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THE ROLE OF CONSUMER COUNSELLING AS PART OF THE BANKRUPTCY PROCESS IN EUROPE[©]

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Debt counselling belongs to a cluster of concepts such as community, family values, sex education, and globalization that every one supports, but no one really knows what they mean. The meaning of debt counselling is obscure, not only because it is new, but also because the concept is used to describe quite different activities in different countries and jurisdictions. The goals of debt counselling, however, are almost always defined in the same way: *prevention* of debt problems, *rehabilitation* of the debtor, and *emancipation* of the debtor from compulsive consumption and use of consumer credit. How these goals are achieved or emphasized differs among jurisdictions.

In the following discussion I will distinguish three different views about debt counselling. Two of them are based on my knowledge of debt counselling in various European countries. By way of contrast, the third begins with the conception of debt counselling expressed in the article by Ruth Berry and Sue McGregor.¹ Following the prescription adopted by the Working Group of the Office of the Superintendent of Bankruptcy in Canada, Berry and McGregor define the purpose of debt counselling as providing the debtor with consumer education skills to reduce the likelihood of repeat insolvency and bankruptcy.² In other words, the primary aim is to avoid future or repeat calamities and bankruptcies. To achieve this, the debtor mainly needs financial management and planning skills to run his or her future budget and to finance future consumption. The debtor also needs traditional consumer educational skills to make informed decisions in the market, including decisions about using new credit. The consumer education and counselling that

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¹ R.E. Berry & S.L.T. McGregor, "Counselling Consumer Debtors Under Canada's *Bankruptcy and Insolvency Act*" (1999) 37 *Osgoode Hall L.J.* 369.

² *Ibid.* at 374.

Berry and McGregor advocate presupposes that the debtor will receive a discharge of his or her debts in bankruptcy.

In continental Europe,³ the relationship between the judicial consumer bankruptcy process and debt counselling is of recent origin for the simple reason that the first consumer bankruptcy laws were not adopted until the early 1990s.⁴ Before that time, the continental European bankruptcy laws did not recognize the possibility of a discharge from consumer debts. Similarly, business bankrupts were also not entitled to a discharge. When the new consumer bankruptcy laws were enacted most countries started to provide debt counselling as part of, or in relation to, the bankruptcy proceedings.

Even those many European countries that still do not have consumer bankruptcy laws have introduced experimental schemes in debt counselling. Other European countries (notably Germany, Sweden, and to some extent Norway) established debt counselling programs before the consumer bankruptcy laws were passed. For example, the German Parliament approved a new insolvency law in 1994 that includes provisions on consumer bankruptcies, but the law only came into force in the beginning of 1999.⁵ Debt counselling, however, was already initiated in Germany in the 1970s by organizations aiding persons released from prisons and other institutions; it has since been expanded so that it is now available to all consumers in need of it. Debt counselling is provided by consumer organizations, social agencies, charitable organizations, trade unions, and other not-for-profit institutions.

In all the continental European countries, debt counselling is part of the welfare state regime. It is usually combined with access to other social services, because debtors may need information about, and referrals to, services such as social security and assistance, low-cost housing, treatment for substance abuse, marriage counselling, etc. Debt

³ My comments are confined to the continental European countries, and do not include the bankruptcy laws of the United Kingdom and Ireland, which have a different history and philosophy. The Anglo-Saxon bankruptcy regimes are discussed by other contributors to this Symposium: see J.D. Honsberger, Q.C., "Philosophy and Design of Modern Fresh Start Policies: The Evolution of Canada's Legislative Policy" (1999) 37 Osgoode Hall L.J. 171; J.S. Ziegel, "The Philosophy and Design of Contemporary Consumer Bankruptcy Systems: A Canada-United States Comparison" (1999) 37 Osgoode Hall L.J. 205; R. Mason, "Consumer Bankruptcies: An Australian Perspective" (1999) 37 Osgoode Hall L.J. 449; and P. Heath, Q.C., "Consumer Bankruptcies: A New Zealand Perspective" (1999) 37 Osgoode Hall L.J. 427.

⁴ For a detailed description of the European development and different laws, see J. Niemi-Kiesiläinen, "Consumer Bankruptcy in Comparison: Do We Cure a Market Failure or a Social Problem?" (1999) 37 Osgoode Hall L.J. 473.

⁵ See *Insolvenzordnung* 5.10.1994 §§ 304-314.

counselling can also be seen as part of a general program of consumer advice and policy. Some European countries emphasize the first approach, others the second.

Institutionally, debt counselling has been arranged quite differently in the various European countries.⁶ In the Scandinavian countries, the counselling is provided by state and county agencies that are connected with consumer or social service agencies. In Germany, private organizations, connected with churches and sometimes with labour unions, have traditionally also played an important role. More recently, specialized, consumer debt counselling organizations, often supported by public funding, have been responsible for the development of counselling in Germany. The private sector has not been quick to react to the demands for debt counselling. Some social banks, notably the municipal banks in the Netherlands, provide counselling.

In jurisdictions without a judicial debt adjustment law, the debtor's rehabilitation is not possible through discharge, but rather requires some debt repayment.⁷ Very often it is a central task of the counsellor to draft a payment plan and to initiate negotiations about rescheduling, either with an individual creditor or with all creditors. Especially in Germany, debt counsellors have been successful in negotiating comprehensive payment plans with considerable reductions in total debt, in the absence of a judicial debt adjustment scheme. The general experience is, however, that creditors are more likely to accept a plan if it promises to repay a considerable part of the debt.

To make even a partial repayment possible, the debtor has to readjust his or her lifestyle. The debtor is encouraged to reduce consumption, change shopping patterns, and increase his or her income (for example, by an increase in working hours or social benefits). Budgeting is often taught as part of the rehabilitation program, and the

⁶ The welfare state literature usually divides the welfare states into three regimes: (1) the Scandinavian welfare states, in which the state is the primary provider of services; (2) the Central European conservative welfare states, in which the services are often provided by private agencies; and (3) the liberal (Anglo-Saxon) welfare states, in which the state has a subsidiary role: see, for example, G. Esping-Andersen, *The Three Worlds of Welfare Capitalism* (Princeton, N.J.: Princeton University Press, 1990). The European welfare states are based on the notion of strong government and the responsibility of the state to guarantee basic services to its citizens. The institutionalization of debt counselling, as seen in Scandinavia, and private, state supported organizations, such as the regime in Germany, follow this distinction.

⁷ The German experience in debt counselling is described in detail in the works of Ulf Groth: see especially his influential textbook, U. Groth, *Schuldnerberatung*, (Frankfurt: Campus Verlag, 1990). In English, see U. Groth, "Debt Counselling in Germany" in G. Hörmann, ed., *Consumer Debt in Europe—The Birmingham Declaration: Proceedings of the Third European Conference on Overindebtedness* (Bremen: Universtät Bremen, 1993) at 102-05.

debtor is expected to keep records of all expenses. Also, the counsellor is expected to check the validity of claims, and to contact creditors about invalid claims. The counselling may include education about consumer credit. The focus of the guidance is not on alternative sources of credit, but rather on different means of paying off existing debts. The options, for example, may be to pay certain debts first (for example, those with high interest rates, or where a family member is acting as guarantor), paying all debts in full, or obtaining a consolidation loan. Sometimes the debtor can choose between submitting to a wage garnishment order and agreeing to a voluntary payment plan. A voluntary payment plan means lower enforcement costs, but to obtain the creditors' consent, the debtor often has to agree to a very low living standard during the period of the plan. Whatever the choice, it invariably means that the debtor has to live at a bare subsistence level for several years.

The new European consumer bankruptcy laws mention debt counselling, but do not usually explicitly require the debtor to receive counselling before filing for consumer bankruptcy. Instead, the legislation requires the debtor to have made a good faith proposal to the creditors to settle the debts before filing for bankruptcy. In practice, the legal requirements for an acceptable proposal are so complicated that the debtor needs professional assistance.

The content of the counselling is not defined in legislation or regulations. It is usually assumed that the counsellor will help the debtor to make a proposal, and to satisfy the other preconditions to a bankruptcy filing. In providing these services, the counsellor acts in a paralegal capacity to the debtor. The counsellor is expected to discuss the reasons for the consumer's debt problems, and how to avoid them in the future. He or she is expected to be familiar with other social services, and to refer the debtor to them where appropriate. Additionally, the counsellor is expected to train the debtor to acquire financial skills to enable him or her to fulfil the plan. Because all of the European consumer bankruptcy laws require the debtor to complete a five-year plan, and the debtor is only allowed to keep the minimum social security income level during the plan, the task of counselling is to assist the consumer to adjust his or her lifestyle to that level.

Where debt adjustment is regulated by law, the legislation will also define the debtor's repayment obligations. In the absence of such a legal regime, any debt rescheduling arrangements require the creditors' consent. The debtors are under pressure to pay more, and to accept longer payment plans and heavier monthly payments, in jurisdictions without a judicial adjustment law. Surprisingly, differences are also found within the same jurisdiction. In Finland, where a debt adjustment

law was passed in 1993,⁸ a recent study compared two counties with different local legal cultures.⁹ In one, most debtors filed for debt adjustment by the court. In the other, counselling agencies preferred debtor-negotiations leading to voluntarily accepted plans in accordance with the spirit of the law. The plans were longer in the latter jurisdiction and, unlike the plans in the other, often only granted a grace period for the repayment of the debts. Because the debtors were heavily indebted, there was a risk that the plans might fail and the debtors subsequently file for the legal adjustment.

In Europe, we expect to achieve prevention, rehabilitation, a change in lifestyle, and partial repayment of debt through counselling. In Canada, the rehabilitation is achieved through bankruptcy, even though the payment requirements in the Canadian consumer bankruptcy system have been increased. The debt counselling is still more future-oriented towards the development of better consumer and financial skills. To what extent, then, is emancipation from debt a goal in the Canadian counselling requirements? Should counselling decrease the debtor's dependency on credit, and can it do so effectively? In Europe, the answer seems to be yes: the debtor has to learn to live without credit just to fulfil the plan. However, the obligation is *imposed* upon the debtor, and it is hard to see it as emancipation from the cultural compulsion to consume excessively. With the limited availability of judicial debt adjustment under the European laws, the reality is often that the debtor has to learn how to survive at a subsistence level. In North America, consumer education aims to produce better consumers of credit.

In conclusion, debt counselling is on the rise everywhere. This is because of the increase in the volume of consumer credit and in the number of consumer debt problems. Counselling in general, however, is now seen to serve a wider role in the supply of social services. Counselling is offered as a cure to a wide range of social problems, such as domestic violence and other discords, maladjustment of young people, victims of crime, problems in parenting, substance abuse, etc. This enthusiasm for counselling coincides with the fact that welfare spending is being rolled back everywhere. While spending on benefits, public housing, education, and health care is decreasing, the state offers counselling as a palliative. Instead of seeking societal remedies to social problems, counselling tends to individualize the problems.

⁸ See *Laki yksityishenkilön velkajärjestelystä* (Consumer Debt Adjustment Act) 25.1.1993/57.

⁹ See J. Iivari & M. Heinonen, *Velkajärjestely vai sovinto?* (Debt adjustment in court or settlement in negotiation?) (Helsinki: Stakes, 1997).

