a summary instalment order if his or her debts amounted to less than NZ\$12,000,¹⁰⁷ and the District Court judge could make an order that was binding on creditors. An instalment order provided that a debtor could pay back his or her debts without the threat of legal action while the order was in force; the process was administered by a third party supervisor and imposed no costs on the debtor.¹⁰⁸ If a debtor decided to petition for bankruptcy, there was a NZ\$40¹⁰⁹ filing fee in the High Court, although a debtor could apply to have the fee waived if he or she could not afford the cost.¹¹⁰ However, if a debtor wished to apply for an early discharge (prior to the end of the three-year period), she had to retain counsel and appear in the High Court at considerable expense.

The NINA model in New Zealand appears to address the disadvantages of a bankruptcy system, like the Australian one, where poor debtors can obtain access without cost but must accept more onerous discharge provisions than higher income debtors can obtain with the help of counsel. In Canada, once poor debtors obtain access to the system, there is no distinction between them and higher-income debtors in terms of how they are treated. For that reason, we do not believe that it is necessary to create a separate NINA system in order to address our concerns about the treatment of poor debtors.

D. *United Kingdom*

The United Kingdom¹¹¹ has also embarked on insolvency law reform, and is working to implement a NINA procedure similar to that in

¹⁰⁶ Telfer, *ibid.* at 268.

¹⁰⁷ Given an exchange rate of 0.6802 (as of 1 July 2006, since the legislation came into force in 2006) the equivalent of the NZ\$12,000 maximum debt in Canadian dollars would be \$8,163. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53.

¹⁰⁸ New Zealand, Insolvency and Trustee Service, *Personal Bankruptcy Toolkit: Information To Help Advisors Assist People Facing Bankruptcy Or People In Bankruptcy*, online: <www.insolvency.govt.nz/its-docs/1/its-bankruptcy-manual-28June.pdf> [Personal Bankruptcy Toolkit] at 6.

¹⁰⁹ Given an exchange rate of 0.6802 (as of 1 July 2006, since the legislation came into force in 2006), the equivalent of the NZ\$40 fee in Canadian dollars would be \$27. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53.

¹¹⁰ *Personal Bankruptcy Toolkit*, *supra* note 108 at 7.

¹¹¹ For the purposes of this article, the United Kingdom refers to England and Wales, as Scotland and Northern Ireland operate under different insolvency regimes.

New Zealand.¹¹² In 2004, the Department for Constitutional Affairs (DCA) published a consultation paper entitled “A Choice of Paths: better options to manage over-indebtedness and multiple debt.”¹¹³ With regard to “can’t pay” debtors,¹¹⁴ the paper proposed two options: the introduction of a court-based debt relief order and a NINA procedure.¹¹⁵ Under the former option, a debtor would be released from his or her debts after twelve months, unless a creditor could provide evidence of non-declared assets. The recommendations for this option included a debt limit and an unspecified fee for debtors to enter the scheme.¹¹⁶ Since the publication of this report, the British Insolvency Service has focused on the latter NINA option, and developed what it deems “... a non-court based scheme of debt relief that would alleviate debt in certain cases where there is currently no realistic alternative, but which is simple and likely to be relatively cheap to administer.”¹¹⁷ The scheme is aimed at those people who cannot pay “even a portion of their debt within a reasonable timeframe”¹¹⁸—people with no assets, very little income, and a relatively low level of liabilities, and who cannot access any of the debt solutions available (such as bankruptcy).¹¹⁹

In March 2005, the Insolvency Service published a paper for discussion, which focussed solely on the NINA procedure, and recognized that “[t]here is a category of person who has fallen into debt and has no way out of it.”¹²⁰ British research has shown that “the great majority of people who fall into arrears with their household bills or credit commitments do so because they are in financial difficulty resulting from a change in circumstance or living long term on a low income.”¹²¹ These

¹¹² Donna McKenzie Skene & Adrian Walters, “Consumer Bankruptcy Law Reform in Great Britain” (2007) 20 *Am. Bank. L.J.* 101 at 127.

¹¹³ United Kingdom, Department for Constitutional Affairs, “A Choice of Paths: better options to manage over-indebtedness and multiple debt” (Consultation Paper CP 23/04) (20 July 2004), online: <<http://www.dca.gov.uk/consult/debt/debt.pdf>> [“Choice of Paths”].

¹¹⁴ “Can’t pay” in this context refers to debtors who cannot pay off their debts as opposed to debtors who cannot pay trustee fees.

¹¹⁵ “Choice of Paths,” *supra* note 113 at 43.

¹¹⁶ *Ibid.*

¹¹⁷ United Kingdom, The Insolvency Service, “Relief for the Indebted—An Alternative to Bankruptcy (March 2005), online: <<http://www.insolvency.gov.uk/insolvencyprofessionandlegislation/condocregister/consultationpaperwithnewannex1.pdf>> at 5 [“Relief for the Indebted”].

¹¹⁸ *Ibid.*

¹¹⁹ *Ibid.* at 18.

¹²⁰ *Ibid.* at 12.

¹²¹ Nicola Dominy & Elaine Kempson, “Can’t Pay or Won’t Pay?: A Review of Creditor and Debtor Approaches to the Non-Payment of Bills” (United Kingdom: University of Bristol & Department

debtors simply lack the money to make payments on time, and include people with low incomes who face unexpected expenditures; people who have had a sudden substantial fall in income, leaving them unable to meet all their commitments; and people with mental health problems that impair their ability to manage their finances.¹²² In England and Wales, the current fee to petition for bankruptcy is UK£310,¹²³ even if the debtor qualifies for remission of or exemption from court fees. The current fee for administering bankruptcy is UK£1,625.¹²⁴ Ideally, a DCA report notes, each bankruptcy estate should cover the costs of its administration. However, this does not always occur, with the result that bankruptcies where there are assets subsidize those where there are none. Waiving the UK£310 fee, the report argues, would mean that cross-subsidization between cases would increase.¹²⁵

The NINA scheme proposed by the paper would be operated by Official Receivers, who would be responsible for making debt relief orders that would result in debtors being discharged from their debts after a period of one year. The procedure would require an upfront entry fee, but less than the deposit required to initiate bankruptcy proceedings. As well, debtors would have to meet certain criteria to make use of the scheme.¹²⁶ The consultation paper proposed a restriction on the number of times a person could apply for an order, and recommended the use of an approved intermediary to collect information about the debtor's affairs, assist in filling out forms, and filter unsuitable applicants.¹²⁷ To balance the rights of creditors, the paper suggested a

of Constitutional Affairs, 2003), online: <http://www.pfrc.bris.ac.uk/publications/creditdebt/Reports/cant_paywontpay.pdf>.

¹²² *Ibid.*

¹²³ Given an exchange rate of 2.1333 (for 1 July 2007), the equivalent of the UK£310 fee in Canadian dollars would be \$661. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53.

¹²⁴ "Relief for the Indebted," *supra* note 117 at 13. Given an exchange rate of 2.1333 (for 1 July 2007), the equivalent of the UK£1,625 fee in Canadian dollars would be \$3,467. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53.

¹²⁵ "Relief for the Indebted," *ibid.*

¹²⁶ See *ibid.* at 25-28 for possible entry criteria: total liabilities of less than UK£15,000, a surplus income of no more than UK£50 per month after necessary living expenses, and no realizable assets over UK£300. Given an exchange rate of 2.3876 (for 1 March 2005, when the report was published) and Average Annual Rate of Inflation/% Decline in the Value of Money of 2.31 the equivalent figures would be: maximum liabilities (UK£15,000) = \$37,489; maximum surplus income per month (UK£50) = \$125; and maximum realizable assets (UK£300) = \$749. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53; inflation: Bank of Canada, *Inflation Calculator*, *supra* note 19.

¹²⁷ *Ibid.* at 23.

means for creditors to object to the making of an order on various grounds, such as failure to disclose assets, income, or liabilities.¹²⁸ The scheme would preserve the ultimate right of appeal to the courts.

After the consultation paper was published and comments received, the Insolvency Service published a second paper highlighting the responses.¹²⁹ The paper put forth the following recommendations:¹³⁰

- an upfront, non-refundable fee paid by debtor to administer the debt order relief scheme of no more than UK£100;¹³¹
- an administrative order, without the intervention of the courts;
- a restriction on the number of times a debtor can obtain an order (no more than once every six years);
- the use of an approved intermediary by the debtor when applying for an order, with intermediaries to be properly funded;
- a cap on permitted liabilities of UK£15,000;¹³²
- a cap on surplus income of UK£50¹³³ per month, with surplus income determined through a common financial statement and with the ability to review the cap so it can be amended if appropriate;
- an asset limit at UK£300,¹³⁴ but kept under review so it can be amended if appropriate; and

¹²⁸ *Ibid.* at 31.

¹²⁹ United Kingdom, The Insolvency Service, *Relief for the Indebted—an alternative to bankruptcy: Summary of Responses and Government Reply* (November 2005), online: <http://www.insolvency.gov.uk/insolvencyprofessionandlegislation/con_doc_register/relieffortheindebtedanalternativetobankruptcyresponse.pdf> [*Relief for the Indebted Responses & Reply*].

¹³⁰ *Ibid.*, at 5-7.

¹³¹ For further detail, see *ibid.* at 12-13. Given an exchange rate of 2.0739 (for 1 November 2005, when the report was published) and Average Annual Rate of Inflation/% Decline in the Value of Money of 2.31 the equivalent in 2007 Canadian dollars would be \$217. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53; inflation: Bank of Canada, *Inflation Calculator*, *supra* note 19.

¹³² The paper recommends that secured debt be included for the purposes of ascertaining the level of liabilities; the position of secured creditors would not be affected, as they would retain their security. *Relief for the Indebted Responses & Reply*, *supra* note 129 at 22. Given an exchange rate of 2.0739 (for 1 November 2005, when the report was published) and Average Annual Rate of Inflation/% Decline in the Value of Money of 2.31 the equivalent in 2007 Canadian dollars would be \$32,564. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53; inflation: Bank of Canada, *Inflation Calculator*, *supra* note 19.

¹³³ Given an exchange rate of 2.0739 (for 1 November 2005, when the report was published) and Average Annual Rate of Inflation/% Decline in the Value of Money of 2.31 the equivalent in 2007 Canadian dollars would be \$109. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53; inflation: Bank of Canada, *Inflation Calculator*, *supra* note 19.

¹³⁴ Given an exchange rate of 2.0739 (for 1 November 2005, when the report was published) and Average Annual Rate of Inflation/% Decline in the Value of Money of 2.31 the equivalent in 2007 Canadian dollars would be \$651. Exchange rate: Bank of Canada, *Daily noon rates*, *supra* note 53; inflation: Bank of Canada, *Inflation Calculator*, *supra* note 19.

– provision for an appropriate range of remedies to tackle misconduct by the debtor.¹³⁵

More recently, the British government has put forward recommendations for the other option identified in the 2004 report: the availability of a court-based debt-relief order. Instead of implementing such an order, however, the DCA has advocated the administrative NINA scheme, deeming the court-based option not cost effective for “can’t pay” debtors.¹³⁶ These reforms are encompassed in the draft *Tribunals, Courts and Enforcement Bill* as a means to provide debt relief for people in the United Kingdom who cannot access currently available remedies, and who have no way to pay what they owe.¹³⁷

An annex to the bill outlines the various options considered by the UK government for “can’t pay” debtors: removing the requirement for people without assets or surplus income to pay a deposit when presenting a petition for bankruptcy, persuading creditors to voluntarily write off debt where there is no prospect that the debt will be paid within a reasonable amount of time, or introducing legislation to enable poor people who are financially excluded to access a system of debt relief.¹³⁸ Preferring a legislative response, the report suggests that the proposal for the NINA scheme would benefit the indebted individual in terms of reduced stress and the effect on health accompanying it,¹³⁹ provide an opportunity for a fresh start, allow him or her to “learn to manage their finances in more favourable circumstances,”¹⁴⁰ and free up court time in cases where creditors are pursuing enforcement action where there is no hope of repayment.¹⁴¹ The DCA anticipates that the scheme will entail initial set-up costs, but with an upfront fee (less than current bankruptcy deposit), it will be possible to meet ongoing

¹³⁵ See *Relief for the Indebted Responses & Reply*, *supra* note 129 at 31-35 for further detail; see also Skene & Walters, *supra* note 112 at 129.

¹³⁶ United Kingdom, Department for Constitutional Affairs, “Explanatory Notes” annexed to the (Draft) *Tribunals, Courts and Enforcement Bill* (25 July 2006), online: <<http://www.official-documents.co.uk/document/cm68/6885/6885.pdf>> [(Draft) *Tribunals, Courts and Enforcement Bill*] 82 at 109.

¹³⁷ United Kingdom, The Insolvency Service, “Plans to Bring Debt Relief to the Socially Excluded,” n.d., online: <<http://www.insolvency.gov.uk/insolvencyprofessionandlegislation/intermediariesworkinggroup/debtrelief.htm>>.

¹³⁸ “Debt Relief Orders” in (Draft) *Tribunals, Courts and Enforcement Bill*, *supra* note 136, 112 at 117-18.

¹³⁹ *Ibid.* at 126.

¹⁴⁰ *Ibid.*

¹⁴¹ *Ibid.* at 127.

administration costs.¹⁴² The DCA predicts the number of people who will use the NINA scheme would plateau at between 34,000 to 36,000 after two years, and that number will increase or decrease with the number of bankruptcies after that point.¹⁴³ Approximately 11% of people currently presenting a bankruptcy petition would be eligible for the new scheme.¹⁴⁴ The scheme, the DCA predicts, will apply to a substantial portion of those seeking advice for debt related problems, who owe less than the proposed liability cap of UK£15,000 and who are not homeowners.¹⁴⁵ The NINA procedure is not currently in effect in the United Kingdom.

The proposed NINA procedure in the United Kingdom responds to a situation more similar to the Canadian system than the New Zealand system. That is, bankruptcy is currently a high-cost process that is not accessible to poor debtors in the United Kingdom. The NINA procedure does not seek to mimic the Australian or mainstream New Zealand models by adding additional restrictive discharge conditions as a trade-off for low-cost access to the system. Rather, the NINA procedure represents a recognition that legislative action is required to provide a low-cost option for bankruptcy for “poor debtors.”

As will be seen in the discussion that follows, while the debates in both the United Kingdom and New Zealand that informed the reform process in these jurisdiction is significant for our analysis, we do not see the need to create a new NINA stream in order to improve access to the bankruptcy system for poor debtors in Canada.

VI. POSSIBLE MODELS FOR THE CANADIAN BANKRUPTCY SYSTEM

The most problematic aspect of the current Canadian system is that—depending on where they live—poor debtors in Canada face different prospects for accessing the bankruptcy system, and face different costs for doing so. In each trustee interview, drawing on the Australian model, we suggested an option that would see poor debtors fill out a simple set of forms and then go to a kiosk in the local shopping mall where the forms and supporting documents could be filed and the

¹⁴² *Ibid.* at 129-30.

¹⁴³ *Ibid.* at 115.

¹⁴⁴ *Ibid.* at 127.

¹⁴⁵ *Ibid.* at 115.

bankruptcy accomplished. We also discussed a variant in which a trustee (or other qualified insolvency professional) might assess the debtor's case before he or she was eligible to use the kiosk. None of the trustees interviewed thought that either option was a good idea.

A. *Trustees' Views on Possible Models*

1. Unanimously Against a Government-Operated System

Perhaps not surprisingly, the private trustees that we interviewed were unanimous in rejecting the idea of a new government-funded and government-staffed program that would handle the bankruptcies of poor debtors. Several recognized that their opposition would be expected, given that any new government-provided service would compete with their own practice. However, it seems clear that their opposition goes beyond simple self-interest.

The trustees agreed that a trained professional should be closely involved in order to handle unexpected situations. One noted that the "trustee learns more about the cases over the nine months, [through] information that would not be available at the time of application."¹⁴⁶ With this in mind, all of the trustees we spoke to expressed the belief that a government program would require one of two unpalatable staffing options. One option would involve the training of a completely new cadre of insolvency professionals to replace the work now done by trustees. The trustees saw little benefit in training a new group to undertake work that they themselves have been trained to do. A second option would be to use less-qualified staff, on the assumption that poor debtors will have simple bankruptcy cases; the trustees thought that such staff would not be able to handle the issues that often arise even in simple cases. Several harked back to the days of Federal Insolvency Trustee Agency (FITA), which seems to be universally reviled as having failed because of the incompetence of its staff.¹⁴⁷ One said that there are "lots of horror stories from FITA. Files that

¹⁴⁶ Interview with Trustee 2, *supra* note 17.

¹⁴⁷ The federal government introduced FITA in 1972 to provide services for those debtors who could not afford a trustee. By 1977, between one third and one half of bankruptcies proceeded under FITA. The program was discontinued in 1979: Igor Livshits, "Accounting for the Rise in Consumer Bankruptcies in Canada and the United States" by Igor Livshits, James McGee & Michèle Tertilt (Paper presented to the York University Department of Economic Seminar Series 2005-2006, 9 March 2005) [unpublished], online: York University Department of Economics <<http://dept.econ.yorku.ca/seminars/2004-2005/BankruptcyRise.pdf>>. Despite the oft-heard opinion that FITA was disastrous because

never got closed, people not getting real assets.”¹⁴⁸ Another believed that “the government employees [of FITA] were not qualified [to administer bankruptcies].”¹⁴⁹ Still another asserted that “the system collapsed because the government was not equipped to handle it and debtors were not advised properly” and that “debtors were not discharged [because] the system was not tracking them.”¹⁵⁰

2. Unanimously Against Making Access Too Easy

The trustees we interviewed had either participated in a BAP case or worked on a number of files with less than \$500 in receipts. All but one were working in firms in which a large part of the work was in consumer bankruptcy, and all showed considerable understanding and sympathy for the plight of poor debtors. Nonetheless, even these trustees were emphatic that bankruptcy should not be made too easy. Their view was that the absence of significant barriers would lead to the abuse of credit and to the abuse of the bankruptcy system.

Apart from their staffing the trustees felt that the kiosk option (or any sort of “car wash” form of bankruptcy) would not provide enough rehabilitation (such as they believe arises from mandatory bankruptcy counselling). A system that allowed too easy a discharge would not teach the debtor any lessons about the misuse of credit and would presumably lead to repeated credit trouble. One trustee felt that counselling made debtors face their responsibility for incurring the debts that led to the bankruptcy, and thought that bankruptcy “shouldn’t be a wash.”¹⁵¹ Others¹⁵² were concerned that the debtors would not learn anything if the procedure was too simple: “They need to learn something so they don’t come back.”¹⁵³ Another thought that in the current system, “the debtors have responsibilities—to get counselling, to report changes in their situation, to make monthly payments, to turn over their financial affairs to the trustee.”¹⁵⁴

bankruptcies were mishandled by incompetent or poorly trained staff, we have seen no documentary evidence of the shortcomings of FITA.

¹⁴⁸ Interview with Trustee 8, 8 September 2006.

¹⁴⁹ Interview with Trustee 3, *supra* note 23.

¹⁵⁰ Interview with Trustee 1, *supra* note 4.

¹⁵¹ Interview with Trustee 8, *supra* note 148.

¹⁵² Interview with Trustee 5, *supra* note 3; Interview with Trustee 3, *supra* note 23.

¹⁵³ Interview with Trustee 5, *ibid.*

¹⁵⁴ *Ibid.*

3. Recent Canadian Reform Efforts

During the deliberations of the Canadian Personal Insolvency Task Force (PITF), a subgroup was assigned to address issues around the “administration process.” The subgroup quickly became focused on the idea of creating a “fast track” process for the many bankruptcy files that are quite simple, because they involve no significant assets and offer little prospect of creditors receiving any significant dividends. A key decision, made without extensive open discussion, was that the “fast track” process would lie within the existing Canadian bankruptcy system, and not require a public trustee as in the Australian case. In a discussion on the Australian system, the subgroup wrote that, given the current Canadian system, a shift to a system with the role of trustee filled by a public actor would be “politically unfeasible.”¹⁵⁵

The definition of eligibility for the “fast track” process was not based on any notion of the need for low-cost bankruptcy services. The subgroup mentioned that there are no reliable data suggesting that there is an issue with access to bankruptcy for poor debtors,¹⁵⁶ and one member questioned whether the subgroup should address affordability at all.¹⁵⁷ In addition, the subgroup (and the PITF as a whole) decided not to tackle the controversial issue of the fees charged by the trustees, which are currently set by trustees within the framework of Rule 128(1).¹⁵⁸ There was some debate within the subgroup as to whether competition would help to decrease fees, and some group members felt that advertising fees would help resolve this issue. Ultimately, however, the subgroup did not create any concrete recommendations on the issue.

The Canadian Association of Insolvency Professionals (CAIRP) and Insolvency Institute of Canada (IIC) made a joint submission to the Standing Senate Committee on Banking, Trade and Commerce.¹⁵⁹ That submission acknowledged that the dissenting members of the PITF raised several issues in respect of access to the process that require further

¹⁵⁵ “Preliminary Draft #2” (PITF subgroup deliberations, 27 November 2000) [unpublished, document on file with the authors] at 6.

¹⁵⁶ *Ibid.* at 9.

¹⁵⁷ John Eisner quoted in “Record of Decision From Conference Call” (PITF subgroup deliberations, 15 November 2000) [unpublished].

¹⁵⁸ See Part III, above, for a more detailed discussion.

¹⁵⁹ CAIRP/IIC, “Submission on Personal Insolvency Reform” (March 2003), online: <<http://www.cairp.ca/pdf/Mar262003.pdf>> at 68-69.

investigation and study, including how the costs of an alternative process would be covered, how access for such debtors would be increased through any alternative process, and how the integrity of the system would be maintained or enhanced. CAIRP/IIC made two recommendations in respect of access to information and assistance to debtors with no assets and no income. First, it recommended that there be increased information provided to debtors about their options, including the trustee referral program. The submission also recommended that the OSB increase the information it disseminates, and “address issues such as garnishees and how to get them lifted or reduced; how to stop harassing phone calls from collection agencies; strategies to deal with temporary layoffs and salary reductions; and key telephone numbers through which to access these remedies and other public agencies.”¹⁶⁰

Neither of the CAIRP/IIC recommendations was adopted in the *Report of the Standing Senate Committee on Banking, Trade and Commerce*.¹⁶¹ The Senate Report did not address trustee fees directly.¹⁶² However, unlike the PITF subgroup, the Senate Report recognized that “access to the bankruptcy system is increasingly compromised for low-asset, low-income debtors,” although it did not recommend reforms such as adopting a NINA process.¹⁶³

Most recently, Statute c. 47¹⁶⁴ provides for the following new section (section 156.1) to allow bankrupts to enter into an agreement to pay for the trustee’s fees after the bankruptcy period:

An individual bankrupt who has never before been bankrupt under the laws of Canada or of any prescribed jurisdiction and who is not required to make payments under section 68 to the estate of the bankrupt may enter into an agreement with the trustee to pay the trustee’s fees and disbursements if the total amount required to be paid under the agreement is not more than the prescribed amount and that total amount is to be paid before the expiry of the 12-month period after the bankrupt’s discharge. The agreement may be enforced after the bankrupt’s discharge.¹⁶⁵

¹⁶⁰ *Ibid.* at 69.

¹⁶¹ Canada, Standing Senate Committee on Banking, Trade and Commerce, “Debtors and Creditors Sharing the Burden: A Review of the *Bankruptcy and Insolvency Act* and the *Companies’ Creditors Arrangement Act*” (November 2003), online: Senate of Canada, Banking, Trade and Commerce Committee <<http://www.parl.gc.ca/37/2/parlbus/commbus/senate/com-e/bank-e/rep-e/bankruptcy-e.pdf>> [Senate Report].

¹⁶² *Ibid.*

¹⁶³ *Ibid.* at 168.

¹⁶⁴ Statute c. 47, *supra* note 14.

¹⁶⁵ Statute c. 47, *ibid.*; Canada, Industry Canada, Corporate and Insolvency Law Policy “*BIA*:

The clause-by-clause briefing notes that this new section is intended:

... to provide a mechanism which will enhance accessibility to the insolvency system for individuals who do not have surplus income and who may otherwise have difficulty paying the costs associated with the administration of a bankruptcy. In some circumstances, especially bankruptcies with small estates, it is difficult for a person to find a trustee willing to act for them because the trustees require payment for their services. If the estate is too small, no trustee will act. This has the effect of leaving the vulnerable person without professional assistance during a difficult experience. By providing that the bankrupt may pay for the trustee's services after the bankruptcy period, the reform should ensure that more people get the assistance they need. Balancing this reform is the limit on fees that can be charged by a trustee pursuant to the rules.¹⁶⁶

The possibility of deferring trustee fees may assist access to the bankruptcy process. However, it represents an intrusion into the fresh start for a particular group of debtors, which may include the group we define as poor debtors, who cannot afford the cost of bankruptcy.

VII. RECOMMENDATIONS

In this penultimate section of the paper, we propose three sets of recommendations. Each set of recommendations addresses the two principal flaws we believe are present in the current Canadian system:

- No national or even local uniformity exists in the treatment of poor debtors.
- Poor debtors face informational and financial barriers that may impede equal access to the fresh start provided by bankruptcy.

Within each set of our recommendations, some may be implemented quite quickly and with limited cost. Others will take longer to implement and will require additional consultation and funding. In particular, further review will be necessary to determine the exact budgetary implications of our recommendations.

The two flaws highlighted by our research do not lead us to recommend the adoption of a separate bankruptcy scheme for poor debtors or NINA debtors. Instead, we recommend that Canada adopt a BAP system that eliminates the out-of-pocket costs for poor debtors. These costs could be eliminated with a combination of fee waivers (*e.g.*, waiving the

Administration of Estates” in *Bill C-55: clause-by-clause analysis: An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies’ Creditors Arrangement Act and to make consequential amendments to other Acts*, (n.d.), online: <<http://strategis.ic.gc.ca/epic/internet/incilp-pdci.nsf/en/cl00813e.html>>.

¹⁶⁶ *Ibid.*

OSB's filing fee) and government subsidy (*e.g.*, having the OSB pay for the mandatory counselling sessions). A BAP system that demands no out-of-pocket payments by poor debtors would address the financial barriers they face. To deal with the informational barriers, we recommend the creation of an impartial agency that provides advice and support to poor debtors trying to deal with collection efforts. We recognize that, in some instances, bankruptcy might not be the appropriate solution for poor debtors and that other options should be available to deal with creditor aggression. By making the judgment-proof status of poor debtors clear, such advice and support provided by an impartial agency would limit the number of debtors who use the bankruptcy process. Finally, to increase the uniformity and certainty of bankruptcy across the country, we propose a method for creating parity while encouraging the voluntary agreements among trustees that exist in some cities.

In addition to the trustee interviews, our recommendations are informed by the analysis found in our comparative account in Part V of this article. In particular, we believe that the situation in New Zealand and Australia provides low-cost access to the bankruptcy process but we do not agree with corresponding to changes to the system that make the process more burdensome for "poor debtors." At the same time, we are persuaded by the arguments in favour of eliminating fees made as part of the reform process in the United States, Australia, New Zealand, and the United Kingdom.

A. *Reform of BAP Regulations*

Our research suggests that a thorough revision of the rules governing the operation of the BAP system is necessary. Our review of the program suggests that the following changes are highly desirable.

RECOMMENDATION 1:

Widespread and improved publicity of the BAP is required.

One reason for the infrequent use of the BAP is that the OSB has made no systematic efforts to make its existence known to poor debtors. Much more information on the operation of the BAP system should be made easily accessible to debtors and trustees. Detailed information on the BAP should be provided to poverty clinics, credit counsellors, and trustees. The information on the OSB website related to the BAP should be updated and improved. The information is difficult to find, and does not give a balanced and accurate sense of the program. For example, the

website currently gives the impression that the BAP requires pro bono work by trustees.¹⁶⁷

RECOMMENDATION 2:

A clear eligibility standard for the BAP should be put into place.

Further consultation should be undertaken to determine the exact nature of a new BAP-eligibility standard. Based on our research to date, we recommend a standard involving low current income and a long-term history of receipt of government transfers. Using low current income alone might lead to abuse by debtors who only temporarily have low income. The appropriate requirement might be that eligible debtors must be in receipt of government transfers (such as income assistance, unemployment insurance, or disability benefits) for twelve of the previous eighteen months. The critique of the New Zealand model presented by Brown and Telfer warns against moving to a standard for eligibility that allows for any significant degree of subjectivity.¹⁶⁸ In addition, some form of procedural fairness will need to be built into such a bright-line eligibility standard. For example, appeals should be allowed by claimants whose status as “poor debtors” is recent but likely to be permanent, *e.g.* by reason of disability.

Under this new eligibility standard, the requirement that debtors must visit two trustees to qualify for the BAP should be eliminated. This requirement imposes an additional barrier to bankruptcy that higher income debtors do not face. The current requirement has a detrimental impact on women in particular, as they must often find care for their children as they move around the city obtaining opinions from two trustees.

RECOMMENDATION 3:

Fees for debtors who qualify for the BAP should be waived.

Ideally, poor debtors should be able to file for bankruptcy without paying any of the out-of-pocket costs. Receipts from tax refunds would remain in the estate, as would any proceeds from the sale of non-exempt assets. The fee waiver could be financed by a combination of OSB waivers, OSB payments to trustees for counselling, or pro bono work by trustees. Further consultation needs to be done with trustees, combined with a careful cost analysis by the OSB, in order to determine

¹⁶⁷ The information is limited to “Directive No. 11,” *supra* note 25.

¹⁶⁸ *Supra* note 94.

the ideal solution. In the interim, we recommend that the \$75 filing fee be eliminated, and that the OSB cover the cost of both counselling sessions. The high mean level of fees in BAP cases means that trustees can recover significant amounts without voluntary payments.

RECOMMENDATION 4:

The BAP should provide that the OSB will file the bankruptcy as a last resort.

The regulations (and the expanded publicity recommended above) should indicate the OSB's commitment to ensuring that the bankruptcy will be filed in a timely fashion even if no private trustee is forthcoming, and even if an OSB official must administer the bankruptcy.

B. *Working Toward Uniformity*

In comparison to the other jurisdictions considered, the issue of uniformity appears to be a uniquely Canadian issue. Poor debtors throughout Canada should have access to the reformed BAP. However, our interviews suggested that trustees are not happy with the existing BAP and, where possible, prefer to rely on voluntary agreements among area trustees or on the goodwill of individual trustees. At least until the reformed BAP can gain the confidence of trustees, we recommend that the voluntary agreements among trustees be encouraged and perhaps expanded in scope. However, these voluntary systems should be at least as affordable as BAP. A first step would be to assess the extent of the geographic coverage of the agreements. CAIRP could become involved by surveying its members to make an inventory of such agreements. Second, the OSB should keep track of files where receipts are low to see if they are spread, in a representative way, across the country.¹⁶⁹

RECOMMENDATION 5:

The OSB should establish, by directive, a system for registering city-specific fee agreements reached by trustees.

While we believe that the voluntary agreements should be encouraged, we also think the OSB should make sure that it is aware of all such agreements and ensure that the terms of the agreements are

¹⁶⁹ To aid in this effort, the Statements of Receipts and Disbursements should be modified so that voluntary payments are shown in a uniform way. As explained in Appendix III, the current form does not allow all voluntary payments to be identified.

consistent with the aim of the reformed BAP: ease of access and low out-of-pocket costs to the debtor. In the end, it is not obvious whether it will be better to have only a reformed BAP, only a set of voluntary agreements, or a combination of the two. Informed decision making about the need for the BAP can only be made if a close watch is kept on the operation of the voluntary agreements.

C. *Impartial Agency*

RECOMMENDATION 6:

An impartial agency should be created to give poor debtors advice on how to deal with their debt.

Currently, Canadian debtors have no place to turn for impartial debt advice. Debtors can seek advice from credit counselling services, but these are either financed by creditors or are for-profit, fee-charging entities; most require 100% repayment.¹⁷⁰ Trustees are another possible source of advice, but they have a clear incentive to recommend bankruptcy. The creation of a neutral agency that provides advice on debtors' rights vis-à-vis their creditors and suggests the most appropriate remedy is recommended. We recommend the creation of an impartial debt advice agency in two to three pilot sites in the short term.

VIII. CONCLUSION

In this paper, we have examined the question of whether poor debtors—defined as those who have very low income and few prospects for higher future income—need greater access to bankruptcy. Our answer is that they do, despite the fact that most are judgment-proof, despite the fact that trustees in some cities have banded together to address their needs, and despite the fact that the OSB's BAP system exists to serve their needs. First, poor debtors need greater access to bankruptcy because their judgment-proof status does not, in practice, prevent aggressive collection efforts and will end if they are ever to escape poverty. Second, the efforts of trustees are limited to a few cities,

¹⁷⁰ The Office of Consumer Affairs recently published a study of credit counselling which highlights the lack of regulation of that industry and its potential bias. Saul Schwartz, "Counselling the Overindebted: A Comparative Perspective" (2005), online: Office of the Superintendent in Bankruptcy <[http://strategis.ic.gc.ca/epic/site/bsf-osb.nsf/vwapj/Schwartz-2005-ENG.pdf/\\$FILE/Schwartz-2005-ENG.pdf](http://strategis.ic.gc.ca/epic/site/bsf-osb.nsf/vwapj/Schwartz-2005-ENG.pdf/$FILE/Schwartz-2005-ENG.pdf)>.

meaning that there is no uniformity of treatment across the country. And, finally, the BAP is little used and in need of significant reform.

To help those poor debtors who may need greater access, we advance three sets of recommendations. The most important of these is that the out-of-pocket costs of bankruptcy (the \$75 filing fee and the \$180 cost of the two mandatory counselling sessions) be waived for poor debtors, defined in this paper by low income and a history of reliance on government transfers. Since it is common for tax refunds to generate significant receipts for the estates even of poor debtors, there may be trustees who are willing to handle the files of poor debtors once the out-of-pocket costs are waived. Accordingly, we recommend that the OSB undertake to be the trustee of last resort, and handle files that private trustees are unwilling to take on.

Finally, poor debtors not only face financial barriers to bankruptcy but also informational barriers. We therefore recommend the creation of an impartial debt advice service that could help overcome these barriers and, in addition, help debtors at all income levels avoid over-indebtedness.

APPENDIX I: DESCRIPTION OF TRUSTEE INTERVIEWS

- Trustee 1 Trustee 1 works in Montreal in a mid-market, regional chartered-accounting and consulting firm with offices in Toronto and Montreal. She has recently moved offices, and the exact number of files and division of consumer/commercial files is not yet available. The primary target market for the firm is privately held companies ranging from \$10 million in revenues to complex organizations with annual revenues of \$150 million.
-
- Trustee 2 Trustee 2 works in the Windsor area, administering approximately 100 bankruptcy files per year. 95% of her business encompasses consumer bankruptcies.
-
- Trustee 3 Trustee 3 is a sole practitioner in Edmonton, having previously worked for large accounting firms and other sole practitioners. She has a social work background. Her practice is composed entirely of consumer bankruptcies, administering about 250 files per year. She has twenty years of experience in the bankruptcy field.
-
- Trustee 4 Trustee 4 is member of a mid-size accounting firm in Toronto where he heads the insolvency division. He has been in practice since the early 1980s, formerly with large accounting firms. He is a specialist in both corporate and personal bankruptcy, providing consulting services to both debtors and creditors.
-
- Trustee 5 Trustee 5 is a sole practitioner in London (Ontario). His firm primarily administers consumer bankruptcies, with 95% of the business focusing on consumer files.
-
- Trustee 6 Trustee 6 works in Halifax, in an office of four trustees; he specializes in the areas of financial restructuring, receivership, and bankruptcy. Trustee 6's firm undertakes both corporate and consumer bankruptcies, handling about 500 consumer bankruptcies each year.
-
- Trustee 7 Trustee 7 works for a small firm with offices in Toronto, Kingston, and Brockville. The business handles mostly consumer files, approximately 400 per year. He has worked as a trustee for ten years.
-
- Trustee 8 Trustee 8 has worked six of her eleven years as a trustee in private practice. She currently handles bankruptcy files in the Greater Toronto Area, administering approximately 400 bankruptcies each year.
-
- Trustee 9 Trustee 9 works at a national firm in Ottawa.
-
- Bankrupt This poor debtor (under our definition) has been through the bankruptcy system two times. The second time she was assigned into bankruptcy it was under the BAP program. She was referred to us by her BAP trustee.

APPENDIX II: *BIA*, RULE 128(1)

Also, see OSB Circular 2,¹⁷¹ which was introduced in 1999 and imposes the \$10,000 maximum.

TRUSTEE'S FEES AND DISBURSEMENTS IN SUMMARY ADMINISTRATION

128. (1) The fees of the trustee for services performed in a summary administration are calculated on the total receipts remaining after deducting necessary disbursements relating directly to the realization of the property of the bankrupt, and the payments to secured creditors, according to the following percentages:
- (a) 100 per cent on the first \$975 or less of receipts;
 - (b) 35 per cent on the portion of the receipts exceeding \$975 but not exceeding \$2,000; and
 - (c) 50 per cent on the portion of the receipts exceeding \$2,000.
- (2) A trustee in a summary administration may claim, in addition to the amount set out in subsection (1),
- (a) the costs of counselling referred to in subsection 131(2);
 - (b) the fee for filing an assignment referred to in paragraph 132(a);
 - (c) the fee payable to the registrar under paragraph 1(a) of Part II of the schedule;
 - (d) the amount of applicable federal and provincial taxes for goods and services; and
 - (e) a lump sum of \$100 in respect of administrative disbursements.
- (3) A trustee in a summary administration may withdraw from the bank account used in administering the estate of the bankrupt, as an advance on the amount set out in subsection (1),
- (a) \$250, at the time of the mailing of the notice of bankruptcy;
 - (b) an additional \$250, thirty days after the date of the bankruptcy; and
 - (c) an additional \$250, four months after the date of the bankruptcy.
- (4) Subsections (1) to (3) apply to bankruptcies in respect of which proceedings are commenced on or after September 30, 1997 and the accounts are taxed on or after April 30, 1998.

¹⁷¹ Canada, OSB, Circular No. 2, "Summary Administration Estates With Realizable Assets Exceeding \$10,000" (16 September 1999), online: Strategis <<http://strategis.ic.gc.ca/epic/site/bsf-osb.nsf/en/br01101e.html>>.

APPENDIX III: NOTES ON DATA

The data analysis reported at several points in the text was conducted by the Business Intelligence Centre (BIC) of the OSB. The statistical analysis of consumer bankruptcy was greatly eased by the advent of electronic filing on 1 January 2002; most documents related to consumer bankruptcies are now electronically submitted and can be analyzed quickly and accurately.

Two factors determined our choice of a data file on which to base our analysis. First, our analysis was concerned with trustee fees, so we needed a sample of bankruptcies that had electronically submitted Statements of Receipts and Disbursements (SRD). The SRD shows all receipts and disbursements arising from a consumer bankruptcy, including trustee fees, voluntary payments by debtors and dividends disbursed to the creditors. The trustee typically submits the SRD to the OSB at least nine months after the bankruptcy is filed, close to the date when the bankruptcy file is closed. Second, most bankruptcies filed by poor debtors will be summary administration cases so we wanted to limit the analysis to such files.

These two factors led us to choose to analyze all summary administration bankruptcies for which an SRD was electronically submitted between 1 January 2006 to 31 December 2006. According to BIC, there were 29,279 such bankruptcies available for analysis.

Note that these are not all summary administration bankruptcies *filed* in the calendar year 2006. Because of the lag between the filing of a bankruptcy and the submission of an SRD months (and possibly years) later, many of the bankruptcies that we analyze will have been filed in calendar 2005 (and, for a small number, in 2004). Furthermore, we are looking only at SRDs submitted electronically. Nonetheless, we do not expect that substantial bias is introduced by our use of electronically submitted SRDs. Finally, not all of the bankruptcies in our analytic file were closed in calendar 2006. After the trustee submits the SRD, the OSB sends the trustee a letter of comment approving the closing of the file. For that reason, not all bankruptcies for which an SRD was received in the calendar year 2006 will have been closed in the calendar year 2006.

All of the statistical information in this paper was generated by BIC using the 29,279 electronically filed cases with SRDs. Many variables, including the dividend paid to creditors and the level of trustee fees, can be accurately derived from the electronically filed cases. However, the value of voluntary payments made by the debtor to the trustee must be estimated because trustees are not required to report such payments in a consistent fashion. Most trustees, however, report them by noting their existence in the SRD. For example, a particular dollar amount in the receipt portion of the SRD might be identified as “voluntary payment” or “payment by debtor.” In some cases, however, voluntary payments will have been made but there is no way to identify them on the SRD.