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Retrospective on the Canadian Consumer Bankruptcy System: 40 Years after the Tasse Report

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A RETROSPECTIVE ON THE CANADIAN CONSUMER BANKRUPTCY SYSTEM: 40 YEARS AFTER THE TASSÉ REPORT

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I. INTRODUCTION

Crispe v. Perrit (1744), Willes 467 at p. 468, 125 E.R. 1272:

A bankrupt is not considered as an unfortunate person, but as one who has been guilty of a crime; and therefore in the four first statutes concerning bankrupts he is frequently called an offender, and in all of them he is considered as one who has endeavoured by fraud or collusion to cheat and deceive his creditors and to prevent their recovering their just and honest debts.

These two stereotypes about bankrupts — the "unfortunate person" and the "offender" — have populated discussions of bankruptcy from the time of Henry viii, when the English Parliament enacted the first bankruptcy law in 1543.1 Even the 1706 Act, which first made the discharge available to English bankrupts, contained a section that made fraudulent bankruptcies a capital offence.2 In Canada throughout the 1870s, Parliament debated whether there should be a bankruptcy law at all. Notions

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1. An Act against Such Persons as do Make Bankrupts, 34 & 35 Hen. 8, c. 4 (1542).
of forgiveness competed unsuccessfully with the idea that all debtors had a moral obligation to repay all debts. In the end, Parliament repealed the Insolvent Act of 1875 in 1880, leaving Canada without any bankruptcy law of general application until 1919.

The story of bankruptcy reform over the 50-volume lifespan of the Canadian Business Law Journal is in no small part a story about these two warring visions of insolvent debtors. Given how little the Canadian consumer bankruptcy system has changed in those years, we would judge the war to have arrived at a stalemate.

We begin this short essay with an analysis of the 1970 Tassé Report — the first post-war policy review of the consumer bankruptcy system in Canada — and its continued relevance today. Next, we provide an account of the most notable change over the last half century — the vastly different number and demographic composition of debtors filing for consumer bankruptcy in Canada. We conclude by highlighting the key consumer bankruptcy reforms coming out of the most recent and long-awaited bankruptcy reform period and show how in many ways, the reforms (and lack of reforms in certain areas) take us back to a system that more closely resembles the one that a debtor would have encountered close to half a century ago. Further, we show that despite the changing demographics of consumer bankrupts and the enduring relevance of the Tassé Report nearly a half century later, the Canadian consumer bankruptcy system continues to resist fully realizing the goals of consumer rehabilitation and a fresh start, and provides little in the way of alternatives and accessibility for low-income debtors.


5. The Bankruptcy Act, S.C. 1919, c. 36.

II. THE TASSÉ REPORT

The plight of the consumer or wage-earner debtor is one of the most important problems that must be faced in the field of bankruptcy in Canada. To a certain extent, this group of debtors represents the social and economic casualties of our industrial and credit system...

1. Background and Mandate of the Study Committee

The origins of the Study Committee on Bankruptcy and Insolvency Legislation (Study Committee) 1970 Report, can be traced to June 19, 1960. On that date, more than 500 credit managers attended the Canadian Credit Men’s Trust Association’s 50th Anniversary Conference in Winnipeg. The theme of the conference was “Canada’s Economy — Credit Manager’s Challenge.” One item featured prominently on the agenda. The Minister of Justice, Davie Fulton, spoke to the delegates about possible reforms to the Bankruptcy Act. The topic would have been of particular importance to the credit managers in the audience given that many of them were employed by wholesale firms responsible for granting credit to retail outlets. According to the Winnipeg Free Press, these delegates controlled “the purse strings of Canada’s largest firms.”

Fulton announced that the Ministry of Justice would “launch an investigation into several sections of Canada’s Bankruptcy Act.” Fulton reminded the credit managers that there were many delays in the bankruptcy system that “made it possible for a debtor to avoid his commitments by fraudulent means.” He concluded: “These claims will be investigated, and if found to be substantiated, then a remedy, possibly on the lines of greater build-in protection for the creditor, will be found.” Fulton’s remarks reflected a growing

7. Canada, Study Committee on Bankruptcy and Insolvency Legislation, Bankruptcy and Insolvency: Report of the Study Committee on Bankruptcy and Insolvency Legislation (Ottawa, Information Canada, 1970) (Chair: Roger Tassé) [Tassé Report], at p. 54.
8. Ibid.
14. Ibid.
15. Ibid.
unease about the increasing number of fraudulent bankruptcies in the 1950s and early 1960s.\textsuperscript{16} This concern, coupled with the growing worry about the rising number of consumer bankruptcies, led the government to appoint the Tassè Committee in 1966.\textsuperscript{17} By the time the Study Committee began its work, it had received around 1,200 reform suggestions as a result of Fulton’s speech.\textsuperscript{18} Most submissions represented the credit, business or legal community.\textsuperscript{19}

The Study Committee consisted of only four members\textsuperscript{20} and was not meant to be a “committee of inquiry [or] investigation.” However, the Committee had been given broad terms of reference in that it was asked “to review and report on the bankruptcy and insolvency legislation of Canada.”\textsuperscript{21} Although it originally planned to recommend amendments to the Bankruptcy Act,\textsuperscript{22} the Committee realized that a new Act should be proposed because of the large number of proposed changes.\textsuperscript{23} Bill C-60,\textsuperscript{24} introduced in 1975, incorporated many of the recommendations of the \textit{Tassè Report}.\textsuperscript{25} When Bill C-60 lapsed, Parliament followed with five other bills in a nine-year period, but all failed to pass.\textsuperscript{26}

\textsuperscript{16} Tassè Report, supra, footnote 7, at p. 18; Ramsay, supra, footnote 6, at p. 403. As a result of these concerns, Parliament enacted amendments to the Bankruptcy Act in 1966 to widen the investigative powers of the Superintendent of Bankruptcy. See An Act to amend the Bankruptcy Act, S.C. 1966-67, c. 32.

\textsuperscript{17} Tassè Report, supra, footnote 7, at p. xi; \textit{Personal Insolvency Task Force Final Report} (Ottawa, The Office, 2002) (Y. Goldstein, Chair), at p. 5. Professor Ramsay notes that by 1971 the number of consumer bankruptcies had exceeded business bankruptcies. See Ramsay, supra, footnote 6, at p. 403.

\textsuperscript{18} Tassè Report, ibid.

\textsuperscript{19} Ibid., at pp. 169-170. Appendix A contains a partial list of organizations that made written submissions. Organizations included wholesale, retail and credit associations, Canadian Banker’s Association, Chambers of Commerce, Boards of Trade, and the Canadian Bar Association. Only one debtor organization, the Debtor’s Assistance Board of Alberta, made a submission to the Study Committee.

\textsuperscript{20} The members were Roger Tassè (Chairman); John D. Honsberger, Q.C.; Pierre Carignan, Q.C.; Raymond A. Landry (Secretary). Jacob Ziegel has dubbed this approach to bankruptcy reform as the “Wise Persons” model. Jacob Ziegel, “The Modernization of Canadian Bankruptcy Law in a Comparative Context” (1999), 4 Can. Bank. Rev. (4th) 151, at p. 185.

\textsuperscript{21} Ibid., at p. iii. See also James Baillie, “The Rewriting of Canadian Business Statutes” (1975-1976), 1 C.B.L.J. 242, at p. 245, note 3.

\textsuperscript{22} Tassè Report, supra, footnote 7, at p. xiii.

\textsuperscript{23} Ibid.

\textsuperscript{24} Bill C-60, An Act respecting bankruptcy and insolvency, 1st Sess., 30th Parl., 1975.

\textsuperscript{25} Ramsay, supra, footnote 6, at p. 404.

\textsuperscript{26} See Jacob Ziegel, “The Languishing Bankruptcy Bill” (1982-1983), 7 C.B.L.J. 249; Jacob Ziegel, “The Travails of Bill C-12” (1983-1984), 8 C.B.L.J. 374 [Ziegel,
2. The Failure of the Study Committee?

Many have suggested possible reasons for why the Tassé Report did not lead to permanent changes to bankruptcy legislation. The failure of the reform bills has been attributed to the "significant number of interest groups opposed to various aspects of the bankruptcy bills." Professor Ramsay's study demonstrates that "Bill C-60 threatened many influential groups" including banks, lawyers and accountants. Professor Ziegel, writing in the early 1980s, concluded that the Tassé Report was "written in a much more affluent and stable economic environment" and "what may have been an adequate approach in 1970 no longer serves as a sufficient blueprint for the problems of the 1980s." Although Professor Ziegel would later recognize "the great scholarship and intellectual integrity" of the Study Committee, the Tassé Report "ultimately had a limited impact because the group only included one insolvency practitioner, and because many of the report's recommendations were too abstract." Although the Tassé Report did not receive a warm welcome in 1970, one must ask whether the Study Committee identified any consumer bankruptcy issues that remain relevant and unaddressed 40 years later. Does the Tassé Report have a lasting legacy in 2010?

3. Legacy and Lessons from the Tassé Report

(a) Consumer Credit and Financial Failure

The Study Committee began by asking whether the principles underlying the Bankruptcy Act reflected "the needs of our present society."

We live in an affluent society. It is characterized by mass production, mass consumption . . . television . . . [and] the two and three car family . . . Accompanying this new affluence have been changing concepts of the morality of work and debt, new methods of doing business and financing . . . [and] the advent of the credit card economy . . . with the . . . 'buy now, pay later' . . . living.

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27. Ramsay, supra, footnote 6, at p. 405.
28. Ibid., at p. 404.
These fundamental changes to society "made much of our legislation obsolete." 32 The Study Committee noted that since World War II, "the explosive use of credit, particularly consumer credit" had "put the bankruptcy system out of balance." 33 In Canadian society, "the producer or manufacturing organizations make vast investments in ... advertising aimed at creating a demand to buy more." 34 Through the "endless stream of persuasion" of media and the mail, the consumer is "exhorted . . . to become indebted." 35 According to the Study Committee, "those who should most strongly resist this pressure are those who are the least educationally, intellectually and culturally prepared to withstand the pressure." 36 These broader concerns raised by the Study Committee are far more relevant today than they were in 1970.

The Study Committee's recognition of the link between the explosion in consumer credit and debt was significant for 1970. However, today new forms of consumer credit, such as payday loans and debit cards linked to overdraft facilities, have emerged along with the proliferation of new types of credit cards and home equity loans. 37 In short, the problem identified in 1970 has only worsened. Although not emphasized by the Tassé Committee, greater consumer debt need not be a problem if income and wealth are rising as well. For example, the median amount of consumer debt in the 2005 Survey of Financial Security was $44,500, an increase of 37.8% over the 1999 value of $32,300 (in 2005 dollars). However, the ratio of consumer debts to consumer assets increased by only 3.5% from $13.06 in debt for every $100 in assets to $13.52 per $100 in assets. 38 The greater problem today may be the distribution of consumer debt across income brackets if, as discussed below, lenders have increasingly focused on "marginal or submarginal risks."

32. Ibid., at p. 81.
33. Ibid., at p. 53.
34. Ibid., at p. 54.
35. Ibid., at p. 53.
36. Ibid., at p. 54.
(b) Social Impact of Consumer Credit

The Study Committee’s picture of the consequences of consumer credit still resonates today. Consumer debtors found themselves “in a trap from which they cannot escape.” “Bad fortune” often led to one “financial emergency following another.” These factors combined with mismanagement led debtors to “become deeper and more hopelessly in debt.”

At the heart of this debt cycle was a “personal tragedy” that had wider implications:

There is much personal tragedy for those who become hopelessly in debt. Each case involves a person who has failed, a person who has been defeated. The failure and defeat not only affect the debtor, but his wife, family, friends and acquaintances. Many children, to escape a harsh, bleak and degrading environment, marry young and become themselves a member of the chronic poor.

Quoting from the 1967 Senate and House of Commons Report on Consumer Credit, the Study Committee recognized the social cost of over-burdened debtors: “The tensions built up in harassed individuals and families frequently contribute to family breakdown, mental illness, crime and economic dependency.”

The Tassi Report’s conclusions point to a broader research agenda that moves beyond the specific study of consumer bankruptcies per se. The social implications of the growing burden on debtors resulting from consumer credit deserve even more scrutiny 40 years after the issuance of the Tassi Report.

(c) Debtor and Creditor Responsibility

Although the Study Committee recognized the plight of heavily indebted debtors, it did not refrain from pointing out that “some debtors, with loose moral standards or not personally affected by the stigma that...attaches to bankruptcy, may abuse credit facilities.”

In line with Minister Fulton’s concern in 1960, the Tassi Report acknowledged that fraudulent conduct on the part of debtors had to be addressed. However, debtor fraud was not the sole focus of the

40. Ibid., at p. 54.
41. Canada, Parliament, Special Joint Committee on Consumer Credit (Prices), Report on Consumer Credit of the Special Joint Committee of the Senate and the House of Commons on Consumer Credit and Cost of Living (Ottawa, Queen’s Printer, 1967) (Chairs: D.A. Kroll and R. Basford), at p. 58.
42. Tassi Report, supra, footnote 7, at p. 53.
43. Ibid., at p. 60.
Tassé Report. The Study Committee also recognized that “[a]s there are good and bad debtors, so are there good and bad creditors.”\textsuperscript{44} According to the Study Committee, the traditional maxim of equal treatment of all unsecured creditors needed re-examination.\textsuperscript{45} While the Tassé Report never fully explains under what circumstances the equitable treatment of creditors would be disturbed, it nevertheless condemned the change in lending transactions. Traditionally, lenders would advance funds:

after a careful consideration of the capacity of the borrower or purchaser to fulfill his obligation. This is often not the case. Some producers may choose to operate closer to full capacity in order to lower their costs and, to dispose of their production, may deliberately extend credit to the marginal or sub-marginal risks. The same may be true of wholesalers, retailers and finance institutions who may attempt to increase their volume of business . . . \textsuperscript{46}

Today, the growth of payday lending and the fallout from the U.S. subprime mortgage crisis demonstrate that there has been a continued growth in the deliberate extension of credit to “marginal or sub-marginal”\textsuperscript{47} risks (i.e., people who may not be able to repay). However, modern lending practices have encompassed a new phenomenon. Targeting low-income debtors has become a significant part of the credit industry. Even though the debtor may not be able to repay the debt, the fees, penalties and interest charges make this category of debtor a profitable one and a good risk for the lender to assume.\textsuperscript{48} The development of credit scoring techniques has permitted credit card issuers to “target consumers who are likely to generate high profits through late payments and borrowing on a card.”\textsuperscript{49} Further, the Study Committee’s concern that some creditors extended credit without careful consideration has given rise to the notion today that creditors should be held accountable for irresponsible lending. For example, Professor Ziegel has proposed that where there is an improvident extension of

\textsuperscript{44} Ibid., at p. 54.
\textsuperscript{45} Ibid., at p. 54.
\textsuperscript{46} Ibid., at p. 53 (Emphasis added).
\textsuperscript{47} Ibid., at p. 53.
\textsuperscript{48} Ziegel, supra, footnote 37, at p. 373. See also Ronald J. Mann, “Patterns of Credit Card Use Among Low- and Moderate-Income Households,” in Rebecca M. Blank and Michael S. Barr, eds., Insufficient Funds: Savings, Assets, Credit and Banking Among Low-Income Households (New York, Russel Sage Foundation, 2009), p. 257.
\textsuperscript{49} Iain Ramsay and Toni Williams, “The Crash that Launched a Thousand Fixes: Regulation of Consumer Credit After the Lending Revolution and the Credit Crunch,” working paper (Kent Law School, University of Kent, 2009), at p. 9, online: SSRN <http://ssrn.com/abstract=1474036>.
credit, the trustee in bankruptcy should be given the power to deny these unconscionable creditor claims under the Bankruptcy and Insolvency Act\(^5\) (BIA). Such an unconscionable claim would be defined in part as where the “creditor knew, or should reasonably have anticipated, that the debtor would not be able to meet . . . the debtor’s obligations under the credit contract.”\(^5\) However, the concept of an improvident extension of credit and an unconscionable claim in the bankruptcy would have to deal with the emergence of securitization of various debt obligations. The ultimate holder of the debt in the bankruptcy, for example, may be a pension fund holding a package of mortgage or credit card accounts. As the last holder of the debt, it would have had nothing to with the originating loan. The improvident extension of credit would have been made much earlier in the chain of transactions by the originator.

(d) Fresh Start

The Study Committee acknowledged that the objective of bankruptcy law should be to “rehabilitate” the debtor and “give him an opportunity to make a fresh economic start in life.”\(^5\) This objective has been a significant feature of the legislation and has long been recognized by the judicial branch.\(^5\) However, an important aspect of the fresh start is ready access to the bankruptcy regime. The Study Committee concluded that relief for the consumer debtor was “not effective or illusory . . . [B]ankruptcy is financially beyond the reach of those who most need it.”\(^5\) According to the Study Committee, bankruptcy “should be equally available, as a last resort to financial disaster, to all debtors whether in business or not.”\(^5\)

\(^51\). Ziegel, supra, footnote 37, at p. 392.
\(^52\). Tassé Report, supra, footnote 7, at p. 87.
\(^54\). Tassé Report, supra, footnote 7, at pp. 54 and 65.
\(^55\). Ibid., at p. 86.
A recent study by Professors Ben-Ishai and Saul Schwartz demonstrates that affordable access to a bankruptcy system may still remain a significant problem.  

In recent years, the rehabilitative purpose of bankruptcy law has been further eroded by statutory amendments. Legislative changes to the BIA have moved the law away from rehabilitation as the underlying theory for the discharge. Straight bankruptcy followed by a discharge and debtor rehabilitation has been made more difficult. Debtors are required to meet surplus income requirements and some debtors with surplus income may have to remain bankrupt for a longer period. Stephanie Ben-Ishai suggested that the 1997 amendments “signalled a return to the ‘debtor deviant’ construct” and the more recent 2005 and 2007 amendments “hold the potential to entrench this construct in Canada’s consumer bankruptcy system.”

Arguably, one of the most important legacies of the Tasse Report was its proposal to introduce consumer proposals as an alternative to bankruptcy. A “watered down” version of that recommendation ultimately appeared in the BIA in 1992. By 1997, accessibility to the discharge and a fresh start became inherently linked to proposals. Under the BIA, the court may refuse, suspend or grant a conditional discharge when “the bankrupt, if the bankrupt could have made a viable proposal, chose bankruptcy rather than a proposal to creditors as the means to resolve the indebtedness.” No such recommendation appeared in the Tasse Report as no doubt the Study Committee would have considered such a provision to undermine the concept of a fresh start.

The 40 years that have elapsed since the release of the report demonstrate that many of the key findings of the Study Committee continue to remain relevant for consumer debtors. Indeed, many of


59. Ramsay, supra, footnote 6, at p. 407 (“The introduction of consumer proposals reflected the historical legacy of the Tassé Report.”).

60. Tassé Report, supra, footnote 7, at p. 91.

61. Ramsay, supra, footnote 6, at p. 408. Ramsay notes that by 1992 “a consumer proposal did not affect the rights of secured creditors.”

62. BIA, s. 173(n).
the problems for debtors identified in 1970 have been exacerbated by the unrelenting growth of consumer credit. Further, the prospects for a fresh start, a key component of bankruptcy law identified in the Report, have been weakened. Although the Study Committee did not provide any empirical evidence or interviews with bankrupts to support its conclusions, the Report provides us with a benchmark in time against which to measure the current plight of consumer bankrupts. The empirical story is the subject of Part III.

III. THE CONSUMER BANKRUPT 40 YEARS LATER: AN EMPIRICAL ACCOUNT

In the early 1970s, shortly after the Tassé Report was released, there were fewer than 5,000 consumer bankruptcies and no consumer proposals. In the 12-month period ending April 30, 2010, there were 109,924 consumer bankruptcies and another 38,717 consumer proposals.63

One reality of contemporary societies is that debt is an integral and accepted feature of the economic lives of consumers. Another reality is that many consumers cannot or do not repay their debts as they come due. The simple division of insolvent debtors into the “honest but unfortunate” on the one hand and the “deviant” on the other does not describe such a complex reality. An “honest but unfortunate” debtor might not have been as careful as she should have been while her life was going well and ended up with large outstanding debts when adverse life events occurred. The “deviant” bankrupt might have been driven to strategic behaviour only after adverse life events set her on a downward spiral.

Nonetheless, one aspect of the power of such simple either-or stories is their resistance to empirical investigation. Such empirical investigations try to ascertain how actual bankruptcy cases are distributed along the spectrum from “honest but unfortunate” to “deviant.” The research can be qualitative, collecting the stories of those who have filed for bankruptcy, or quantitative, seeking to infer

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the nature of the bankrupts from economic and demographic information. The ultimate causes of any bankruptcy, however, cannot be determined without ambiguity. For example, is the ultimate cause the fact of borrowing in the first place, when perhaps the debtor might have managed without borrowing? Is the ultimate cause “job loss” when the debtor had run up large debts prior to losing her job? Is the ultimate cause “mismanagement” when expenses were incurred to give children opportunities similar to their peers? Recognizing the difficulty of arriving at a true picture, we can review the empirical investigations of Canadian bankrupts.

The last comprehensive, quantitative examination of Canadian bankrupts dates back to 1997 when, on behalf of the federal Office of Consumer Affairs, Professors Saul Schwartz and Leigh Anderson conducted a survey of about 1,000 debtors filing for bankruptcy.64 Twenty years earlier, in 1977, Brighton and Connidis had also studied a sample of bankrupts.65 For our purposes, the relevance of the Schwartz and Anderson survey is in one of its conclusions:

... the economic situation of those who sought bankruptcy protection in 1997 was quite weak. This is evidence against arguments that the bankruptcy laws are widely used by economically healthy individuals who simply want to avoid paying legitimate debts.66

Overall, the Schwartz and Anderson survey revealed that the economic situation of debtors filing for bankruptcy in 1997 was similar to that of debtors filing in 1977, even though their numbers were far larger. This is not to say that the samples were similar demographically. The proportion of women filing for bankruptcy in 1997, for example, was far higher than it had been in 1977, likely reflecting more equal access to credit and higher divorce rates.

Looking at the debtors’ reports of their 1996 pre-tax annual income, their occupation and their receipt of government transfers, Schwartz summarized the situation by concluding that “... it seems that individuals seeking bankruptcy protection in 1997 were not much different from those who declared bankruptcy in 1977. They were in severe economic straits, with low incomes, poor job prospects, and a history of social assistance or unemployment insurance receipt.”67

65. J.W. Brighton and J.A. Connidis, Consumer Bankrupts in Canada (Ottawa, Consumer and Corporate Affairs Canada, 1982).
66. Ibid., at p. 85.
67. Ibid., at p. 107. The Schwartz and Anderson survey had two sources of income
A more recent analysis of Canadian bankruptcy data, by Redish, Sarra and Schabas (2006), is limited to a subset of those filing for bankruptcy who were age 55 or older. Redish et al. note that "...15.3% of all individual bankrupts in Canada were over age 55 in 2003. In 1993 this figure was 6.9%." As they point out, the rise in the proportion of older people filing for bankruptcy is counterintuitive because one would think that spending patterns and lifestyles are determined well before age 55, so that large changes are unlikely to occur. Redish et al. went into their study thinking that perhaps "new temptations," in the form of more accessible gambling opportunities or the rise of television (and online) shopping might have had an influence. Or, they speculated, there might have been a rise in the number of adult children needing significant amounts of financial help from their parents. However, none of these potential causes of bankruptcy showed up in large numbers in their analysis and the causes that did appear were quite similar to those characterizing the bankruptcies of younger people. The one exception was the understandably greater importance of "medical reasons" as a cause of bankruptcy.

Although the U.S. and Canadian bankruptcy laws are different in important ways, the similarity in the two economies might suggest that American bankrupts are similar to Canadian bankrupts. The Consumer Bankruptcy Project in the United States has completed three profiles of American bankrupts, in 1991, 2001 and 2007. A detailed comparison of the 1997 Schwartz and Anderson data and the Consumer Bankruptcy Project data is beyond the scope of this paper but, generally speaking, the profiles are similar — in both countries, bankrupts are typically those who are working and who have relatively low income.

Interestingly, the distribution of income among bankrupts in the United States was about the same in 2007 as it had been in 2001.

Information. The first was derived from the bankrupts' statements of affairs and represents "net monthly income" at the time of filing. The second was derived from the survey that accompanied the statement of affairs and represents annual pre-tax household income in 1996, the year before the bankruptcy filings.


69. Ibid., at p. 9.

70. For a list of papers associated with the Consumer Bankruptcy Project, see online: Bankruptcy Data Project at Harvard University <http://bdp.law.harvard.edu/fellows.cfm>.
Because the 2005 U.S. bankruptcy reform was driven by a stated desire to discourage high-income debtors from filing, one might have thought that the median income of filers would have fallen from 2001 to 2007. The number of American bankruptcies dropped considerably between 2005 and 2007, but the median income of the bankrupts did not, suggesting that the reform discouraged bankruptcies across the spectrum of incomes. As will be shown in the next section, the recent Canadian bankruptcy reform was also aimed at discouraging “can pay” debtors from filing for bankruptcy and receiving a quick discharge. It would be useful to undertake a follow-up study of Canadian bankrupts to see if the changes had the desired effects; the 1997 Schwartz and Anderson study is now quite dated and a newer profile would be of great value.

IV. THE 2009 REFORMS: A STEP BACK?

1. Middle-Class Debtors and the Deviant Debtor Construct

A key component of consumer bankruptcy in Canada has, since 1919, been the non-waivable or mandatory consumer bankruptcy discharge. As recognized in the Tassi Report, bankruptcy’s non-waivable discharge has in recent times been regarded as part of economic rehabilitation of the debtor, which is equated with a “fresh start.” However, the amendments to consumer bankruptcy legislation since the Tassi Report have for the most part moved away from the fresh start goal and understanding of consumer bankruptcy. A clear example are the 1997 amendments that attempted to effect a move from rehabilitation of the debtor to asking debtors to rehabilitate their debts by making payments out of surplus income. The 1997 amendments required trustees to assess whether bankrupts could have made a viable consumer proposal and whether they co-operated with the trustee by meeting any surplus income requirements.

Despite the underlying assumption that many bankrupts have an ability to make repayments to creditors, in practice, these amendments had a limited impact on the majority of bankrupts who could not make a proposal because they did not have surplus

72. This section summarizes in part sections from Chapters 13 and 14 of Ben-Ishai and Duggan, supra, footnote 53.
73. Telfer, supra, footnote 57.
74. Ibid.
income. As discussed earlier, while the 1997 BIA amendments had limited practical impact, they signalled a return to the “deviant debtor” construct, which positions bankruptcy law as a response to deviant behaviour. The 2009 reforms further entrench this construct in Canada’s consumer bankruptcy system and also establish the “middle class” user of the system. The 2009 consumer bankruptcy reforms largely respond to the needs and problems experienced by the existing users of the system — that is the middle-class or close-to-middle-class debtor and her creditors — and on this basis reflect and expand on the status quo. Three examples illustrate this point: the exclusion of RRSPs and RRIFS from property of the bankrupt, the longer bankruptcy periods for surplus income earners, and the treatment of bankrupts with high income tax debt.

(a) RRSPs and RRIFS

The protection of RRSPs and RRIFS (tax-sheltered retirement savings plans) provided by provincial law is restored by the 2009 reforms, such that they do not become property of the bankrupt divisible among his or her creditors. Where RRSPs and RRIFS are not protected by provincial law, they will be afforded protection under the BIA. An exception is provided for any contributions made in the 12 months preceding bankruptcy. Such contributions are not excluded from property of the bankrupt divisible among his or her creditors.

This reform is based on the reality that Canadians are increasingly being called upon to provide for their own retirement, as private pensions are less often offered by employers and the government provides for older Canadians only in a limited way. Further, as the earlier section demonstrated, older Canadians are increasingly represented among the bankrupt population. Accordingly, in order for the bankruptcy system to truly provide a fresh start, and to ensure that older Canadians do not find themselves right back in the bankruptcy system, this reform attempts to provide some protection for debtors’ retirement savings.

One limitation of this reform is that many Canadians have neither RRSPs nor RRIFS. Of those that do, relatively few have employer-
provided pensions. However, the majority of over-indebted Canadians have neither retirement plans nor retirement savings. Accordingly, these reforms provide little assistance to them.

(b) Longer Bankruptcy Periods

For most Canadian debtors, bankruptcy is a simple nine-month process that can be handled electronically by a bankruptcy trustee. When a consumer assigns herself into bankruptcy, there is an automatic stay that stops collection efforts (such as telephone calls and letters demanding repayment) by her unsecured creditors. Following an assignment into bankruptcy, all of the bankrupt's non-exempt property vests in the bankruptcy trustee to be sold for the benefit of her creditors. If the bankrupt earns an income above the surplus income threshold provided for in the Office of the Superintendent in Bankruptcy Directives, she will be required to make surplus income payments to the trustee. Following the 2009 amendments, bankrupts with surplus income are now required to wait for the expiration of a 21-month period before becoming eligible for an automatic discharge. During this period they must continue to make surplus income payments to the bankruptcy trustee. Second-time bankrupts are entitled to an automatic discharge following the expiration of a 24-month period. If a second-time bankrupt has surplus income, she must wait for the expiration of a 36-month period. The second time bankrupt must make surplus income payments to the trustee during this period.

In practice, many Canadian consumer bankrupts have little or no non-exempt property to be distributed among their unsecured creditors and earn incomes below the surplus income threshold. Accordingly, the reforms to the automatic discharge will only affect a small number of debtors. The reforms seek to increase the availability of the automatic discharge (to second time bankrupts), while at the same time increasing for some debtors the period of time before eligibility for an automatic discharge.

The Canadian reforms stand in contrast to the most recent American reforms — a central feature of which was means-testing. Means-testing requires all debtors to calculate their estimated ability to pay (according to complex formulae) and to file these calculations for approval.

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78. *BIA*, at s.168.1 and Forms 65, 82 and 84 and Directive No.11R2.
with their Chapter 7\textsuperscript{83} petitions.\textsuperscript{84} A failure to do so results in automatic dismissal of their petition. In contrast, the Canadian approach is to focus on means-measurement. That is, for liquidation bankruptcies, the bankruptcy trustee, on the basis of regulations set by the Office of the Superintendent in Bankruptcy, sets the amount debtors are required to pay (if any) during the bankruptcy period.\textsuperscript{85}

For debtors who are required to pay under the current means-measurement tests — that is, those who are required to make surplus income payments — the reforms will increase the period of repayment. The reforms do not seek to introduce means-testing into the Canadian system. Means-testing and means-measuring serve different purposes under the American and Canadian regimes. Under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA),\textsuperscript{86} the purpose of means-testing is to deny debtors relief if they fail the test, while in Canada the object of means-measurement is to ensure that the surplus income received by the bankrupt during the bankruptcy period is made available to the estate. Paradoxically, the Canadian means-measurement approach is more effective at putting into action the key objective set out by the proponents of means-testing in the United States than the United States system itself. That is, means-measurement focuses specifically on "can pay" or so-called "undeserving" debtors and imposes a tax on them for the privilege of escaping their commitments. At the same time, because Canadian debtors with surplus income are still able to move through the bankruptcy process, they are not directly prevented from accessing the fresh start offered by a liquidation bankruptcy.

With respect to the claim that means-testing, by increasing the likelihood of repayment of debts, decreases the cost of borrowing, it is questionable whether means-measurement will achieve this objective. Even though surplus payments have historically had only a trivial impact on disbursements to creditors, this may change with the introduction of the longer payment. In addition, by imposing a longer payment period for debtors with surplus income, it is likely that a larger number will turn to consumer proposals. At the same time, the greater flexibility offered by the current Canadian approach allows debtors with a modest surplus income to make payments for a relatively short period, and to earn their discharge

\textsuperscript{83} Bankruptcy Code, 11 U.S.C. § 101 \textit{et seq.} (Bankruptcy), Chapter 7.

\textsuperscript{84} See Stephanie Ben-Ishai, "Means Testing," in Ben-Ishai and Duggan, supra, footnote 53, p. 343.

\textsuperscript{85} Telfer, supra, footnote 57.

without forcing them into making unrealistic consumer proposals. As the longer payment periods apply equally to debtors regardless of the amount of their surplus payments, debtors with low income may turn to consumer proposals, which they are unable to complete successfully. It will be important to monitor whether the number of consumer proposals increases with the enactment of the reforms, and the success rate of these proposals.

A key issue in the American consideration of means-testing — the use of discretion — is also at the heart of the Canadian reforms. Similar to the American concern with the use of judicial discretion and the resulting lack of uniformity, a concern existed with respect to the trustee’s use of discretion in extending the surplus payment period. The *Personal Insolvency Task Force Report* (PITF) states that “[t]he discretion afforded to trustees allows debtors to ‘shop’ for a trustee who will not require any additional payments,” creating a situation in which the imposition of shorter payment periods would result in a personal gain for trustees. The use of bright line rules for the repayment period minimizes the ability of debtors to choose trustees on the basis of their position on repayment periods and introduces a more standardized approach. At the same time, there remains a degree of discretion left to trustees in applying the directive to the debtor’s specific financial situation, determining if surplus payments are required and, if so, in what amount. Arguably, this aspect of the Canadian system retains the “human side of the law” that has been lost in the American approach to bright line means-testing. In addition, a comprehensive mediation process is in place to address situations where the debtor and the trustee cannot agree. Of course, to the extent that some level of discretion is preserved for trustees, there remains anxiety around uniformity with regard to surplus payment amounts.

(c) High Income Tax Debtors

For bankrupts with more than $200,000 (including principal, interest and penalties) in personal income tax debt (federal and/or provincial), representing 75% or more of their total unsecured proven claims, an application for discharge is now required by the 2009 reforms. For first and second-time bankrupts, such an application may be made when the bankrupt would have been

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88. *BIA*, at s. 172.1.
eligible for an automatic discharge.\textsuperscript{89} For all other bankrupts, the hearing may not be heard until 36 months have expired.\textsuperscript{90}

The court may refuse the discharge, suspend the discharge, or provide a conditional discharge. The burden is on the bankrupt to justify the relief requested and the court is directed to take into account:

(i) The bankrupt's circumstances at the time the personal income tax debt was incurred;
(ii) the efforts made by the bankrupt to pay the personal income tax;
(iii) whether the bankrupt paid other debts while failing to make reasonable efforts to pay the personal income tax debt; and
(iv) the bankrupt's financial prospects for the future.

A discharge order may be modified after one year.\textsuperscript{91}

The reforms to the treatment of one form of government debt — income tax debt — stand in contrast with the reforms to another form of government debt — government-funded student loan debt.\textsuperscript{92} Since 1998, government-funded student loans incurred within the 10-year period prior to the bankruptcy date have formed an exception to discharge. The 2009 reforms shorten this period and modify the process for discharging these loans.

In general, the reforms soften the treatment of student loan debt in some respects, but leave the basic scheme untouched. The 10-year "waiting period" has been reduced to seven years. In addition, bankrupts may make an application, after five years, for relief on hardship grounds.\textsuperscript{93} Moreover, bankrupts who have non-dischargeable student loans at the time of bankruptcy (i.e., those who were in school less than seven years prior to the date of bankruptcy) are entitled to make an application for discharge of these student loans after the seven years have elapsed. However, debtors must make a costly discharge or relief application in these cases and may have limited access to assistance in handling the application. Contrary to the Senate Report\textsuperscript{94} and PITF Report

\textsuperscript{89} Ibid.
\textsuperscript{90} Ibid.
\textsuperscript{91} Ibid.
\textsuperscript{92} By "government-funded student loans", we mean the loans that are defined in s. 178(1)g of the BIA:
\textsuperscript{93} BIA, s. 178.
\textsuperscript{94} Canada, Standing Senate Committee on Banking, Trade and Commerce, Debtors
recommendations, there is no provision for partial relief; and most importantly, there is no empirically-based rationale for excepting student loans from the discharge. In addition, the statute provides little direction to the courts in the exercise of their discretion in hardship applications.

The introduction of a special discharge procedure for tax debts meets one criticism of the student loan provisions: previously government-funded student loans were the only form of government debt excepted from the discharge. Now tax debts will also be excepted in certain circumstances. However, this is where the consistency ends. A student loan debtor will be unable to apply for discharge of the debt until at least five years after ceasing to be a student, whereas a tax debtor can apply for a discharge as early as nine months after filing for bankruptcy. In addition, the statute provides a specific list of factors to be taken into account at the tax debtor's discharge hearing. Furthermore, while an absolute discharge cannot be granted, a suspended or conditional discharge may be granted with some measure of partial relief. Unlike the majority of student loan debtors, many tax debtors that fit within these provisions will have the resources to engage counsel to represent them at the discharge hearing and assist them in obtaining partial relief.

Taken together, the treatment of debts owed to the government push at the rehabilitation model of consumer bankruptcy without a clear or principled underpinning. Historically, the small list of exceptions to the discharge in bankruptcy was consistent with the position that where the bankrupt acts in good faith, she is entitled to the discharge. This is the case even where the bankruptcy is the result of poor financial decisions. Accordingly, by excepting student loan debt and tax debt, the legislature characterizes bankrupts with this type of debt as deviant and dishonest. Student loan debtors are the most deviant, while tax debtors deserve a symbolic slap on the wrist. By contrast, other bankrupts, such as those who owe fines imposed by a court and damage awards arising from civil proceedings other than for bodily harm, sexual assault, or wrongful death, remain entitled to have those debts discharged. In addition, both measures

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run counter to the bankruptcy policy, in place since 1992, that the Crown should not be afforded special treatment in bankruptcy.95

2. Missed Opportunities

Arguably, making bankruptcy harder for a small group of high-income bankrupts does not detract from the possibility of realizing the fresh start objective underlying the Canadian bankruptcy system. However, the reforms are a further example of a missed opportunity to take up the challenge articulated in the Tassé Report — one adopted in countries around the world — to provide accessible bankruptcy options to low-income and no-income debtors. Two examples illustrate this point — the continued use of registrars and the lack of a public or low-cost bankruptcy option.

(a) Court Hearings

Most consumer bankruptcy cases in Canada result in automatic discharge and there is no court hearing. Nevertheless, there are still a substantial number of debtors involved in hearings. The reforms remove the need for a court hearing in the case of second-time bankrupts, impose a hearing on tax debtors, create an incentive and a more accessible vehicle for creditors to oppose a discharge (which will result in a discharge hearing), and retain the possibility for an application for relief from the exception to discharge for student loans. It is unclear whether the reforms will result in a net increase or decrease in the number of court hearings.

In any event, in each of these instances, the court is instructed to use its judicial discretion in different ways, and different controls operate in the discharge process without clear policy rationales. For example, in the case of student loan debt, the legislation gives the court very little guidance in the exercise of its discretion to grant relief. By contrast, in the case of tax debt, the new provisions set out a detailed list of factors the court must consider in ruling on an application for a discharge. For oppositions to discharge in all other instances, the court is given a list of factors on the basis of which it may refuse or suspend the discharge or impose conditions. This list differs from the list provided for tax debtors.

The reforms overlook a key issue, namely the role and form that dispute resolution should take with respect to the consumer bankruptcy discharge. More particularly, should the hearing

95. Stephanie Ben-Ishai, "Technically the King Can Do Wrong in Reorganizing Insolvent Corporations: Evidence from Canada" (2004), 13 Intl. Insol. Rev. 115.
continue to play a role in the discharge process, and if so, what principles should guide the process?

(b) Low-Cost Bankruptcy Option

The discussion in the earlier section on means-measuring versus means-testing offered a positive perspective on how the reforms contribute to a fresh start for high-income debtors. The focus was on debtors who are currently able to access the bankruptcy system and how this will change with the enactment of the reforms. Unlike the American system, the Canadian surplus payment requirements do not impose additional front-end administrative and financial burdens that in themselves will prevent the poorest of potential bankrupts from accessing the bankruptcy system. However, a number of obstacles hinder access to the bankruptcy process for the poorest debtors. In particular, such debtors will have difficulty paying the trustee in bankruptcy approximately $1,800 in costs associated with the administration of a bankruptcy. The reforms go some way to address this concern by providing a mechanism for the bankrupt to reach an agreement with the trustee to continue paying for bankruptcy services after the bankruptcy period. However, this agreement itself stands in the way of a “true” fresh start. The 2009 reforms represent yet another missed opportunity to establish a low-cost bankruptcy option for poor debtors.

V. CONCLUSION: LOOKING FORWARD TO 2050

The 2009 Canadian bankruptcy law reforms discussed in this article, while offering some additional support to middle and high-income debtors, by way of enabling them to pay a surplus for a period and still have access to a fresh start, do not go far enough to address the needs of low-income debtors — the most vulnerable debtor group. Low-income debtors, in contrast to their wealthier counterparts, face many obstacles when attempting to engage with the bankruptcy system, the first of which is the $1,800 fee required to initiate the process. Other difficulties that low-income debtors face are exacerbated by the shift in attitude that underpins the recent law reform: debtors have come to be seen less as “unfortunates” and more as “deviants” in need of punishment. This has been a constant theme in the history of bankruptcy law reform. In our current culture, where credit is easily and widely available, this change in attitude puts low-income debtors at a double disadvantage: less able
than their more affluent and educated peers to avoid bad credit, they become punching bags for the bankruptcy system in general. Though actual prison sentences are no longer doled out to poor debtors, the bankruptcy and credit system currently in existence has a tendency to metaphorically imprison low-income individuals. A classic illustration of this would be how agreements to pay the trustee’s fees after the bankruptcy period ends directly impede the bankrupt from acquiring a true “fresh start.”

The 2009 law reforms also run counter to previously accepted concepts, the most important of which is that unsecured creditors, including the Crown, are to be treated equally. The Crown’s preferential treatment can be seen in the way that tax debts are now being treated. Obligations to make partial payments of tax debts constitute the “slap on the wrist” to debtors; these same obligations to pay also run counter to the availability of complete discharge that is present with other debts. The treatment of student loans further bolsters our argument that the Crown continues to be accorded special treatment; the waiting time for discharge of student debts puts a heavier obligation on bankrupts to pay. Perhaps the youth of former student debtors contributes to their quite obviously perceived deviance! (Here, there is an effect and cause relationship between the preferential treatment being accorded to the Crown and the shift in ideology (or the lobbying power of large creditors) that forms the basis for the legislation.)

It is obvious to the authors of this article that though there were positive elements to the 2009 reforms, much needs to occur in order to create a bankruptcy system that is effective and fair, from both the perspective of debtors and creditors. We therefore look forward to future reforms, and particularly to those targeted at improving the situation and options of low-income bankrupts. For poor bankrupts have become the current “social and economic casualties of our industrial and credit system.”

97. Tassé Report, supra, footnote 7, at p. 54.