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Economic Rehabilitation: Understanding the Growth in Consumer Proposals under Canadian Insolvency Legislation

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Economic Rehabilitation: Understanding the Growth in Consumer Proposals under Canadian Insolvency Legislation

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Abstract

Economic rehabilitation is the notion underlying Canada's *Bankruptcy and Insolvency Act (BIA),* providing consumer debtors with an opportunity for a "fresh start" through the mechanism of bankruptcy or making a proposal to their creditors for payment of their debts on terms that allow them to rehabilitate their financial status. This article undertakes a comparison of consumer proposals and consumer bankruptcies, examining 5,773 individual insolvencies in the past two years, with a view to discerning choices by individual insolvent debtors of insolvency proceeding. It compares causes of financial distress, income levels, quantum of debt and the assets of those filing proposals or bankruptcies. The data indicate that overextension of credit is a primary cause of insolvency, being 20% to 24% the primary cause across all cohorts. Home mortgage liability is significant for the Division I proposal debtors, but less significant for bankrupts, many of whom do not have equity in homes. Credit card debt is a serious problem across all groups. Credit card debt, unlike fixed loans such as mortgages, can quickly escalate, is owed at much higher interest rates that can rapidly compound financial distress, and the lack of a defined payment plan, other than a minimum payment, means that consumer debtors are not encouraged to pay these debts first, leading to longer term financial distress. Yet, to date, insolvency policy does not really factor the nature of this debt into policy development. Job loss and seasonal employment together are a significant cause of insolvency across Division II consumer proposal debtors (26%), Division II business proposal debtors (33%), and bankrupts (28%), but less so for Division I proposal debtors (16%). These data suggest that there are broader economic and social challenges that need to be addressed, as financial distress is often beyond the control of the individual debtor. To date, there is little linkage in Canada between economic stimulus and employment policy development and insolvency law policy development. Medical reasons are also a significant cause for Division II business proposal debtors (15%) and bankruptcy (11%), compared with the other cohorts. However, it is uncertain whether medical bills and lack of coverage, or medical problems resulting in inability to earn sufficient income are the real source of the financial distress. Equally, medical debt may be masked if consumer debtors have paid for medical bills by credit card on exit from hospital or particular outpatient services, as is the normal practice in some regions. The study offers both observations on the data and recommendations for future research and policy development.

I. Introduction

Economic rehabilitation is the notion underlying Canada's bankruptcy and insolvency system. As with many jurisdictions, the *Bankruptcy and Insolvency Act (BIA)* provides consumer debtors with an opportunity for a "fresh start" through the mechanism of bankruptcy or through the mechanism of making a proposal to their creditors for payment of their debts, but on terms that allow them to rehabilitate their financial status.[2] This paper examines the insolvency of individuals in Canada;

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[2] *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended (*BIA*).

specifically, it undertakes a comparison of consumer proposals and consumer bankruptcies under the *BIA*.

There has been an increase in the number of consumer proposals in recent years, with little public understanding of what may be driving the shift from bankruptcy to proposals. The 1997 amendments to the *BIA* were aimed in part at encouraging proposals as an alternative mechanism for individual debtors to address their financial distress. While the number of proposals filed has increased, the number of failed proposals has also increased; yet the failure rate has not resulted in a lessening of the numbers filed. The reasons underlying this trend are not immediately evident. It could be the greater facility with which proposals can be filed. There has also been some speculation that the high costs of trustee fees, surplus income payments and/or other recent policy measures have driven the change. This research project sought to establish an empirical basis for the growth in filing of proposal proceedings, including an investigation of what factors are drivers in the shift to proposals and what may serve as a deterrent to this option. The objective was to try to discern the impact of particular policy choices on consumers' decisions to undertake a proposal instead of bankruptcy as the resolution to their financial distress.

This study undertakes an analysis of 5,773 individual insolvencies in the past two years, with a view to discerning choices by individual insolvent debtors of insolvency proceeding. It undertakes a comparison of the causes of financial distress and income levels of debtors filing proposals in comparison with a representative sample of consumer bankrupts, to determine whether the cause of financial distress is a determinant of choice of proceeding. The study also examines the type and quantum of debt and the assets of those filing proposals or bankruptcies, in order to discern patterns in consumer financial distress. One working hypothesis of the study was that consumers that have assets to protect, particularly family homes, are more likely to opt for a proposal, in order to try to protect those assets from seizure and liquidation. The paper explores whether the policy choices in Canada offer effective options for consumer debtors at a time of particular vulnerability. The project was funded with the support of the Research Initiative of the Canadian Office of the Superintendent of Bankruptcy (OSB).

It merits note at the outset that there is an indeterminate number of consumer debtors in Canada that do not access formal insolvency proceedings at all. The data on these individuals are almost non-existent in Canada, and they are not included in this study. However, it is important to be mindful of the fact that there may be significant market and regulatory reasons that drive financially distressed consumer debtors to opt for neither a bankruptcy application nor a proposal. This group of debtors requires further scholarly research and public policy consideration.

Part II of this paper explains the methodology of the study, including the limitations of such data analysis. Part III sets a context for the study. Part IV sets out the legislative framework, providing a brief overview of the options for economic rehabilitation for consumer debtors, including Division II consumer proposals, Division I proposals and bankruptcy.[3] Part V examines the primary causes of insolvency and provides a summary analysis of the types of debts and assets that consumer debtors bring to the proceeding. Part VI looks briefly at prior bankruptcies and proposals. Part VII examines potential points of failure of proposals and Part VIII looks at the type and amount of recoveries under different proceedings. Part IX concludes by summarizing research questions and making observations about the choice of proceedings by consumer debtors. The findings may offer a baseline of information that could be utilized for comparative purposes in a few years, in order to assess insolvency trends such as whether the nature of

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[3] *BIA, ibid.* See also *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act,* Statutes of Canada, Chapter 36, Royal Assent, December 14 2007, part proclaimed in force July 7, 2008 and the remainder not yet declared in force as of September 1, 2008 (Chapter 36).

financial distress for consumer debtors is deepening with time, whether income profiles, causes of insolvency are changing or are factors driving choice of proceeding.

II. Methodological Approach

The study concentrated on consumer debtors 2005-2007, examining 5,773 individual insolvencies in depth. The study examined 2,967 consumer debtors that filed Division II proposals; 1,063 Division II business proposals involving sole proprietors/individuals; 743 Division I proposals made by insolvent consumer debtors; and 1,000 consumer bankruptcy files.

A literature search was conducted at the outset, in order to identify the issues relevant to consumer financial distress and to ascertain the scope of empirical data that exists in other jurisdictions. While empirical scholarship on consumer debtors continues to be limited in Canada, there is a rich body of literature in the United States (US), in particular, that of the scholars involved with the Consumer Bankruptcy Project, a large-scale longitudinal research program initiated in 1981 by scholars Teresa Sullivan, Elizabeth Warren and Jay Westbrook and involving a number of scholars from multiple disciplines over the past 25 years, which has examined bankrupt households on a national basis.[4] The literature was examined to assist with identifying research questions and data that should be examined. Future work will hopefully compare the Canadian and U.S. findings.

The first part of the study involved design of research fields for retrieval of electronic records, working with staff and economists at the OSB. The data was generated by region across Canada to be representative of the breakdown of persons filing in various regions, in proportion to numbers filed, size of estates and type of file, in order to create an accurate representative sample.

The study then analyzed the cases to determine the causes of insolvency. One problem that currently exists with the electronic data is that there are not separately captured fields for cause of insolvency. Hence, the data on causes had to be manually pulled from the files; assessed in terms of the primary cause of insolvency, self-declared with the assistance of the trustee or administrator; and then entered into an Excel database. This task was very labour intensive, undertaken by UBC law students. Protocols for inputting data and a methodology for analyzing the data were developed, coding variables within cases on a consistent basis so that comparisons could be generated across region and cohort. The author undertook a random second-check on 300 files to verify consistency in the inputting of data.

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[4] The Consumer Bankruptcy Project (CPB) has conducted surveys and interviews and analyzed court filings and other data for large sample populations for 1981, 1991, 2001 and 2007, producing a series of research papers. See for example, Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, *Folklore and Facts: A Preliminary Report from The Consumer Bankruptcy Project*, 60 AM. BANKR. L.J. 293 (1986), (1981 CBP data); Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, *Consumer Debtors Ten Years Later: A Financial Comparison of Consumer Bankrupts 1981-91*, 68 AM. BANKR. L.J. 121 (1994), (1991 CBP data); Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, *Less Stigma or More Financial Distress: An Empirical Analysis of the Extraordinary Increase in Bankruptcy Filings,* 59 STAN L. REV. 213 (2006), (2001 CBP data); Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, *As We Forgive our Debtors: Consumer Credit and Bankruptcy in America* (Oxford University Press 1989); Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, *The fragile Middle Class: Americans in Debt* (Yale University Press, 2000); Elizabeth Warren and Amelia Warren Tyagi, "The Two-Income trap: Why Middle Class Mothers and Fathers are Going Broke" (2003); Robert M. Lawless, Angela K. Littwin, Katherine M. Porter, John A. E. Pottow, Deborah K. Thorne, and Elizabeth Warren, "Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors", (2008) AM. BANKRUPTCY LAW J., VOL. 82, at 349-406.

One limitation to analyzing these data was that there were instances in which bankrupts listed more than one cause of bankruptcy, for example, job loss combined with over-extension of credit. For purposes of examining the files, we took the declared primary and secondary causes, but it is important to note that there are frequently synergistic contributions to financial distress that are not captured when reporting global statistics.

The next stage was to analyze the full data set of 5,773 files by retrieving data and undertaking analysis of the data by region, type and quantum of debt and assets, dividends received by creditors, and other reported information.[5] Income to debt analysis would have been helpful, but there was inadequate data available on income of the consumer debtors studied. The data that were available allowed for global analysis of the files across different cohorts, as discussed later in this paper. While the data set was relatively complete, there were files in which fields had not been completed with information.[6] The data were generated through the OSB's database; hence a real strength of the study is the quality and reliability of the data on which various policy options can be explored. The OSB's move to e-filing and the collection of data have been extremely important initiatives for both government policy makers and scholars, in that it offers the opportunity to examine empirically what is occurring in the field. The information generated by study of the OSB data was supplemented by information gathering from a sample group of ten trustees in the insolvency professional community, who work on a daily basis with consumer debtors and with the existing legislation.

A limitation of the study is that it did not seek the direct input of consumer debtors through survey or other means. As discovered in a previous empirical study of elderly debtors under the OSB's research initiative, it is difficult to directly canvass consumer debtors, given their vulnerability, fear of public exposure and current university ethics standards for contact with vulnerable study populations.[7] However, as noted by scholars associated with the US Consumer Bankruptcy Project, direct interviewing and surveying considerably enhances the quantity and quality of information regarding consumer debtors and should be a future research priority in Canada.[8]

There were a number of research questions that the project sought to answer. First, was whether the causes of financial distress are a determinant of choice of proposal or bankruptcy. Second, what factors drive the filing of a Division I proposal, as opposed to a Division II consumer proposal? Third, what impact does the different timing period for rehabilitating one's credit rating have on the decision to make a proposal or not; and how does the availability of automatic discharge influence the choice to opt for bankruptcy? Are current surplus income requirements creating normative pressure to select a particular proceeding? Has the trustee's obligation to make a report that, in its view, the debtor was in a position to make a proposal had an impact on the type of filing? Will current proposed amendments encourage more debtors to undertake proposals? Only some of these questions were possible to answer with the nature and type of data available.

III. Context for the Study

In Canada, there has been a steady growth in consumer insolvency since the early 1970s. During the 1980s and 1990s, the average annual growth of consumer insolvency in Canada was approximately 7.5%. However, since 2000, the rate has slowed to an average annual rate of growth 1.9%. In 2006, the rate of consumer insolvency decreased for the first time by 4.1%, but continues to remain substantially higher than 25 years ago. There are no data available for why

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[5] The data was generated on December 1, 7 and 20, 2007 by the OSB.

[6] Given that some data collection is relatively recent by the OSB, the completeness of the data is likely to be enhanced in the future.

[7] Janis Sarra, "Growing Old Gracefully, An Empirical Investigation into the Growing Number of Bankrupt Canadians over Age 55", *2006 Annual Review of Insolvency Law* (Toronto: Carswell, 2007).

[8] Lawless *et al, supra*, note 4.

the rate slowed in the past two years. It could be as a result of better economic conditions, lower unemployment and higher GDP. However, it could also be as a result of individual debtors waiting longer to file insolvency proceedings. In the U.S., Ronald Mann has suggested that financially troubled consumer debtors are delaying filing bankruptcy, what he has called the "sweat-box" theory of consumer lending, whereby credit card lenders encourage debtors to continue making payments on their high interest credit cards for a few months longer before they file, contributing to the lenders' profits, but exacerbating the amount of debt of debtors by the time they file, placing them in deeper debt and thus at risk of losing more of their assets to satisfy creditors' claims.[9] Absent longitudinal data in Canada, one cannot determine if the same trend is occurring in this country.

In 1980, the rate of insolvency was 1.1 per thousand Canadians; by 2006, it was 3.8 per thousand, more than three times the 1980 rate.[10] To place this rate in context, the rate in the US was 7.0 insolvencies per thousand people in 2004; in the United Kingdom, 1.1 in 2004 and in Australia, 1.6 per thousand.[11] Hence, while Canada's rate is considerably lower than in the US, it is several times greater than the UK and Australia.

In 2007, there were a total of 108,830 bankruptcies and proposals in Canada.[12] Of these files, 79,796 or 73% were consumer bankruptcies.[13] 6,307 were business bankruptcies, which includes corporate and non-corporate businesses.[14]

As an alternative to bankruptcy, the *BIA* allows consumers and businesses to make a proposal, which is an arrangement with creditors for a compromise of liabilities, a revised schedule for payment or other arrangement that allows the debtor to work out its financial distress. The *BIA* proposal proceedings are used for individuals and for all sizes of business, from sole proprietorships to larger corporations, although this study examines only individual insolvency. Proposals can be made under the Division II consumer proposals provisions or under the Division I proposal provisions of the *BIA.* In 2007, there were 22,727 proposals filed, of which 3,241 were business proposals and 19,486 were consumer proposals.[15]

Another reason for undertaking this study was the growth in credit card debt in Canada and the need to consider the impact of that growth. Credit card debt has become a major contributing factor to the amount of debt carried by consumers, in some cases leading to insolvency. Given the high interest rates on credit cards, consumer debtors that do not have an income stream to cover the minimum payment are more likely to default on the credit card payments. Bankruptcy becomes a means of relieving the financial distress and having a "fresh start" in terms of the credit card debt. Ronald Mann has observed that to the extent that credit cards have facilitated entrepreneurial activity and consumer borrowing, they have been an important component of a modern economy, but that there are social costs associated with credit cards, in the form of financial distress and an increase in consumer bankruptcy.[16] He observes that excessive credit card debt can impose substantial costs on the debtor, family members and the general welfare

[9] Ronald Mann, "Consumer Bankruptcy and Credit in the Wake of the 2005 *Bankruptcy Reform Act* and the 'Sweat Box' of Credit Card Debt", (2007) U. Ill. L. Rev. 375 at 398.
[10] OSB, *An Overview of Canadian Insolvency Statistics to 2006, http://strategis.ic.gc.ca/epic/site/bsf-osb.nsf/vwapj/Statsbooklet2007-EN.pdf/$FILE/Statsbooklet2007-EN.pdf.*
[11] *Ibid.*
[12] Office of the Superintendent of Bankruptcy (OSB), *Annual Report, 2007*, http://strategis.ic.gc.ca/epic/site/bsf-osb.nsf/vwapj/annual-report2007.pdf/$FILE/annual-report2007.pdf.
[13] *Ibid.*
[14] OSB, *An Overview of Canadian Insolvency Statistics to 2006, http://strategis.ic.gc.ca/epic/site/bsf-osb.nsf/vwapj/Statsbooklet2007-EN.pdf/$FILE/Statsbooklet2007-EN.pdf.*
[15] *Ibid.*
[16] Ronald Mann, *Charging Ahead, The Growth and Regulation of Payment Card Markets,* (Cambridge University Press, Cambridge, 2006) at 3.

safety net; as well as cost consequences from the diminished productive activities of those individuals in financial distress.[17]

The pattern of consumer insolvency in Canada matches somewhat the pattern in the US, at least prior to the most recent round of legislative reform in the US. Essentially, increased numbers of consumer debtors are experiencing financial distress, from all levels of the social strata and from diverse regions.[18] Over-extension of credit appears to be a primary driving cause.[19]

Professors Warren, Westbrook and Sullivan, in their empirical study of consumer insolvencies in the US, report that consumer debtors filing for bankruptcy in the US have substantially larger debt loads than in the previous years; and median total debt loads in 2001 were up 55.9 percent from 1981 in inflation adjusted dollars.[20] Their data found that mean debt loads climbed tremendously between 1991 and 2001, in particular, home mortgages and payday loans. They observe that higher secured debt loads are consistent with greater assets and an increase in the number of homeowners since 1991, but also a consistent rise in unsecured debt over a twenty year period. Warren, Westbrook and Sullivan found that bankrupts had a very high degree of credit on an unsecured basis, a finding reinforced by the data in this study on Canada.[21] Mean unsecured debt in the US increased 48.9 percent from 1981 to 2001.[22]

Iain Ramsay has noted that in the US, there is substantial overlap of consumer and business debt, with many business debtors reporting a combination of business and personal reasons as triggers for their bankruptcy filings.[23] The data here also suggest a similar comingling of personal and business debt. This comingling of debt may help to explain the number of "business proposals" under the Division II consumer debtor proposal provisions under the *BIA*, as discussed below in Part V.

The rise in consumer debt in Canada is in part attributable to the growth in the alternative financial services market, the most well known of these services being pay day loans. While there has not yet been sufficient study of the effects of these services, Ruth Berry and Karen Duncan report that more than 350,000 Canadians use pay day loans each year, and that while costs of a first pay day loan may be 20% interest over two weeks, typically the loans are repeatedly rolled over with increased fees and service charges.[24] Another study indicates that on average, pay day lenders provide 15 rollover loans for every first time pay day loan extended.[25] Berry and Duncan found that in 2006, 25% of insolvent consumer debtors owed more than 25% of their monthly income to payday lenders.[26] This figure is incredibly high and may explain some

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[17] *Ibid.* at 49-50.
[18] Karen Gross, *Failure and Forgiveness*: Rebalancing the Bankruptcy System (New Haven: Yale University Press, 1997).
[19] *Ibid.*
[20] Warren, Elizabeth, Westbrook, Jay Lawrence and Sullivan, Teresa A., "Less Stigma or More Financial Distress: An Empirical Analysis of the Extraordinary Increase in Bankruptcy Filings" (May 2006) ('Less Stigma"); available at SSRN: http://ssrn.com/abstract=903355 at 13. Warren, Elizabeth and Westbrook, Jay Lawrence, "Financial Characteristics of Businesses in Bankruptcy" (January 2000). American Bankruptcy Law Journal Available at SSRN: http://ssrn.com/abstract=194750 or DOI: 10.2139/ssrn.194750
[21] Warren *et al,* Less Stigma, *ibid.*
[22] *Ibid.*
[23] Iain Ramsay, "Comparative Consumer Bankruptcy" . University of Illinois Law Review, p. 241, 2007 Available at SSRN: http://ssrn.com/abstract=958190. Iain Ramsay conducted a five-year empirical study of about 3,200 business cases originally filed in Chapter 7, Chapter 11 and Chapter 13 in 23 judicial districts during 1994, including both small and large businesses.
[24] Ruth Berry and Karen Duncan, "The Importance of Pay Day Loans in Canadian Consumer Insolvency, 2008 (on file with the Office of the Superintendent of Bankruptcy).
[25] Ernst & Young, "The Cost of Providing Payday Loans in Canada" (2006) http://www.cpla-acps.ca/english/reports/EYPaydayLoanReport.pdf.
[26] *Ibid.* at 11.

of the reason that consumer debtors file in Canada, although, as will be seen below, the amount of pay day debt is still not transparent, as it gets recorded across different categories of debt.

A canvass of the extensive literature on consumer insolvency is beyond the scope of this study; however, the scholarship does assist in framing some of the research questions posed here and does highlight the need for much further research into the nature of consumer financial distress and potential policy options.

IV. The Legislative Framework

It is helpful to commence with a very brief overview of the types of remedies available to individuals under the *BIA* when they are insolvent; specifically, bankruptcy, Division I and Division II proposals.[27]

1. Bankruptcy

An insolvent individual can make an assignment in bankruptcy or creditors can file an application for a bankruptcy order in respect of the individual.[28] In Canada, such bankruptcies are generally referred to as personal bankruptcy or consumer bankruptcy, and these terms are used interchangeably in this paper. By section 43(1) of the *BIA*, a creditor may file an application for a bankruptcy order against a debtor, defined as an insolvent person, who, at the time an act of bankruptcy was committed by him or her, resided or carried on business in Canada.

The *BIA* defines insolvent person in section 2(1) for purposes of access to the statute:

> 2(1) … "insolvent person" means a person who is not bankrupt and who resides, carries on business or has property in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and
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> (a) who is for any reason unable to meet his obligations as they generally become due,
> (b) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or
> (c) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due.

The *BIA* sets out ten acts of bankruptcy, the most commonly used one being that the insolvent person has ceased to meet liabilities as they generally become due.[29] The act of bankruptcy must have occurred within six months preceding the filing of the application for a bankruptcy order.

When a debtor is insolvent and seeking access to the *BIA*, a trustee in bankruptcy reviews the debtor's financial situation, explains the various options available, and determines whether any surplus income payments are required. All insolvent individuals are required to take counselling on money management, warning signs of financial difficulties, and obtaining and using credit, as well as counselling advice on creating a financial plan of action.

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[27] There are alternatives to proceedings under the *BIA*; however, such options are beyond the scope of this paper.
[28] For an explanation of the provisions, see L. Houlden, G. Morawetz and J. Sarra, *The 2008 Annotated Bankruptcy and Insolvency Act* (Toronto: Carswell, 2007), Part II, Bankruptcy Orders and Assignments, at 130-201.
[29] *BIA*, s. 42(1).

Automatic discharge is available for first-time bankrupts nine months after they make an assignment or are ordered into bankruptcy, unless the trustee recommends a discharge with conditions or it is opposed by a creditor, the trustee, or the Superintendent of Bankruptcy. The *BIA* sets out fifteen facts for which discharge may be refused, suspended or granted conditionally, including that the assets of the bankrupt are not of a value equal to fifty cents on the dollar on the amount of the bankrupt's unsecured liabilities, unless the bankrupt can satisfy the court that this situation has arisen from circumstances for which the bankrupt cannot justly be held responsible; the bankrupt has continued to trade after becoming aware of being insolvent; the bankrupt has failed to account satisfactorily for any loss of assets; and the bankrupt has contributed to the bankruptcy by rash and hazardous speculations, by unjustifiable extravagance in living, by gambling or by culpable neglect of the bankrupt's business affairs.[30] A conditional discharge may also be imposed where the bankrupt did not pay the agreed amount of surplus income, or the bankrupt filed for bankruptcy instead of proposing a viable proposal.

For second time bankrupts or those who do not qualify for an automatic discharge, the trustee is required within one year from the beginning of the bankruptcy to apply to the court for a hearing of the application for a discharge.[31] The court can order an absolute, conditional or suspended discharge, the latter requiring particular conditions be satisfied before the discharge is final.

The effect of bankruptcy is a "fresh start" financially. The bankrupt is released of most debts; however, specified debts are not released, for example, an award for damages in respect of an assault, spousal or child support, a debt arising out of fraud, any court fine, and debts for student loans when the bankruptcy occurs while the debtor is still a student or within ten years after the bankrupt has ceased to be a student.[32] The fresh start framework of bankruptcy under the *BIA* allows the bankrupt to begin to rebuild his or her credit rating and affords the bankrupt relief from the crushing burden of debt.

As noted in the introduction, an alternative to bankruptcy for the insolvent individual is a proposal under the *BIA.* There were 18,080 proposal estates closed in 2007, with assets valued at 1,761,978,535 CAD and liabilities of 3,254,998,920 CAD. Of those estates, the trustees realized 932,157,479 CAD and dividends that were paid to creditors totalled 707,428,734 CAD.[33] Hence, under *BIA* proposals, creditors realized 21.7% of the claims outstanding against the debtor. This amount is considerably higher than what creditors, particularly unsecured creditors, can expect to receive in bankruptcy. There are two kinds of proposals, Division I and Division II.

2. Division II Proposals

Proposal is defined in the *BIA* as including a proposal for a composition, where creditors agree to accept less than full repayment or an extension of time; and/or a scheme of arrangement in terms of alteration of debt and equity structure.[34]

Under both Division II and Division I proposals, there is an initial automatic stay on creditors moving to enforce any of their claims for a thirty day period, which gives the insolvent debtor a chance to negotiate with creditors for a possible proposal and going-forward plan to address the insolvency. A trustee or administrator assists with development of the proposal, and acts in a monitoring and advisory capacity.

[30] *BIA*, s. 173(1).
[31] When the recent amendments to the *BIA* come into force, there will be the availability of automatic discharge for second time bankrupts.
[32] *BIA*, s. 178(1).
[33] Administration costs for proposals totalled 224,728,745 CAD in 2006.
[34] *BIA,* section 2(1).

Division II consumer proposals are available to insolvent individuals whose debts are less than 75,000 CAD, excluding a mortgage on the individual's principal residence.[35] The provisions were enacted as a mechanism to deal with smaller estates on a more cost-effective and expedited basis. The number of consumer proposals has been growing since the introduction of Division II consumer proposals in 1993.[36] In 2006, more than 19,200 consumer proposals were filed, as opposed to 2,200 in 1993. Hence, 19.5% of consumer insolvency files were proposal proceedings in 2006, compared with only 3.8% in 1993.[37]

Division II proposals are exclusively consumer proposals. "Consumer debtor" is defined in the *BIA* as "a natural person who is bankrupt or insolvent and whose aggregate debts, excluding any debts secured by the person's principal residence, do not exceed seventy-five thousand dollars".[38] A consumer proposal must be made to creditors generally, but is not binding on secured creditors that have not filed a proof of claim.[39] While the statute does not distinguish between types of Division II proposals, the OSB collects data based on two types of filings. Where the individual debtor's debts are 50% or more business related, the OSB terms their proposals "Division II business proposals", even though they are filed by individuals under the Division II consumer proposal provisions. For consumer debtors whose liabilities are 50% or more consumer debt, the OSB collects the data under "consumer proposals".

Division II proposal proceedings are commenced by the debtor obtaining the assistance of an administrator in preparing the consumer proposal; and providing the administrator with the prescribed information on the consumer debtor's current financial situation.[40] The duties of the administrator, a trustee or another insolvency professional, are set out in the statute.[41]

A person already bankrupt can also make a proposal, but it must be approved by the inspectors of the bankruptcy estate and the bankrupt must have obtained the assistance of a trustee who will be the administrator of the consumer proposal.

The administrator investigates the consumer debtor's property and financial affairs in order to assess with reasonable accuracy the consumer debtor's financial situation and the cause of insolvency. The administrator provides counselling in accordance with directives issued by the OSB; prepares a consumer proposal; and files a copy of the proposal, signed by the consumer debtor, with the Official Receiver.[42] Within ten days following, the administrator prepares and files with the Official Receiver a report on the results of the investigation; the administrator's opinion as to whether the consumer proposal is reasonable and fair to the consumer debtor and his or her creditors; whether the consumer debtor will be able to perform the proposal; a condensed statement of the consumer debtor's assets, liabilities, income and expenses; and a list of the creditors whose claims exceed two hundred and fifty dollars.[43]

A consumer proposal must provide for the payment of preferred claims; for the payment of all prescribed fees and expenses of the administrator related to the proposal proceedings and of any person providing counselling.[44] The proposal must also set out the manner of distributing dividends. A proposal typically takes three to five years to complete the payment schedule.

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[35] It is possible to make a joint consumer proposal to consumer debtors who do not have total debts exceeding $75 000. Two or more consumer proposals may be joined where they could reasonably be dealt with together because of the financial relationship of the consumer debtors involved. *BIA*, s. 66.12(1.1).
[36] OSB, at 37.
[37] *Ibid.*
[38] *BIA*, s. 66.11. That cap will increase to $250,000 when the new amendments are proclaimed in force.
[39] *BIA*, s. 66.28.
[40] *BIA,* s. 66.13 (1).
[41] *BIA*, s. 66.13.
[42] *BIA.,* s. 66.13 (2).
[43] *BIA.,* s. 66.14.
[44] *BIA,* s. 66.12(6).

The administrator sends a copy of the proposal and the report to creditors, along with a claims form and a statement explaining that a meeting of creditors will be called only if the Official Receiver directs the administrator to call a meeting of creditors within 45 days, or if creditors having an aggregate of at least 25% in value of the proven claims request a meeting.[45] In most cases, no meeting of creditors to vote on the proposal is necessary.

Creditors have up to 45 days to consider whether to accept or reject the proposal. If creditors do not respond, they are considered to have accepted the proposal. If a sufficient number of creditors accept the proposal, it is binding on the debtor and creditors. Where, at the expiration of the 45 day period no obligation has arisen to call a meeting of creditors, the consumer proposal is deemed accepted by the creditors.[46] No court hearing is required, unless the administrator receives a request from the Official Receiver or any other interested party within 15 days of the acceptance or deemed acceptance of the proposal; and failing such request, the proposal is deemed approved by the court.[47] Hence, the proceeding is highly streamlined and cost effective, saving time and resources in terms of creditors' meetings and court appearances where creditors and the Official Receiver do not object to the proposal. When the proposal is fully performed, the administrator submits a certificate of full performance to the debtor and the Official Receiver.

If the proposal is rejected by creditors, the stay under the *BIA* is no longer in effect and creditors can move to enforce their claims. If the debtor fails to comply with the terms of the proposal, the court, on application, can annul the proposal where it appears to the court that the debtor was not eligible to make a consumer proposal when the proposal was filed; or where the consumer proposal cannot continue without injustice or undue delay; or where the approval of the court was obtained by fraud. The effect of annulment is a deemed assignment in bankruptcy.[48]

In addition to these provisions, a consumer proposal is deemed annulled where payments under a consumer proposal are to be made monthly or more frequently and the consumer debtor is in default to the extent of three months payments; or where payments under a consumer proposal are to be made less frequently than monthly and the consumer debtor is in default for more than three months on any payment.[49] The exception to the deemed annulment is where the court has previously ordered otherwise or where an amendment to the consumer proposal is filed before the deemed annulment.[50]

On annulment of a consumer proposal, if the debtor was insolvent prior to making the proposal, creditors have a claim against the debtor for the amount owed to them before the proposal, minus any amount the debtor paid them during the proposal. If the debtor was bankrupt when the proposal was made and the court subsequently annuls the proposal, the debtor is considered bankrupt on the date of the annulment.

The OSB reports that the failure rate of consumer proposals is about 30%, although it is important to examine at what point the proposal fails, as discussed below. By way of comparison, the failure rate under Chapter 13 of the US *Bankruptcy Code* is more than double this rate.[51]

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[45] *BIA*, s. 66.15.
[46] *BIA*, s. 66.18.
[47] *BIA*, s. 66.22.
[48] *BIA*, s. 66.30.
[49] *BIA*, s. 66.31.
[50] *BIA*, s. 66.31.
[51] Jacob Ziegel, Anthony Duggan and Thomas Telfer, *Canadian Bankruptcy and Insolvency Law, Cases, Text and Materials* (Toronto: Emond Montgomery, 2003) at 614. They suggest that the higher US rate is due to the fact that the ratio of Chapter 13 to Chapter 5 cases is about twice the ratio of consumer proposals to bankruptcies in Canada, and hence a number of debtors appear to be opting for proposals when perhaps they should be in liquidation, and second, that US consumers have previously had stronger incentives to opt for Chapter 13, even where the prospects for successful plan completion are not good. The incentives

Professors Ziegel, Telfer and Duggan have suggested that there are two possible explanations for the growth in Division II proposals since the mid-1990s, the first being that in 1997, amendments to the *BIA* required individual bankrupts to make mandatory surplus income payments; and second, the fee structure in the bankruptcy rules was substantially altered in 1998 to give trustees a stronger incentive to recommend consumer proposals to debtors.[52]

3. Division I Proposals

Division I proposals are available for individuals and businesses, and frequently used where the debts are more than 75,000 CAD and thus Division II is not available. Often the debtor needs time to prepare a proposal and so the legislation allows the debtor to file a "notice of intention to make a proposal", which creates a stay on creditors' enforcing their claims for a specified period until the debtor is able to make a proposal.[53]

A proposal trustee performs many of the same functions as an administrator in a Division II proposal, assessing the debtor's ability to make a proposal, monitoring the process, and assisting the debtor with mandatory filing requirements. As with Division II proposals, the Division I proposal provisions are highly codified, creating some certainty and predictability for both debtors and creditors.

Filing a notice of intention to make a proposal creates an automatic stay for 30 days, and the court has the authority to extend the stay for periods up to 45 days to a maximum of six months. The stay affords the debtor breathing space to devise a proposal that will be acceptable to creditors.[54] The debtor must file a projected cash flow statement with a trustee and the trustee must report on the reasonableness of the statement.[55] When the debtor has a proposal to present to creditors, a meeting is called, which allows creditors to vote on the proposed plan.[56] The statute requires that a majority of creditors in number and two-thirds in value of the claims of each class of creditor vote in favour of the proposal.[57] If the debtor garners the requisite support, the proposal is brought to the court for approval.[58]

The *BIA* sets out specific requirements of the proposal, in terms of the priority of claims that must be observed in a proposal, the fees and expenses of the trustee, specified Crown claims, and specified amounts owing to employees where the debtor is a business.[59] The court has the authority to annul a proposal if there is a default in the performance of any provision of the proposal, where the court's approval was obtained by fraud, or where it appears that the debtor cannot continue the proposal without injustice or undue delay.[60]

While Division I proposals were originally aimed particularly at small and medium size businesses, in terms of giving them an accessible and cost effective mechanism to devise an

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include the fact that Chapter 13 has a substantially higher ceiling for the admissible amount of debt; it permits the debtor to modify the rights of holders of secured claims, other than a claim secured only by a security interest in the debtor's principal residence and provides for the waiving or curing of any default; the list of non-dischargeable debts is smaller in Chapter 13 than it is for Chapter 7 filings; and the courts can grant hardship relief, although this authority is rarely exercised, *ibid.* at 612-614.

[52] *Ibid.* at 613.

[53] *BIA*, s. 50(1) and s. 50.4.

[54] *BIA*, s. 50.4.

[55] *BIA*, s. 50.4(2).

[56] *BIA*, ss. 51, 54.

[57] *BIA*, ss. 54, 62.

[58] *BIA*, ss. 58, 59.

[59] *BIA*, s. 60.

[60] *BIA*, s. 63.

arrangement with creditors to avoid bankruptcy and liquidation, they have been used increasingly by individuals whose debts exceed the cap allowable under the Division II consumer proposal provisions. This use is likely to shift somewhat if and when the amendments to the *BIA* are proclaimed in force, in that the cap under Division II will be increased to debts of 250,000 CAD. The files examined for purposes of this study were individual debtors using the Division I provisions, not companies.

The next part examines the causes of insolvency, the nature and type of liabilities and assets for each of the four data sets in the study.

V. Primary Causes of Insolvency and Nature of Debts and Assets

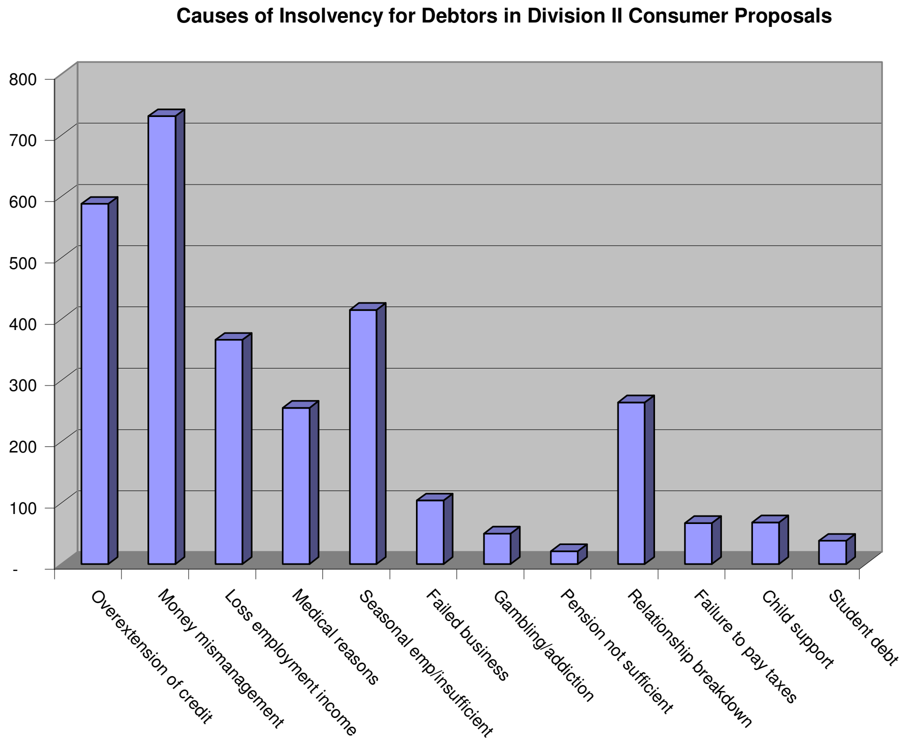
The study analysed the data for the primary causes of insolvency for the 5,773 files examined, broken down by Division I proposals, Division II consumer proposals, Division II business proposals by individuals, and bankruptcies, as set out in Graphs 1 to 4 below. As noted in the introduction, the causes had to be pulled manually from the files. The data offers fresh evidence and insight into why debtors might choose a proposal instead of bankruptcy, based on the cause of the financial distress and the nature and quantum of debt.

1. Division II Consumer Proposals

Graph 1 sets out the primary causes of insolvency for debtors that filed Division II consumer proposals between 2005 and 2007. Of 2,967 sample files reported in Graph 1, the primary causes of insolvency were over-extension of credit and money mismanagement. 20% (588) of the Division II consumer debtors declared overextension of credit as the primary cause of their insolvency, while 25% (731) reported that it was money mismanagement. These figures align with data in the US, which cites overextension of credit as a significant contributing factor to insolvency.[61]

Graph 1

[61] Ronald J. Mann, *Charging Ahead, The Growth and Regulation of Payment Card Markets*, (Cambridge University Press, 2006). See also articles from the Consumer Bankruptcy Project, cited at note 4.



Graph 1 also indicates that for just over 12% (366), the primary cause was loss of employment income and for 14% (415), the cause was seasonal employment or insufficient income. Together, therefore, employment related causes as the primary cause of insolvency comprised 26% of all debtors in the cohort. In this respect, Division II proposals offer consumer debtors relief from the temporary loss of employment or reduction in work. The statistics also support the finding of US scholars, who have observed that individuals are often driven to insolvency proceedings due to exogenous shocks such as job loss.[62]

8% (255) cited medical reasons for the insolvency, although it is difficult to discern from the data in any statistically significant manner if the rates refer to medical bills over and above coverage by the national healthcare system, or if some portion is due to lost income arising from medical problems. These causes appear somewhat conflated in the reported descriptions field, and deserve further study, particularly since Canada has a socialized health care system, where medical costs should not be a bar either to access to health care or a financial burden.

Only 2.3% cited the primary cause as failure to pay taxes. Relationship breakdown, which includes marriage breakdown and breakdown of a common law relationship, accounted for 8.9% (264) of the insolvencies. Student debts, child support and level of pension were not significant causes of insolvency for this group of consumer debtors. There had been anecdotal evidence from trustees that gambling and addiction are growing causes of individual insolvency, but such causes are not statistically significant in the reported reasons. However, the figures may be partially unreliable because of the stigma associated with such disclosures and because such addictions may be the underlying reason for over-extension of credit or money mismanagement.

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[62] Sullivan, Warren and Westbrook, *The Fragile Middle Class, supra*, note 4**.**

Given that over extension of credit was the primary cause of insolvency for one fifth of all the files, and that 90% of all debtors filing Division II consumer proposals had credit card debt, Table 1 below analyzes in some depth the sources of debt for this group of debtors. Overall, the total debt for this cohort was 249,105,530 CAD of which almost 58% was secured. However, if one excludes liability for real property mortgages that are residential homes, only 10.4% of the remaining total debts were secured debt. The data suggest that while home ownership is a significant asset for some debtors, it is coupled with significant mortgage debt, which comprises the majority of secured debt of Division II consumer debtors. Over-extension of credit was cited as the secondary cause of insolvency for an additional 11.3% of consumer debtors in this category.

Table 1 illustrates that credit card debt is a particularly acute problem. 18.2% of total liabilities for this category of consumer proposals were for credit card debt, both credit cards issued by banks and those issued by retail stores and other non-bank lenders. 99.6% of that debt was unsecured. The average (mean) debt was 12,419 CAD for credit cards issued by banks and trust companies and the median was 9,045 CAD. These figures are lower for credit cards issued by retail stores, etc., specifically 7,222 CAD was the mean and 4,884 CAD was the median.

13% of all liabilities were for bank loans, excluding real property residential mortgages, with a mean debt of 16, 605 CAD and a median debt of 13,218 CAD. 66.5% of all debtors in this cohort held such bank loans. Trustees have attributed the high amount of unsecured bank loan debt to the introduction of on-line credit applications and approvals, increasing the ease with which debtors acquire such loans. This amount represents the greatest amount of median debt after mortgage debt, about the same median as credit card debt owed when credit card debt of all types are tallied.

Table 1 also indicates that finance company loans comprised 5.9% of total liabilities for debtors filing Division II consumer proposals. In the Division II consumer proposal cohort, 44% of debtors had finance company loans, with the mean amount owed 11,380 CAD and the median 9,000 CAD. Trustees have reported that there are often consolidating loans whereby debtors get credit card debt consolidated into a lower interest rate loan, and that this effort to control debt is frequently undertaken before any insolvency filing, as a mechanism to address financial strain. Two thirds of these loans are secured.

Table 1

Sources of Debt for Debtors Filing Division II Consumer Proposals

Type of Debt	Total (Preferred, Unsecured and Secured)	Secured Amounts	Unsecured Amounts	Preferred Amounts	Number of Estates (Preferred, Unsecured and Secured)	Mean (Preferred, Unsecured and Secured)	Median (Preferred, Unsecured and Secured)
Bank Loans (except real property mortgage)	32,744,404	5,142,127	27,602,277	-	1,972	16,605	13,218
Credit Cards Bank/Trust Companies Issuers	30,439,616	81,570	30,358,046	-	2,451	12,419	9,045
Credit Cards Other Issuers	14,890,905	79,518	14,811,386	-	2,062	7,222	4,884
Finance Company							

Loans	14,713,800	4,988,816	9,724,984	-	1,293	11,380	9,000
Loans from Individuals	462,545	34,877	427,668	-	71	6,515	5,000
Other	14,141,308	1,605,315	12,529,743	6,250	1,692	8,358	3,966
Real Property Mortgage	132,972,293	131,728,840	1,243,453	-	934	144,692	137,137
Student Loans	3,048,292	3,000	3,045,292	-	268	11,374	7,547
Taxes Federal/Provincial/ Municipal	5,692,367	122,300	5,555,067	15,000	921	6,181	2,000
Total	249,105,530	143,786,364	105,297,916	21,250	2,967		

Table 1 above also indicates that liability for mortgages on real property for this cohort was 53% of all liabilities by total dollar value, of which 99% was secured debt. 31.5% of all debtors in this cohort had mortgage debt. In respect of the value of the home equity, these debtors declared house assets in the amount of 153,308,078 CAD, of which only 23,999,583 CAD or 16% was exempt, as indicated in Table 2 below. The fact that 84% of mortgage home equity was non-exempted assets suggests that the high degree of equity in the home was a significant factor in filing a proposal.

A consumer proposal affords insolvent consumer debtors the opportunity to hold onto a house, and that avenue may be a driver in choice of solution to the financial distress. The median amount of assets in a home for this cohort was 152,500 CAD. Comparing median mortgage debt and median house assets, consumer debtors filing Division II consumer proposals had a median amount of about 15,000 CAD of house equity to protect. Given that Canada has modest exemption amounts for home, with some jurisdictions having no exemption, proposals offer a means of retaining that equity while managing the burden of debts faced by the consumer debtor.

Table 1 indicates that taxes comprised 2.3% of all liabilities; and while 31% of this cohort had outstanding tax debt, the median amount was only 2,000 CAD. Student loans were 1.2% of total liabilities, but 31% of all debtors in this cohort had outstanding student loans.

Table 2 breaks down the assets of debtors by type of asset. One can see that after an interest in a house, the value of cottages and motor vehicles is relatively high. The retention of a car for purposes of commuting to work is a key driver in the US, and these data appear to align, with the median for automobiles, motor cycles and other motor vehicles over 4,000 CAD. While there is some exemption for motor vehicles on bankruptcy, Table 2 illustrates that overall, 63% of the automobile assets were non-exempt, had the consumer debtor opted for bankruptcy. Other assets have a relatively low median value.

Table 2

Assets of Debtors Filing Division II Consumer Proposals

Type of Asset	Total (Exempt and Non-Exempt)	Exempt Amounts	Non-Exempt Amounts	Estimated Realizable	Number of Estates	Mean (Exempt and Non-Exempt)	Median (Exempt and Non-Exempt)
Automobile	13,463,914	4,946,499	8,517,415	659,635	1,928	6,983	4,606

Cash on hand	264,674	12,481	252,193	195,429	352	752	250
Cash surrender value	9,642,021	6,863,640	2,778,381	1,113,410	721	13,373	4,000
Cottage	524,500	454,000	70,500	14,400	8	65,563	24,500
Estimated tax refund	22,280	-	22,280	17,140	13	1,714	950
Furniture	6,153,009	6,041,870	111,139	8,491	2,489	2,472	1,800
House	153,308,078	23,999,583	129,308,495	4,899,440	934	164,141	152,500
Land	432,770	16,810	415,960	85,312	18	24,043	14,250
Motorcycle	328,331	71,304	257,027	43,850	59	5,565	4,225
Other assets	2,191,079	1,213,309	977,770	389,352	342	6,407	1,500
Other motor vehicle	485,002	88,700	396,302	57,025	68	7,132	4,400
Personal effects	2,396,789	2,355,826	40,963	22,623	1,819	1,318	1,000
Recreational equipment	335,036	20,700	314,336	60,927	70	4,786	2,250
Securities	3,036,955	1,901,801	1,135,154	350,745	315	9,641	2,492
Snowmobile	46,150	600	45,550	6,172	20	2,308	1,700
Total	192,630,587	47,987,123	144,643,464	7,923,951	2,967		

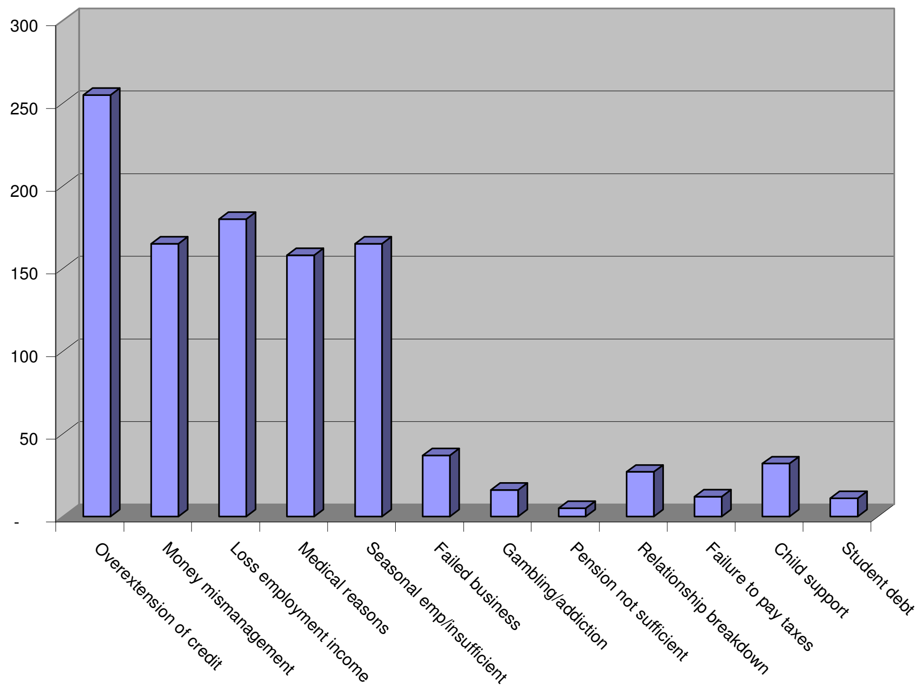
2. Division II Business Proposals

Turning to the next data set, Graph 2 summarizes the causes of financial distress for individuals that are insolvent and filed Division II consumer proposals, but they are classified as “business proposals” by the OSB because 50% or more of their debt is business-related. There are 1,063 files in this cohort. This category is comprised primarily of individuals that were sole proprietors or in a small partnership. 24% (255) of the Division II business proposal debtors declared overextension of credit as the primary cause of their insolvency, while 15.5% (165) reported that it was money mismanagement.

For 17% (180), the primary cause was loss of employment income and for 15.5% (165), the cause was seasonal employment or insufficient income. Interestingly, although called business proposals by the OSB’s 50% business debt measure, only 3.5% (37) report a failed business as a cause of the insolvency. One possible explanation is that the objective of making the proposal is to salvage the business activity where possible; hence, the debtor does not declare the business failed. This figure can be compared, for example, with the bankruptcy data in Graph 4, below, where failed businesses account for almost three times the number of primary causes of bankruptcy.

Graph 2

Causes of Insolvency for Debtors Filing Division II Business Proposals



The data indicates that in a number of cases, other financial pressures placed the individual into financial distress and the business proposal provided the mechanism to try to preserve the business. Surprisingly, 15% (158) reported medical reasons as the primary cause of their insolvency, a considerably higher percentage than for the other two proposal categories. One explanation for this higher figure is that the individual in many cases would not have access to supplemental health benefits and income replacement that is often available in an employment relationship with companies. If the business is a sole proprietorship, any lengthy illness can place the business at risk as the individual is not able to perform the services offered by the business.

Only 1.1% (12) of Division II business debtors cited the cause as failure to pay taxes. Relationship breakdown, student debts, child support and level of pension also were not significant causes of the insolvency, as illustrated in Graph 2

Turning to the types of liabilities these individuals had at the time of filing, Table 3 sets out the sources of debt for the cohort of debtors that filed Division II business proposals. Here again, mortgages play a significant role in the insolvency and may be a driver for filing a proposal rather than bankruptcy. 60.8% of total liabilities for this cohort are mortgage debt, of which the overwhelming majority is secured. The mean and median amounts per individual are almost identical to that for other Division II consumer debtors.

14.6% of total liabilities are for credit card debt, of which 98% is unsecured. The average is higher than for Division II consumer proposal debtors, but the mean is comparable. 12.3% of total liabilities are for bank loans, excluding mortgages on real property. Here both the mean and median are 5-6,000 CAD more than the median amount for the individuals in the consumer Division II cohort, 22,263 CAD and 18,192 CAD respectively for this group. One explanation is that the nature of the business debts may result in higher level of liabilities, even for debtors with less than 75,000 CAD in debt. The data also indicate that individuals filing business proposals rely heavily on credit card debt and bank loans as a means of financing their business activities.

Table 3 also highlights that 5.7% of total liabilities, a median of 10,000 CAD, are for finance company loans, most of which were unsecured. The reason for this relatively high figure is likely the same as for consumers filing Division II consumer proposals, as discussed above. However, another explanation is that finance companies are willing to extend operating loans to small businesses on an unsecured basis, as long as the amounts remain modest.

Here again, the amount of tax owed is only 1.3% of total liabilities by dollar amount, suggesting that tax relief for this cohort is not a significant factor in choice of proceeding. However, 40% of all those filing had taxes owing, with the median at 1,964 CAD. This figure suggests that while tax debt is not a primary cause of insolvency for this group, a significant number of people may let their taxes slide in the period prior to becoming financially distressed.

Table 3

Source of Debt Division II Business Proposals

Type of Debt	Total (Preferred, Unsecured and Secured)	Secured Amounts	Unsecured Amounts	Preferred Amounts	Number of Estates (Preferred, Unsecured and Secured)	Mean (Preferred, Unsecured and Secured)	Median (Preferred, Unsecured and Secured)
Bank Loans (except real property mortgage)	17,342,925	3,178,779	14,164,146	-	779	22,263	18,192
Credit Cards Bank/Trust Companies Issuers	12,779,590	33,250	12,746,340	-	907	14,090	9,911
Credit Cards Other Issuers	7,747,140	12,013	7,735,127	-	844	9,179	5,843
Finance Company Loans	8,004,626	2,835,589	5,169,037	-	605	13,231	10,000
Loans from Individuals	181,552	57,000	124,552	-	23	7,894	5,000
Other	6,381,596	701,235	5,677,061	3,300	707	9,026	4,339
Real Property Mortgage	85,775,072	84,972,365	802,707	-	592	144,890	137,000
Student Loans	935,623	-	928,623	7,000	90	10,396	7,367

Taxes Federal/Provincial/ Municipal	1,868,519	93,695	1,759,824	15,000	422	4,428	1,964
Total	141,016,643	91,883,925	49,107,417	25,300			

Table 4 sets out the summary data on the assets of debtors filing Division II business proposals. The median amount of house value is 150,000 CAD and compared with mortgage liabilities for this cohort, there is a median amount of equity of close to 15,000 CAD, almost the same as the Division II consumer proposal group. Also similar to that group, here there are significant assets in motor vehicles of different kinds, cottages and land, the vast majority of which are non-exempt assets. The median amount of securities held by this group is higher than that for the Division II consumer proposal debtors, with a mean of 13,115 CAD and median of 3,200 CAD.

Table 4

Assets for Debtors Filing Division II Business Proposals

Type of Asset	Total (Exempt and Non-Exempt)	Exempt Amounts	Non-Exempt Amounts	Estimated Realizable	Number of Estates (Exempt and Non-Exempt)	Mean (Exempt and Non-Exempt)	Median (Exempt and Non-Exempt)
Automobile	7,442,293	2,249,066	5,193,227	281,246	896	8,306	5,750
Cash on hand	190,998	18,389	172,609	153,721	137	1,394	250
Cash surrender value	5,360,655	4,279,992	1,080,663	361,250	331	16,195	5,532
Cottage	129,900	-	129,900	76,800	7	18,557	16,000
Estimated tax refund	1	-	1	1	1	1	1
Furniture	3,307,865	3,245,504	62,361	9,745	869	3,807	3,000
House	94,030,201	12,680,658	81,349,543	2,318,804	604	155,679	150,000
Land	225,046	-	225,046	79,117	15	15,003	8,946
Motorcycle	81,899	32,550	49,349	9,351	26	3,150	2,000
Other assets	1,632,370	730,052	902,319	159,909	162	10,076	2,000
Other motor vehicle	361,766	34,500	327,266	66,495	54	6,699	4,000
Personal effects	1,146,020	1,128,490	17,530	7,500	590	1,942	1,000
Recreational equipment	226,976	17,200	209,776	64,407	45	5,044	2,500
Securities	1,796,801	1,545,574	251,227	92,831	137	13,115	3,200
Snowmobile	45,051	6,500	38,551	12,400	24	1,877	1,250
National	115,977,843	25,968,474	90,009,368	3,693,578			

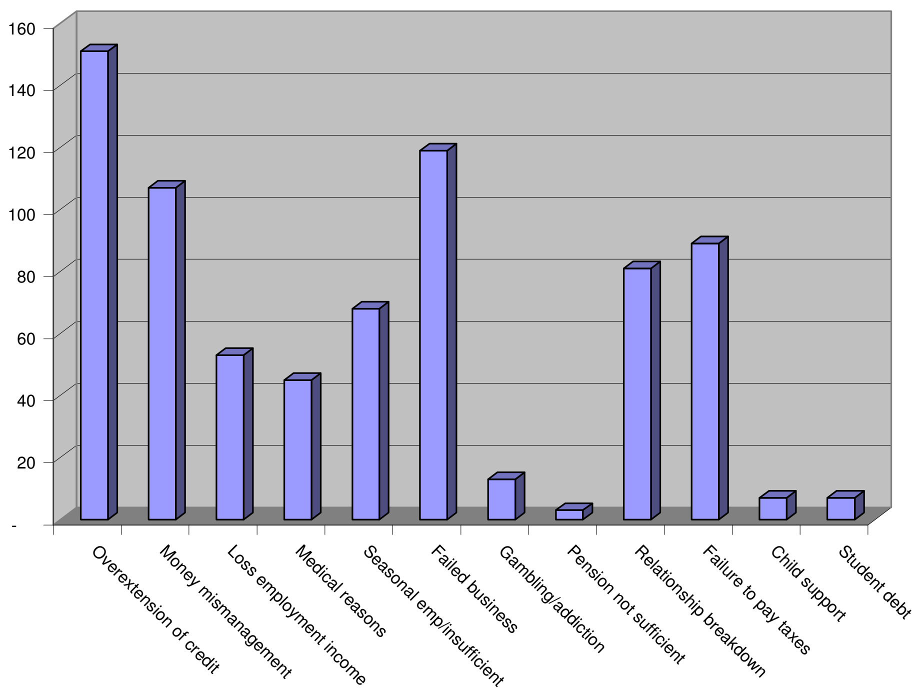
3. Division I Proposals

Turning to the Division I proposals by individuals, Graph 3, below, summarizes the data for 743 Division I proposal files. Here, debtors generally have more than 75,000 CAD in debt, excluding mortgages on the home. The most frequent causes of insolvency were over-extension of credit, a failed business and money mismanagement. 20.3% (151) of the Division I consumer debtors declared overextension of credit as the primary cause of their insolvency. 16% (119) declared a failed business to be the primary cause for filing a Division I proposal. 14.4% (107) reported that it was money mismanagement.

Graph 3 illustrates that only 7.1% (53) reported that the primary cause was loss of employment income, considerably less than for Division II. For 9% (68), the primary cause was seasonal employment or insufficient income. 12% of Division I individual debtors cited the cause as failure to pay taxes, significantly higher than observed for Division II proposals. Marriage breakdown and breakdown of a common law relationship accounted for 10.9% (81) of the insolvencies. Student debts, child support and level of pension were not significant causes of the insolvency.

Graph 3

Causes of Insolvency for Debtors in Division I proposals



Analyzing the sources of debt for this cohort, Table 5 illustrates that 14.3% of total liabilities are credit card debt. The median amounts are more than double those for Division II proposals, not surprising given the liability cap on Division II proposals. 14.3% of total liabilities are bank loans, excluding real property mortgages. The mean and median of bank loans owed are higher than for Division II proposals, the mean being double the amount. 27.8% is mortgage debt, of which 95% is secured. Here again, both the mean and median are higher than for the other categories of proposals.

Interestingly, 17.2% of all liabilities are for taxes owing, a significantly higher amount than for the other proposal categories. Equally, while the mean owing was 91,627 CAD, the mean was 30,300 CAD, a fairly significant tax debt. These figures suggest that debtors with significant tax debt are using Division I proposal proceedings as a mechanism to address their tax debt. They are frequently ineligible to file a proposal under Division II because of the quantum of debt overall.

Five of the trustees interviewed for purposes of the study also observed that debtors with high tax debt, as well as others with considerable assets, may file a Division I proposal knowing that creditors, in particularly Canada Revenue Agency, will not support the proposal, resulting in automatic bankruptcy. They nevertheless file in this way, in order to bypass the stigma of the bankruptcy notices that must be publicly advertised when a debtor files bankruptcy proceedings. While the data cannot confirm the extent of such a practice, it may illustrate that the data do not paint the entire picture of why particular options are being chosen when a debtor becomes insolvent.

Table 5

Sources of Debt - Division I Proposals

Type of Debt	Total (Preferred, Unsecured and Secured)	Secured Amounts	Unsecured Amounts	Preferred Amounts	Mean (Preferred, Unsecured and Secured)	Median (Preferred, Unsecured and Secured)
Bank Loans except real property mortgage	27,118,428	6,991,658	20,126,769	-	51,361	35,467
Credit Cards Bank/Trust	19,859,184	618,098	19,241,086	-	33,660	22,762
Credit Cards Other Issuers	7,249,875	25,000	7,224,875	-	15,969	8,387
Finance Company Loans	11,718,043	3,934,279	7,783,764	-	36,965	16,000
Loans from Individuals	4,597,302	202,000	4,395,302	-	117,880	19,500
Other	32,341,410	4,654,182	27,671,444	15,784	70,155	12,700
Real Property Mortgage	52,683,548	49,907,256	2,776,292	-	176,790	150,952
Student Loans	1,163,067	10,000	1,153,067	-	20,405	11,383
Taxes	32,619,341	1,455,340	31,154,988	9,013	91,627	30,300
National	189,350,198	67,797,813	121,527,588	24,797		

Table 6 provides summary data of assets held by the individual debtors filing Division I proposals. The median value of houses is substantially higher than in the Division II cohorts, approximately 36,000 CAD higher. Table 6 illustrates that there are also significantly more assets in terms of land, recreational equipment, and securities held. With more debts than Division II debtors, this group of debtors has also had greater assets, which are at risk if the debtor is not able to successfully complete a proposal. As noted above, debtors file Division I proposals to protect their assets, but the fact that the same stigma does not attach to a proposal as a bankruptcy may offer another explanation of choice of proceeding. While there has been a public policy shift away from viewing bankruptcy as a negative status, studies in both Canada and the US indicate that there continues to be considerable stigma associated with filing bankruptcy.[63]

Table 6

Assets for Debtors Filing Division I Proposals

Type of Asset	Total (Exempt and Non-Exempt)	Exempt Amounts	Non-Exempt Amounts	Estimated Realizable	Number of Estates (Exempt and Non-Exempt)	Mean (Exempt and Non-Exempt)	Median (Exempt and Non-Exempt)
Automobile	6,348,458	2,900,667	3,447,792	184,639	502	12,646	7,501
Cash on hand	875,526	35,000	840,526	752,095	118	7,420	500
Cash surrender value	13,097,723	10,724,902	2,372,821	1,131,598	315	41,580	10,000
Cottage	397,600	-	397,600	87,383	8	49,700	27,500
Estimated tax refund	26,785	-	26,785	19,665	7	3,826	1,820
Furniture	1,947,091	1,908,976	38,115	15,665	609	3,197	2,500
House	73,177,072	19,974,131	53,202,941	5,334,768	345	212,107	186,930
Land	2,166,230	106,800	2,059,430	392,999	25	86,649	69,600
Motorcycle	210,350	74,000	136,350	32,275	28	7,513	6,000
Other assets	7,394,391	2,912,689	4,481,703	992,554	247	29,937	3,500
Other motor vehicle	582,350	152,700	429,650	86,116	36	16,176	6,250
Personal effects	817,355	794,135	23,220	29,180	467	1,750	1,000
Recreational equipment	1,008,523	5,000	1,003,523	197,120	73	13,815	7,000
Securities	1,413,361	589,661	823,700	512,293	48	29,445	7,501
Snowmobile	67,550	-	67,550	28,000	19	3,555	2,000
National	109,530,366	40,178,660	69,351,706	9,796,349			

63 Sarra, *supra*, note 7 and Lawless *et al*, *supra*, note 4.

Having now analyzed a snap shot of proposal debtors in terms of causes, assets and liabilities, their files are compared with 1,000 representative bankrupts on the same criteria.

4. Consumer Bankruptcies

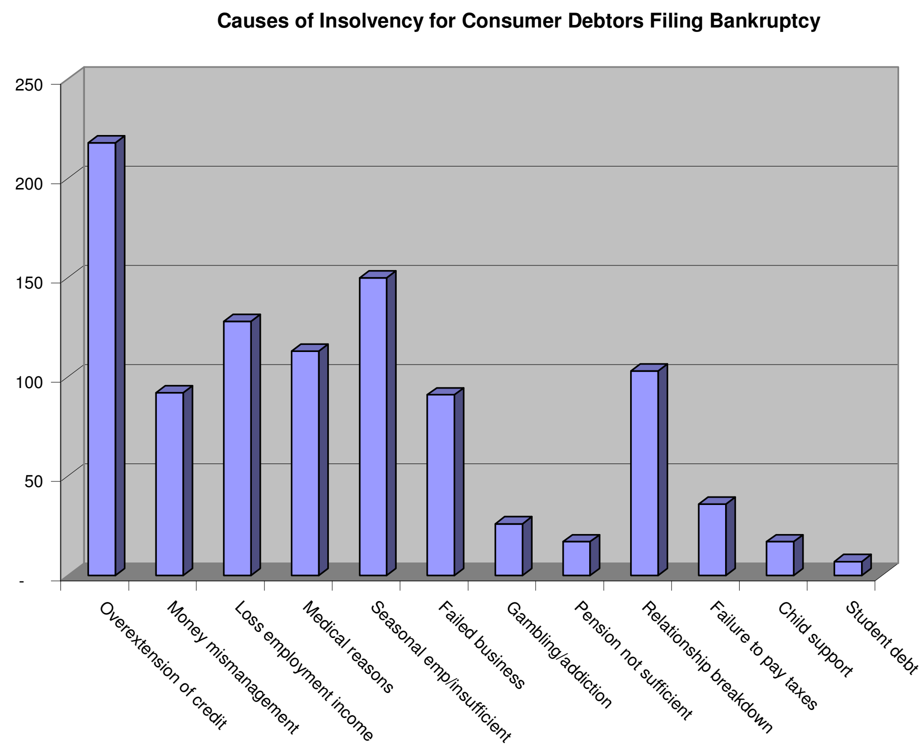
One can contrast the causes of insolvency for proposals with the sample of consumer bankruptcies, as illustrated by Graph 4. Here we see a somewhat different pattern for the sample of 1,000 files. Overextension of credit is by far the most significant cause of insolvency. 22% of the debtors filing consumer bankruptcy reported overextension of credit as the primary cause of their insolvency. A smaller percentage, only 9.2%, reported money mismanagement. Loss of employment income as the primary cause was 12.8%. For 15%, the cause was seasonal employment or insufficient income, only slightly higher than for those that filed consumer proposals. Together then, almost 28% of consumer bankrupts had employment related causes of insolvency.

Slightly higher, 3.6% of bankrupts cited the primary cause as failure to pay taxes. Relationship breakdown, which includes marriage breakdown and breakdown of a common law relationship accounted for 8.9% (264) of the insolvencies. Student debts, child support and level of pension were not significant causes of insolvency, the same as for those filing Division II proposals.

A higher number of bankrupts cited medical reasons as the primary cause of insolvency, 11.3% compared with 8.6% for debtors filing Division II proposals. Medical problems cited included supplementary medical bills, loss of employment from extended illness, and loss of income to be home to care for elderly and ill family members, including parents and children. The disclosed information was too limited and could have benefited from more in-depth survey or interview information. The high rate is of significant concern as Canada prides itself on its socialized healthcare system. Further research should be conducted to examine more precisely the extent to which medical issues are facing consumer debtors in insolvency proceedings.

Failed business was also reported as 9.1% for consumer bankrupts, compared with only 3.5% of those filing a consumer proposal. In terms of marriage and common law relationship breakdown, for 10.3% of consumer bankrupts it was the primary cause of financial distress, whereas it was 8.9% for Division II proposal filers.

Graph 4



Turning to the sources of debt for this cohort, Table 7 illustrates that 17% of the total debt was from credit card debt, a median of 14,137 CAD. Mortgages comprise 22.3% of the liabilities, 105,430 CAD; and bank loans 15%, with the median being 14,137 CAD. Finance company loans comprised 7% of total liabilities, a median of 9,000 CAD. A greater percentage reported taxes owing as a primary cause, compared with those debtors filing Division II consumer proposals. However, the median amount owing of 3,204 CAD remains relatively low. Overall, 72% of debt was unsecured. The significance of these amounts is set out in the preliminary observations below.

Table 7

Sources of Debt Consumer Bankruptcies

	Total (Preferred, Unsecured and Secured)	Secured Amounts	Unsecured Amounts	Preferred Amounts	Number of Estates (Preferred, Unsecured and Secured)	Mean (Preferred, Unsecured and Secured)	Median (Preferred, Unsecured and Secured)
Bank Loans (except real property mortgage)	14,298,254	2,534,742	11,763,512	-	609	23,478	14,137
Credit Cards Bank/Trust Companies Issuers	11,216,560	107,902	11,108,659	-	752	14,916	8,353

Credit Cards Other Issuers	5,592,478	25,350	5,567,129	-	667	8,385	4,502
Finance Company Loans	6,610,546	2,240,069	4,370,477	-	449	14,723	9,000
Loans from Individuals	5,011,913	55,000	4,956,913	-	43	116,556	4,000
Other	23,936,534	2,213,590	21,696,594	26,350	695	34,441	4,925
Real Property Mortgage	21,919,095	20,309,887	1,609,209	-	173	126,700	105,430
Student Loans	1,390,952	575	1,390,377	-	126	11,039	8,500
Taxes Federal/Provincial/Municipal	8,219,035	186,757	8,030,410	1,868	368	22,334	3,204
National	98,195,368	27,673,871	70,493,280	28,218			

In terms of assets for this cohort, overall, consumer bankrupts have fewer unencumbered assets and less equity in the home. As the discussion in Part IX illustrates, in a number of cases, the equity for consumer bankrupts in the home is negative, meaning that bankruptcy may provide relief where there is no equity to protect and the mortgage debt is exacerbating the financial distress. Given fewer assets overall, bankruptcy may be the most viable option for these debtors, given that it offers a shorter period of time to exit the process, and arguably a more cost effective means by which to rehabilitate their credit rating.

Table 8

Assets Consumer Bankruptcies

Type of Asset	Total (Exempt and Non-Exempt)	Exempt Amounts	Non-Exempt Amounts	Estimated Realizable	Number of Estates (Exempt and Non-Exempt)	Mean (Exempt and Non-Exempt)	Median (Exempt and Non-Exempt)
Automobile	3,666,166	1,138,486	2,527,680	150,422	583	6,288	3,000
Cash on hand	89,220	2,054	87,166	86,144	222	402	200
Cash surrender value	1,527,673	1,074,983	452,690	124,147	122	12,522	3,950
Cottage	93,512	-	93,512	6,200	5	18,702	5,000
Estimated tax refund	2,935	-	2,935	2,486	3	978	451
Furniture	1,752,704	1,732,909	19,795	2,507	756	2,318	2,000
House	23,885,608	5,328,571	18,557,037	168,383	201	118,834	105,000

Land	532,100	159,600	372,500	5,100	7	76,014	15,000
Motorcycle	57,700	10,900	46,800	7,950	13	4,438	5,000
Other assets	1,780,510	388,981	1,391,529	73,744	116	15,349	1,500
Other motor vehicle	192,659	9,300	183,359	4,861	21	9,174	2,859
Personal effects	483,213	473,464	9,749	6,891	479	1,009	500
Recreational equipment	240,552	30,700	209,852	17,153	32	7,517	1,825
Securities	957,328	786,106	171,222	105,478	75	12,764	2,350
Snowmobile	42,250	1,000	41,250	4,325	9	4,694	3,000
National	35,304,131	11,137,054	24,167,077	765,790			

VI. Prior Bankruptcies and Proposals

The study looked briefly at prior bankruptcies and prior proposals to see if anything could be discerned. Tables from two of the proposal cohorts are included here. It is evident from Table 9, below, that some jurisdictions, such as Alberta and Ontario, and to a lessor degree, British Columbia and Québec, have a number of second or more previous proposals and prior bankruptcies. However, these figures do not really provide any insights independent of other information required. They do not measure the regional breakdown by either population of the province or territory, or by the population of bankrupts in those regions. It is difficult to determine if previous filers made filing choices this time in light of previous experience with proposals or bankruptcies, and whether that experience was positive or negative. The Tables are included here only in hopes that it will spark the interests of legal scholars in the near future to examine these and other questions.

Table 9

Prior Bankruptcies and Prior Proposals, Division 1 Proposal Cohort

Province	Prior Bankruptcy	Prior Bankruptcy (%)	Prior Proposal	Prior Proposal (%)
Alberta	32	29%	16	39%
British Columbia	21	19%	5	12%
Manitoba	1	1%	-	-
New Brunswick	4	4%	1	2%
Newfoundland	1	1%	-	-
Northwest Territories	-	-	-	-
Nova Scotia	1	1%	1	2%
Nunavut	-	-	-	-
Ontario	21	19%	8	20%
Prince Edward Island	-	-	-	-
Québec	18	16%	5	12%
Saskatchewan	13	12%	5	12%
Yukon	-	-	-	-
National	112		41	

Table 10
Bankruptcies and Prior Proposals, Division II Business Proposal Cohort

	Prior Bankruptcy	Prior Bankruptcy (%)	Prior Proposal	Prior Proposal (%)
Alberta	6	2%	-	-
British Columbia	10	4%	1	4%
Manitoba	3	1%	-	-
New Brunswick	1	0%	-	-
Newfoundland	1	0%	-	-
Northwest Territories	-	-	-	-
Nova Scotia	14	5%	-	-
Nunavut	-	-	-	-
Ontario	125	49%	14	52%
Prince Edward Island	-	-	-	-
Québec	88	35%	12	44%
Saskatchewan	7	3%	-	-
Yukon	-	-	-	-
National	255		27	

Of note is that Berry and Duncan found that in 2006, 32% of insolvent pay day loan holders had previously filed bankruptcy or proposal proceedings, compared with 15% of those not holding pay day loans.[64] However, they found that the incidence of filing proposals and bankruptcies was almost identical, suggesting that the data do not point to consumers filing for bankruptcy over a proposal based on the number of pay day loans held.[65]

VII. Success and Failure Rates of Division II Proposals

There were also some data on the success and failure rates of Division II proposals, which deserve brief mention here. Table 11 examines the total number of proposals that failed, are ongoing and were successfully completed for 2002 to 2007. However, given that most of the files from 2004 forward are still ongoing, there is little insight that can yet be drawn from 2006 and 2007. More significant, perhaps, is the data in Table 12, which indicates when and why proposals fail. Even the incomplete data for 2006 and 2007 indicate the same pattern of failure for proposals.

Table 11
Division II Proposals by Year and Status at December 5, 2007 [66]

Table of Div II proposals by year and status

Year	Group			Total
	Failed	Ongoing	Success	
2002	5119	551	8684	14354
2003	5218	2544	7748	15510
2004	4983	5511	5159	15653
2005	4539	9732	2393	16664
2006	3620	13120	965	17705
2007	1409	16688	294	18391
Total	24888	48146	25243	98277

[64] Berry and Duncan, *supra*, note 24 at 13.
[65] *Ibid.*
[66] Office of the Superintendent of Bankruptcy, data provided 2008.

Table 12
Failed Division II Proposals by Year and Reason for Failure 2002 to December 2007 [67]

Table of Div II Proposals by Year and Failed Estate Type Code

	Withdrawn Div II Proposal Before Approval (Ss. 66.25)		Rejected Div II Proposal - Creditor Acceptance Refused (Ss. 66.19(1))		Refused Div II Proposal - Court Approval Refused (Ss. 66.24(2))		Reinstated Bankruptcy - Div II Prop Withdrawn or Creditors Acceptance Refused		Reinstated Bankruptcy - Div II Prop Court Approval Refused		Deemed Annulment - Div II Proposal by a Debtor - In Default (Ss. 66.31(1))		Court Annulment - Div II Proposal by a Debtor (Ss. 66.3(1,3))		Deemed Annulment - Div II Proposal by a Bankrupt (no bankruptcy)		Court Annulment - Div II Proposal by a Bankrupt (bankruptcy) (Ss. 66.3(5)(a))		T
2002	194	3.79%	401	7.83%	4	0.08%	6	0.12%	1	0.02%	4475	87.37%	8	0.16%	30	0.59%	3	0.06%	5
2003	249	4.77%	545	10.44%	1	0.02%	7	0.13%	0	0.00%	4380	83.89%	14	0.27%	22	0.42%	3	0.06%	5
2004	306	6.14%	583	11.70%	2	0.04%	10	0.20%	0	0.00%	4027	80.81%	27	0.54%	28	0.56%	0	0.00%	4
2005	293	6.46%	542	11.94%	2	0.04%	2	0.04%	0	0.00%	3657	80.57%	32	0.71%	11	0.24%	0	0.00%	4
2006	330	9.12%	622	17.18%	2	0.06%	3	0.08%	0	0.00%	2639	72.90%	7	0.19%	17	0.47%	0	0.00%	3
2007	276	19.59%	498	35.34%	2	0.14%	2	0.14%	0	0.00%	627	44.50%	3	0.21%	1	0.07%	0	0.00%	1
Total	1648	6.62%	3191	12.82%	13	0.05%	30	0.12%	1	0.00%	19805	79.56%	91	0.37%	109	0.44%	6	0.02%	24

Taking 2002 to 2006 data only, 1,372 or 6% of 23,485 Division II proposals are withdrawn prior to approval, pursuant to ss. 66.25 of the *BIA*. There had been observations by several trustees interviewed that the filing of a proposal proceeding serves as a placeholder for consumer debtors, granting them temporary relief from creditors until they determine what they are going to do about their financial distress. This use of the stay is apparent in some cases, particularly commencing 2004, but given the low overall percentage, it does not appear to be the predominant practice.

The decision by creditors not to approve a proposal is a significant reason for a failed proposal. 11.5% of proposals fail because creditors vote against the proposal. However, almost 90% survive the creditor approval threshold. The high approval rate at this stage of the process is likely in large measure due to the statutory deemed creditor approval structure where creditors do not object in requisite numbers, as discussed in Part III.

The court rarely refuses to approve a proposal once it has received requisite creditor support and thus the failure rates at this point in the proceeding are insignificant.

The most significant reason for failure is the deemed annulment. Again taking the 2002 to 2006 data, 19,178 files failed due to the deemed annulment provisions. That figure is 82% of all failed proposals. The high rate of failure at this point is likely due to the arbitrariness of the deemed failure provisions and limited opportunity to salvage a proposal once three months of payments or three payments are missed, even where there are legitimate and temporary reasons for a missed payment and where a debtor otherwise has had an excellent payment record under the proposal. This problem is likely to be addressed with the 2007 reforms, expected to be in effect in 2009, as discussed below.

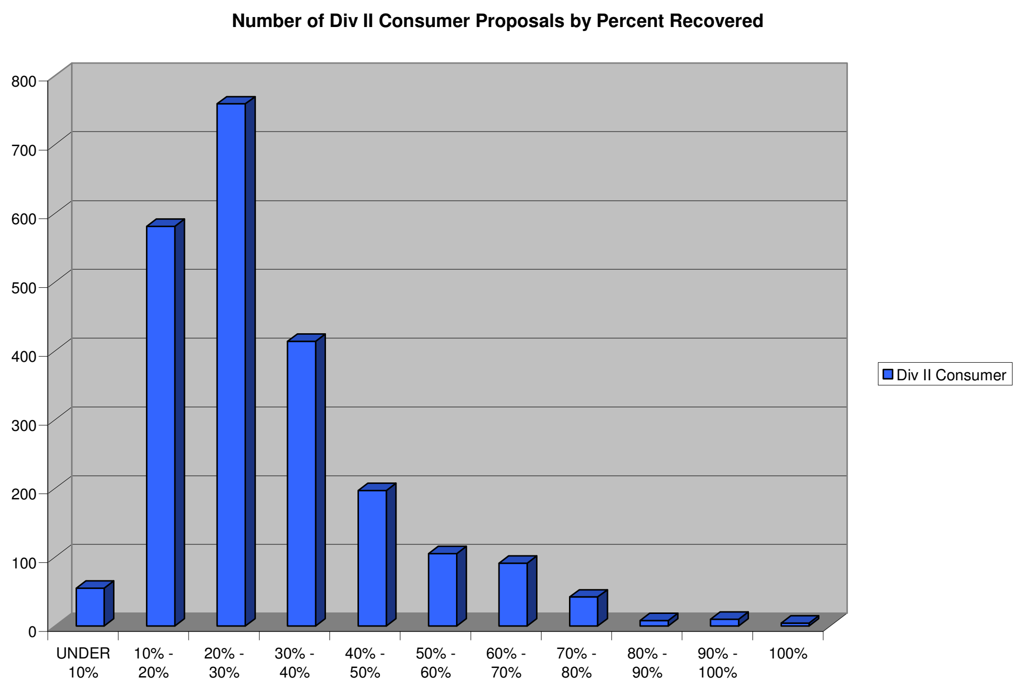
[67] Office of the Superintendent of Bankruptcy, data provided 2008.

VIII. Percentage of Estate Recovered

Not surprisingly, the data indicate that overall, recovery rates to creditors are higher under all types of proposals than they are on a bankruptcy. In part, this greater recovery is due to the amount of assets and surplus income that such debtors have; and because the ability to make payments over three to five years enhances the ability of such debtors to meet a portion of their debt obligations.

Graph 5 illustrates that for Division II consumer proposals, 63% of the files resulted in a 10% to 40% recovery rate for creditors, after fees and disbursements were paid out. Of that amount, one third recovered 20% to 30%. These figures suggest that proposals do allow some recovery for creditors, although not the full amount owed. Less than one percent (0.65%) of the files allowed a recovery to creditors of more than 80%.

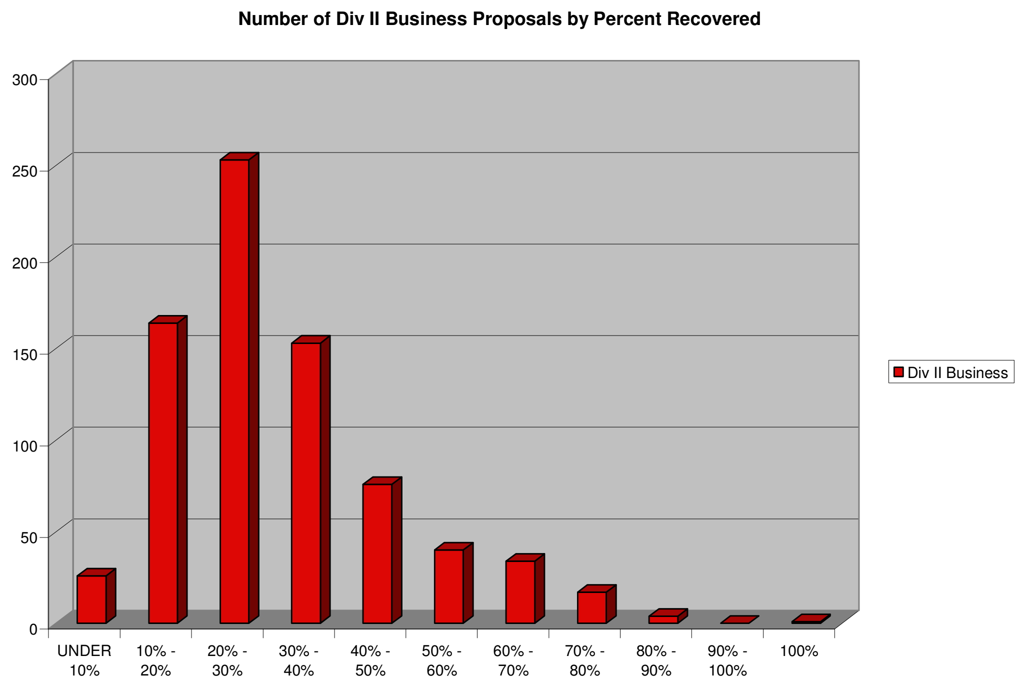
Graph 5
Recovery Rate Division II Consumer



The graph for business proposals made by individual debtors under Division II proceedings reveals a similar pattern, as illustrated by Graph 6 below. For the majority of the sample files, the rate of recovery of assets for creditors was between 10% and 40%. In one third of files, creditors recovered 20% to 30% of the value of their claims. This figure affirms that proposals do allow some recovery for creditors, although not the full amount owed. Less than one percent (0.65%) of the files allowed a recovery to creditors of more than 80%.

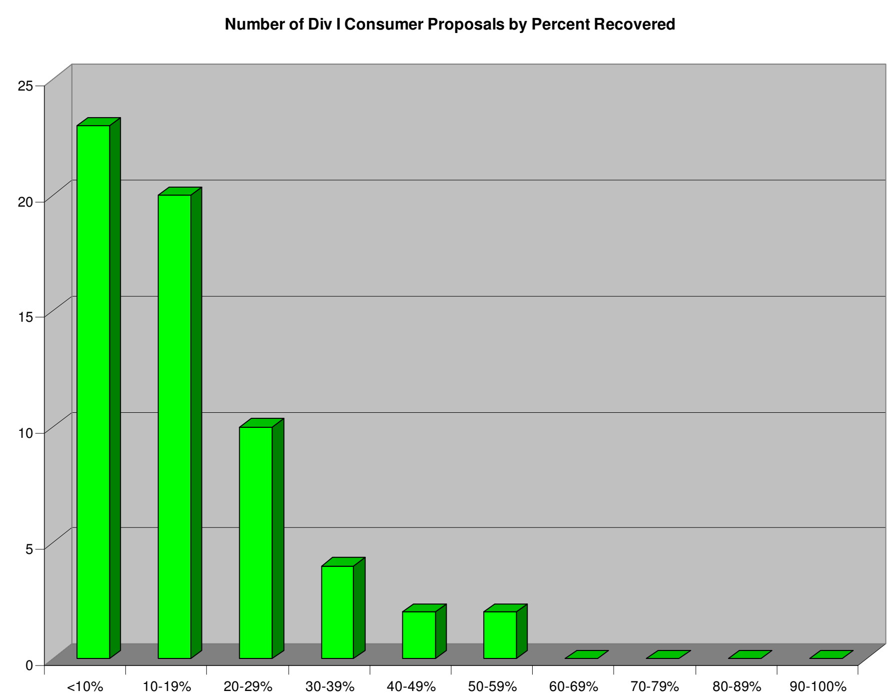
Graph 6

Recovery Rate for Division II Business Proposals



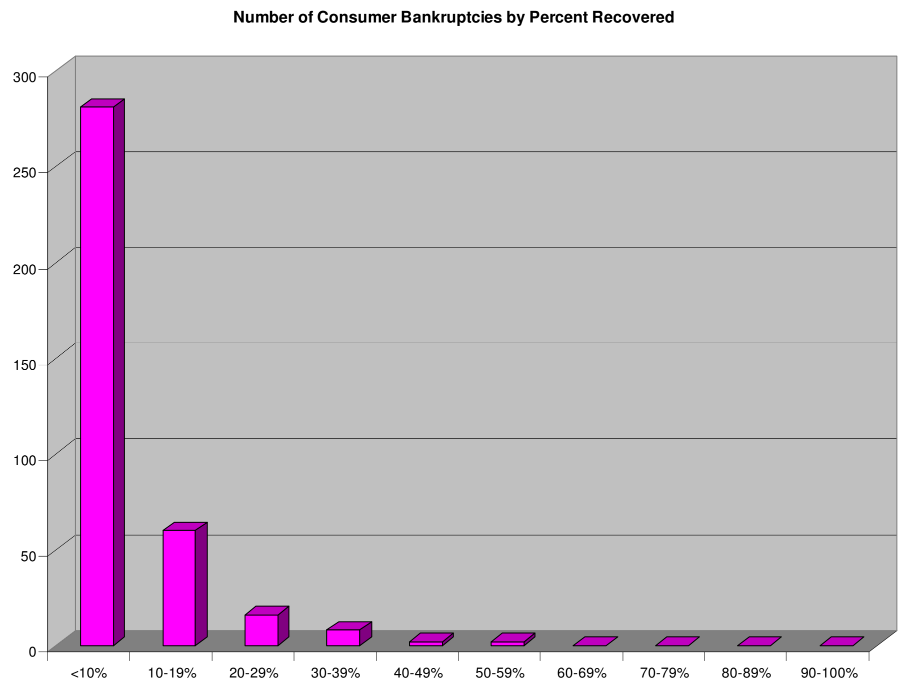
Graph 7 illustrates that the recovery by percentage of debt is lower under Division I, although the amount of debt is considerably higher. In the majority of cases, the recovery is less than 20% of total outstanding liabilities, suggesting that Division I proposals offer considerable relief to debtors from their outstanding debt.

Graph 7
Recovery Rates Division I Proposals



Finally, Graph 8 illustrates that there is relatively little recovery of debt under consumer bankruptcy proceedings, and creditors receive less than 10% of their claims in the vast majority of cases. In part, these figures are due to the lower asset levels of bankrupts, as discussed above, and in part, it is due to lower income and thus an inability of most consumer bankrupts to make surplus income payments.

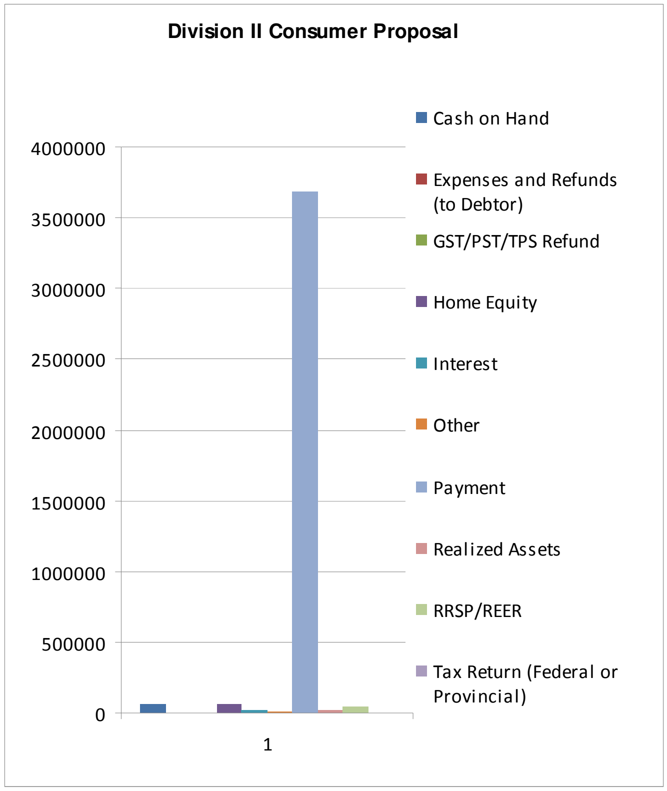
Graph 8
Recovery Rates Bankruptcy



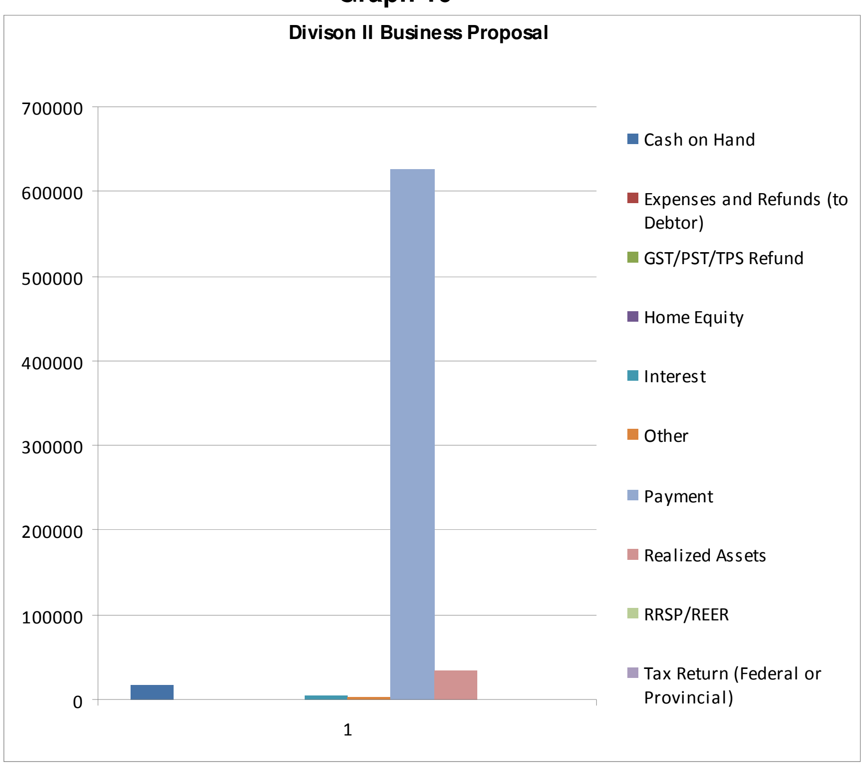
In looking at where creditors have realized on assets or income of the debtor, Graphs 9 to 12 illustrate the receipts to the estate and thus to creditors, after fees and disbursements of the trustee or administrator. Unfortunately, the data were in a format that did not allow any firm conclusions in respect of choice of proceeding and method of realizing on claims.

For Division II consumer and business proposals, the receipts come primarily from surplus payments, as illustrated in Graphs 9 and 10. There was some limited recovery of assets under Division II business proposals, but payments were the principal source of receipts.

Graph 9

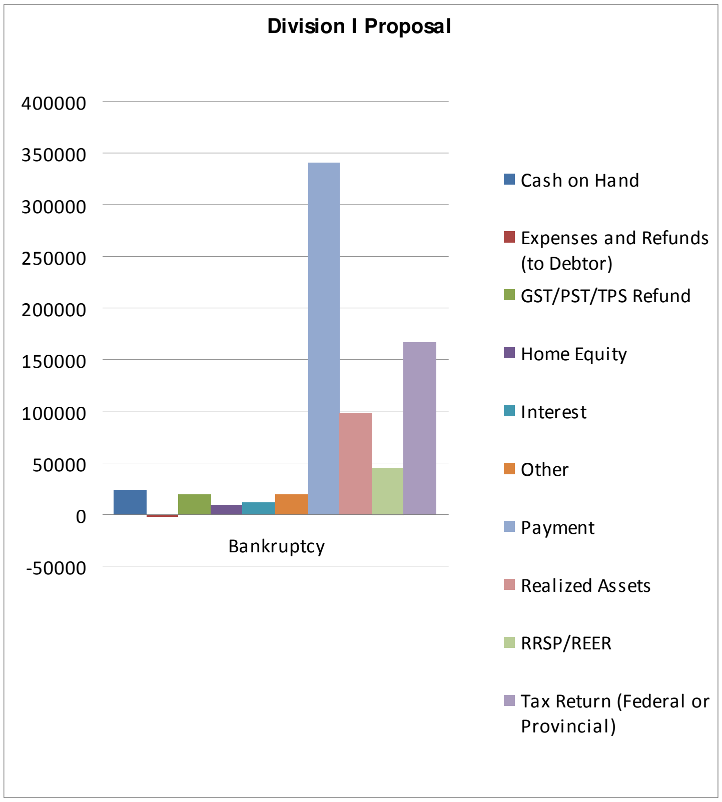


Graph 10



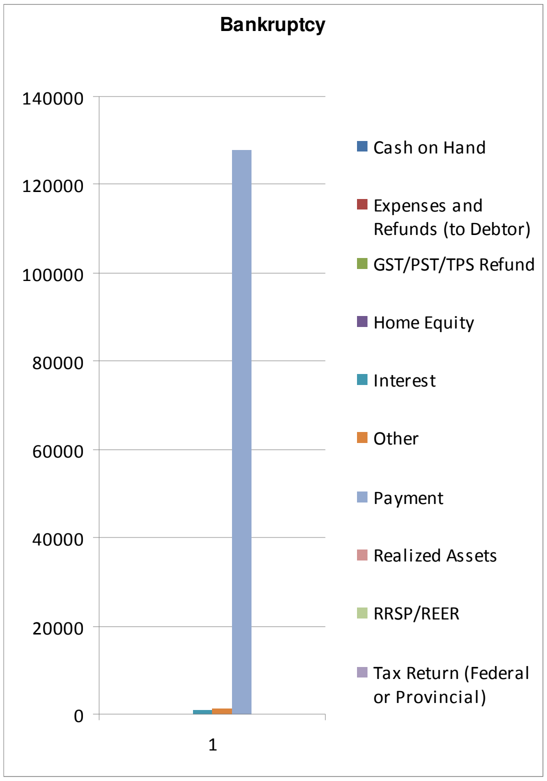
In contrast, Graph 11 illustrates that the value to meet creditors' claims in a Division I proposal is drawn from a number of sources, including payments, tax return receipts, realized assets, RRSPs and cash on hand.

Graph 11



For bankruptcies, Graph 12 illustrates that most recoveries come from surplus income payments. There is not a clear explanation for this pattern, given that consumer debtors do have some non-exempt assets. Moreover, it is important to note that an estimated 85% of all consumer bankrupts do not have surplus income that is available to pay creditors' claims. These data require further examination and more detailed information before any meaningful observations can be made.

Graph 12



Overall, these data offer some baseline information that could prove valuable in further assessment of consumer insolvency, either at a period after individual debtors exit insolvency proceedings, as a way of measuring the success of their choice of proceeding and longer term financial wealth; or as a baseline for future studies of the nature of consumer debtor financial distress. Data is not currently collected on this basis, but such information would allow for deeper and more nuanced observations regarding the position of consumer debtors and their best options for remedying their financial distress.

IX. Research Questions and Observations

This part provides some summary observations in respect of the research questions.

1. Are the causes of financial distress a determinant of choice of proposal or bankruptcy?

It does not appear from the data that the causes of bankruptcy, for the most part, are a determinant of choice of proposal or bankruptcy, although in particular instances, some debts may drive choices in one direction. The data above allow for some preliminary observations across data sets. In terms of causes of insolvency, the top four causes are summarized for each cohort. For Division II consumer proposals, the top causes were money mismanagement (25%); overextension of credit (20%); seasonal employment/insufficient income (14%) and job loss (12%). For Division II individual business proposals, the primary declared causes were overextension of credit (24%); money mismanagement (16%); job loss (17%) and seasonal employment/insufficient income (16%). For Division I proposals, those causes were overextension of credit (20%); failed business 16%); money mismanagement (14%) and failure to pay taxes (12%). Finally, for bankruptcy, it was overextension of credit (22%); seasonal employment/insufficient income (15%); job loss (13%) and medical reasons (11%).

The data indicate that overextension of credit is a primary cause of insolvency, with it being 20% to 24% the primary cause across all cohorts. Home mortgage liability is significant for the Division I proposal debtors, but less significant for bankrupts, many of whom do not have equity in homes.

Credit card debt is a serious problem across all groups, and is growing, as observed by Ronald Mann and other scholars. Canada would benefit from longitudinal data in respect of credit card or other debt. Qualitative data in respect of credit card debt within this study made some reference to use of credit cards for payment of groceries and utilities, in addition to more general consumer spending, particularly in the period leading up to filing insolvency proceedings. These data confirm an earlier study that found that credit card debt was being used by older consumer debtors to buy necessities.[68] Given that credit card debt is high interest debt and not subject to specific payment schedules, credit card debt can more easily accumulate and then pose significant problems for low income debtors. Yet, to date, insolvency policy does not really factor the nature of this debt into policy development.

Job loss and seasonal employment together are a significant cause of insolvency across Division II consumer proposal debtors (26%), Division II business proposal debtors (33%), and bankrupts (28%), but less so for Division I proposal debtors (16%). These data suggest that there are broader economic and social challenges that need to be addressed, as financial distress is often beyond the control of the individual debtor. To date, there is little linkage in Canada between economic stimulus and employment policy development and insolvency law policy development. Without longitudinal data over an extended period, it is difficult to know whether the problem of insufficient employment opportunities is a growing phenomenon, data that would be helpful to collect in the future.

Money mismanagement as the primary cause of insolvency figures prominently in Division II consumer proposal debtors (25%), and is relatively important in Division II business proposals (15%) and Division 1 proposals (14%); but is less so in bankruptcy (9%). It makes sense that those debtors who could better manage financially may end up in proposal proceedings, because they have assets to protect and a proposal may allow them to become financially viable if they can acquire the skills and information to live within their financial capacity. Current mandatory counselling that focuses on the money management aspects of consumer insolvency may assist, although there has been little empirical study to date on the effectiveness of mandatory credit counselling. However, there is some question as to the value of these programs where poor money management is less of an issue than lack of reasonable levels of employment income or lack of jobs. These programs need future assessment in terms of whether they expend resources in the most appropriate direction.

Failed business was most significant for Division I proposal debtors (16%). However, the reasons underlying the failure of the businesses in the cohort were not sufficiently disclosed to make meaningful observations. Future research should be conducted into what aspects of the business failed, as there is considerable difference between larger market failures, sector downturns, and mismanagement or poor governance practices within a small business.

Medical reasons are a significant cause for Division II business proposal debtors (15%) and bankruptcy (11%), compared with the other cohorts, Division II consumer proposal debtors (8%) and Division I proposal debtors (6%). However, as noted earlier, it is uncertain whether medical bills and lack of coverage, or medical problems resulting in inability to earn sufficient income are the real source of the financial distress. Equally, medical debt may be masked if consumer

[68] Sarra, *Growing Old Gracefully, supra*, note 7.

debtors have paid for medical bills by credit card on exit from hospital or particular outpatient services, as is the normal practice in some regions. Direct survey and interview data would assist in acquiring a clearer picture of this cause of insolvency.

2. Does home ownership influence the decision regarding choice of proceeding?

The OSB offers the following summary data on home ownership, indicating that overall, bankrupts have fewer houses than other categories of consumer debtors:[69]

Table 13

Percentage Estates with Houses by Type

	Total Estates	Estates with Houses	Percentage
Bankruptcy	993	201	20.24%
Division I	731	345	47.20%
Division II Business	1085	604	55.67%
Division II Consumer	4453	1344	30.20%
Total	7262	2494	34.34%

From the data in this study, it appears that home ownership is one predictor of proposal filing, but only where there is equity to preserve in the home.

The data indicate that mortgage debt as a percentage of total liabilities is high in Division II proposals in particular, less so for Division I and even less for bankruptcies. Mortgage debt was 53% of total liabilities for Division II consumer proposals, with 32% of all debtors in this cohort holding mortgage debt. Mortgage debt was 61% of total liabilities for Division II business proposals, with 56% of all debtors in this cohort holding mortgage debt. Mortgage debt was 28% of total liabilities for Division I proposals, with 40% of all debtors in this cohort holding mortgage debt. In contrast, mortgage debt was only 22% of total liabilities for bankruptcies studied, with 17% of all debtors in this cohort holding mortgage debt. Mortgage debt is thus not as significant in bankruptcy, as compared with Division II proposals or Division I proposals.

These figures indicate that fewer bankrupts have houses, compared with proposal debtors. One can examine the mean and median amount of house assets against the mean and medium amount of mortgage debt as an indicator of equity that debtors are trying to protect. Although not a straight calculation, it is a rough measure of equity across the cohort.

Amount owed under mortgage

	Mean	Median
Division II consumer	$ 144,692	$ 137,137
Division II business	$ 144,890	$ 137,000
Division I	$ 176,790	$ 150,952
Bankruptcy	$ 126,700	$ 105,430

House asset value

	Mean	Median
Division II consumer	$ 164,141	$ 152,500

[69] Source, Office of the Superintendent of Bankruptcy, December 20, 2007.

Division II business	$ 155,679	$ 150,000
Division I	$ 212,107	$ 186,930
Bankruptcy	$ 118,834	$ 105,000

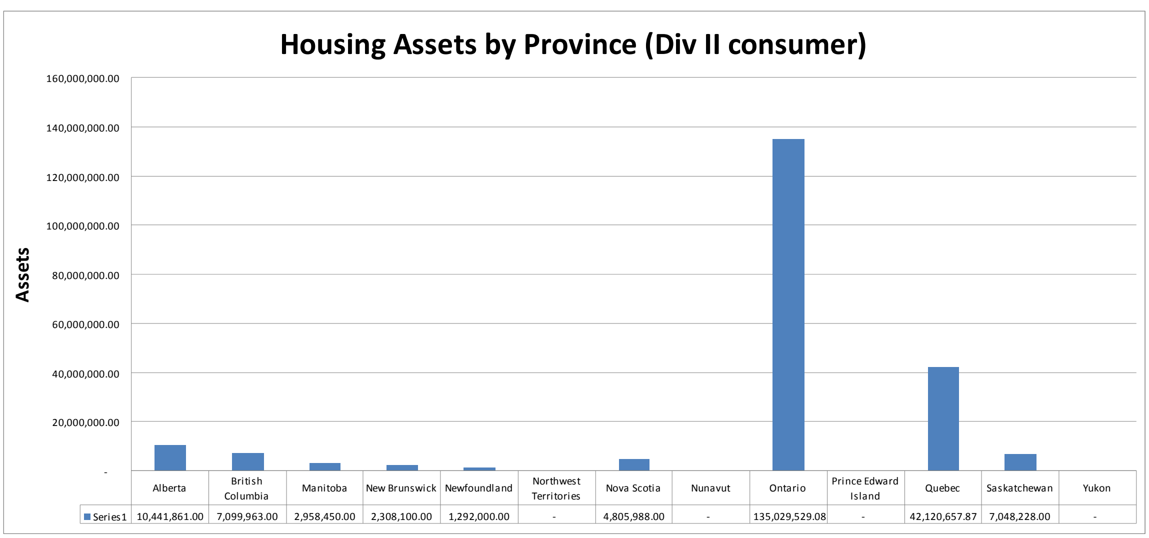
Comparing figures across data sets, it is clear that for both mean and median, the amount of mortgage debt for consumer bankrupts is greater than the value of the assets, meaning that the bankrupts were in possession of homes, although lower value than other categories, but they did not have equity in the home to protect. The negative equity can be a function of dropping house prices and/or further borrowing on the mortgage in the period prior to financial distress. These data are drawn from the period before the sub-prime mortgage crisis in the US.

In contrast, there is considerable house equity across all categories of proposals, suggesting that protection of home equity, the most valuable asset in all proposal categories, is a major influence on choice of proceeding. For Division II consumer proposal debtors, the median equity was over 15,000 CAD; for Division II business proposal debtors, the median equity was 13,000 CAD; and for Division I proposal debtors, it was 36,000 CAD. Hence, protection of house assets appears to be a significant influence on choice of proposal versus bankruptcy.

Given that there are different exemption rates for homes across the country, a further research question is the extent to which regional exemption rates for primary residences influence choice of proceeding. This is an important issue that deserves further investigation as this study was not able to undertake a detailed analysis of this issue.[70] However, on a summary basis alone, one can view the regional distribution of housing assets for the Division II and Division I consumer data sets, as summarized in Graphs 13 and 15 below.

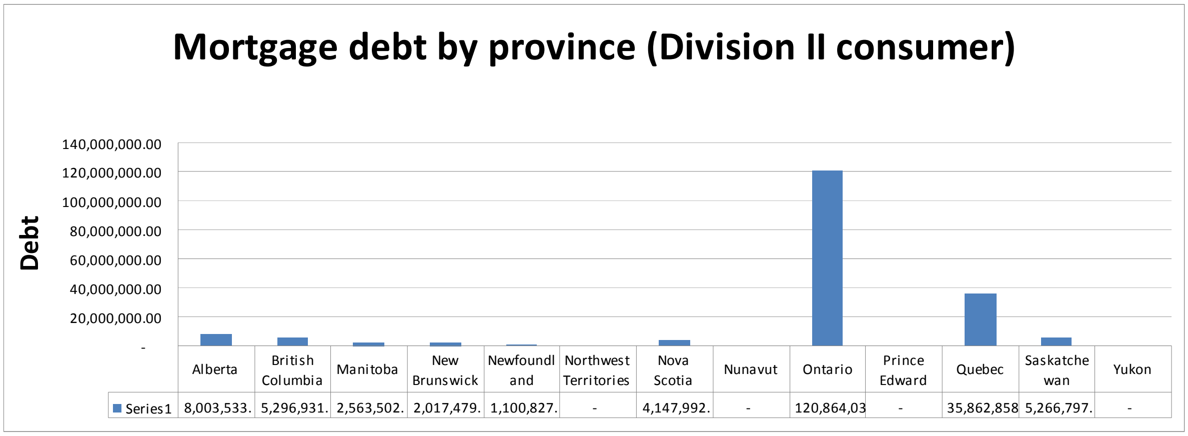
On simple overall totals, unadjusted for regional population totals, Graph 13 illustrates that the overall dollar amount of housing assets is far more significant in Ontario and Québec than other jurisdictions for Division II consumer debtors. Graph 15 illustrates that the overall dollar amount of housing assets for Division I debtors is more evenly distributed across several provinces, although Ontario is still significantly higher than the other regions. Graphs 14 and 16 below illustrate that the mortgage debt follows the same regional pattern as housing assets for Division II and Division I consumer debtors.

Graph 13 Housing Assets by Province, Division II Consumer

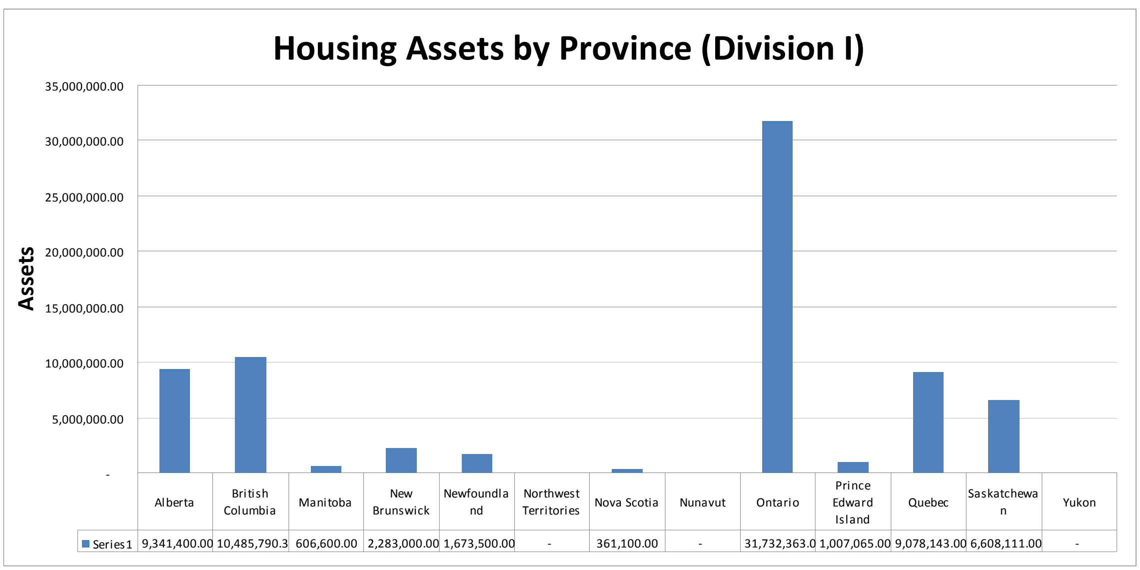


[70] Due to a limitation of time and resources.

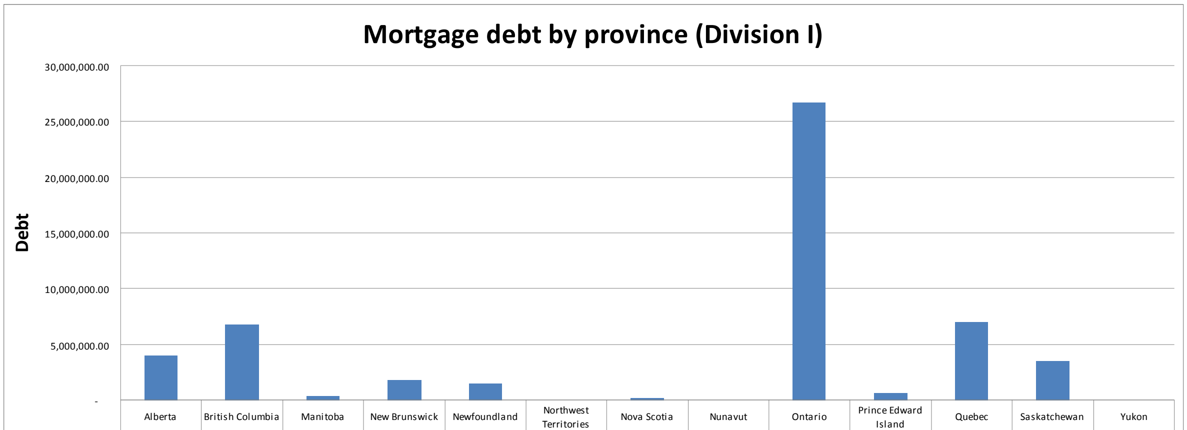
Graph 14 Mortgage Debt by Province, Division II Consumer (unadjusted)



Graph 15 Housing Assets by Province, Division I (unadjusted)



Graph 16 Mortgage Debt by Province, Division I (unadjusted)



	Alberta	British Columbia	Manitoba	New Brunswick	Newfoundland	Northwest Territories	Nova Scotia	Nunavut	Ontario	Prince Edward Island	Quebec	Saskatchewan	Yukon
Series1	4,046,973.37	6,825,810.95	371,804.00	1,862,437.00	1,548,080.30	-	196,000.00	-	26,675,298.61	624,027.00	7,044,694.43	3,488,422.13	-

It is the value of the equity in housing, combined with the provincial exemption rate that may be a significant driver towards a particular insolvency process. However, the data would have to be analyzed in the context of median and mean amounts and the amount of exemptions by province before meaningful conclusions could be drawn.

The exemptions for equity in homes vary considerably in the provinces and territories in Canada, the amounts varying from no exemption to an exemption of $40,000 in Alberta. In October 2005, the Canadian Association of Insolvency and Restructuring Professionals, in its submission to the government on legislative reform, highlighted the wide discrepancies in exemptions for equity in homes, observing that for Ontario, Québec, New Brunswick, PEI and Nova Scotia, there is no exemption at all.[71] In the Yukon, NWT and Nunavut, the exemption is $3,000; and in Newfoundland and Labrador, it is $10,000. For British Columbia, the exemption is $12,000 in the Capital Regional District or Greater Vancouver Regional District and $9,000 for the rest of the province. In Saskatchewan, the exemption is $32,000; and in Alberta the exemption is $40,000. In Manitoba, it is the residence or home, not held in joint tenancy or tenancy in common, of any debtor other than a farmer, where the value does not exceed $2,500, or where held in joint tenancy or tenancy in common, the value of interest of the debtor does not exceed $1,500.[72]

If one considers these regional differences in the context of the above graphs, it is evident that in jurisdictions where there is no exemption for equity, a significant factor in opting for a proposal may be the equity in the home. In Ontario, for example, the graphs indicate that there is considerable equity in homes of both Division I and Division II consumer debtors.

Graphs 17 and 18 below, providing data on the value of housing assets and mortgage debt for bankrupt consumers illustrates that in jurisdictions where there is no exemption, the bankrupt may not have much, if any, equity to protect, whereas in jurisdictions with exemptions, it appears that bankruptcy may be an option, where the bankrupt able to protect some equity in the home.[73]

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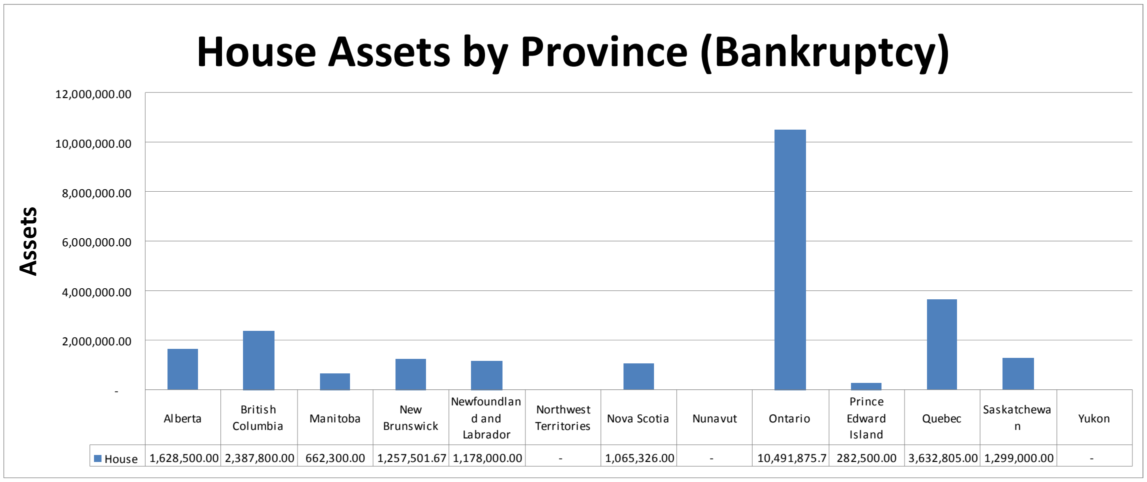
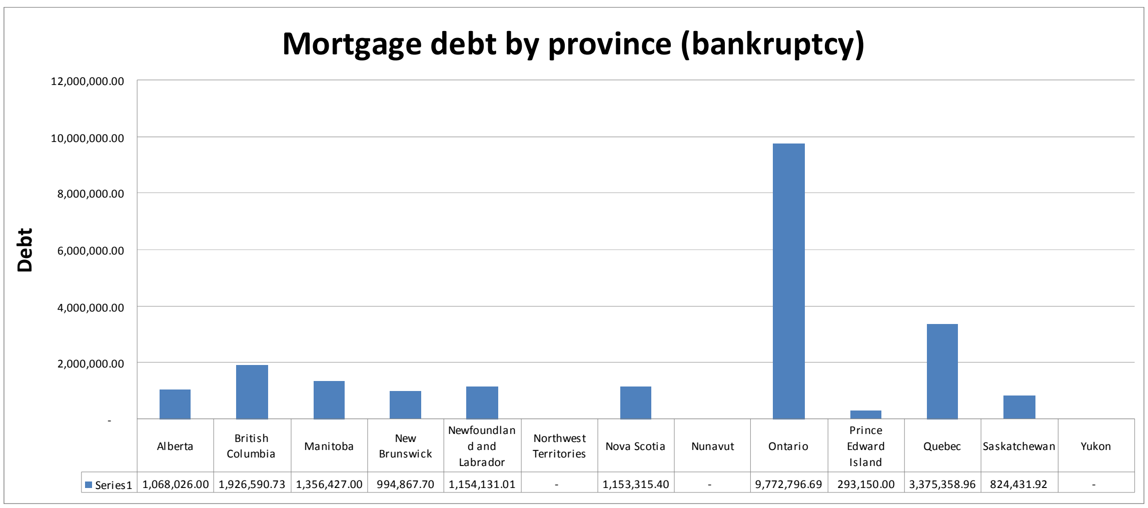
[71] Canadian Association of Insolvency and Restructuring Professionals, Submission on Proposed Personal Insolvency Amendments under Bill C-55 to the House of Commons Standing Committee on Industry, Natural Resources, Science and Technology, October 21, 2005, http://www.cairp.ca/pdf/Bill%20C-55%20Personal%20Submission.pdf last accessed May 25, 2008.
[72] *Ibid.*
[73] As noted above, further analysis is required of the data before any meaningful conclusions can be drawn.

Graph 17 Housing Assets by Province, Consumer Bankruptcy (unadjusted)



Graph 18 Mortgage Debt by Province, Consumer Bankruptcy (unadjusted)



It also merits note that in addition to houses, ownership of land, cottages and motor vehicles are also significant assets that debtors are seeking to protect by opting for a proposal proceeding, as indicated by Tables 2, 4, and 6 above, although, the amount of equity in those assets is difficult to determine from the data as collected by the OSB. Motor vehicles are exempted in a number of provinces, to a specified amount, either explicitly or as a tool of trade where they are needed in the employment of the bankrupt.

3. Is credit card debt a factor in consumer insolvency in Canada?

The data indicate that credit card debt is a significant factor in consumer insolvency; however, other than the dollar amount of such debt in Division I proposals, there is not really a distinction in the amount of credit card debt between Division II proposal debtors and bankrupts, as illustrated by the summary below. Credit card debt as a percentage of total liabilities is relatively consistent across data sets, between 14% and 18% of all liabilities. Credit card debt as percentage of total liabilities was 18% for Division II consumer proposal debtors; 15% for Division II individual business debtors; 14% for Division I consumer debtors and 17% for consumer bankrupts.

Similarly, the mean and median amount of credit card debt, while a significant amount of debt in terms of cause of insolvency, does not vary greatly as between bankrupts and Division II proposal debtors. In contrast, Division I proposal debtors have more than double the mean and median amount of credit card debt.

Amount owed under bank-issued credit cards

	Mean	Median
Division II consumer	$ 12,419	$ 9,045
Division II business	$ 14,090	$ 9,911
Division I	$ 33,660	$22,762
Bankruptcy	$ 14,916	$ 8,353

There is also significant credit card debt from non-bank credit cards, such as those offered by retailers, which has also contributed to the financial distress of these debtors:

Amount owed under non-bank issued credit cards

	Mean	Median
Division II consumer	$ 7,222	$ 4,884
Division II business	$ 9,179	$ 5,843
Division I	$ 15,969	$ 8,387
Bankruptcy	$ 8,385	$ 4,502

When taken together with bank-issued credit cards, there is some indication that debtors have multiple credit cards and incur substantial liability on those cards before filing insolvency proceedings. However, as between bankruptcy and Division II proposals, the median amount of debt does not seem to be a factor driving choice of proceeding as the amounts are similar.

Credit card debt carries high interest rates. Moreover, neither incurring the debt nor paying it is subject to rigorous parameters that assist debtors in managing their finances. For example, a mortgage payment or payment on a movable such as an appliance are debts for a fixed amount, payable at lower interest rates over a fixed period of time. Failure to make the specified payments each month or other specified period results in default of the loan, and can give rise to rapid enforcement action. In contrast, credit card debt can quickly escalate, is owed at much higher interest rates that can rapidly compound financial distress, and the lack of a defined payment plan, other than a minimum payment, means that consumer debtors are not encouraged to pay these debts first, leading to longer term financial distress. A future area of research would be to determine the extent to which these differences in type of debt and repayment terms are a contributing factor to consumer financial distress, the capacity to manage debt, and the potential for economic rehabilitation of individual debtors.

4. Are bank loans a factor in consumer insolvency in Canada?

Here again, it is clear that bank loans, other than mortgages on real property, are a significant source of debt. While the amount of bank loan debt varies across cohorts, as a percentage of total liabilities, there is consistency across all groups. Similarly, the total number of debtors that have bank loans, excluding mortgages on real property, is fairly consistent across all cohorts.

For Division II consumer proposal debtors, bank loans comprised 13% of total liabilities and 67% of all these debtors had bank loans; for Division II business proposal debtors, bank loans comprised 12% of total liabilities and 73% of all these debtors had bank loans; for Division I proposal debtors, bank loans comprised 14% of total liabilities and 71% of all these debtors had bank loans; and for bankrupts, bank loans comprised 15% of total liabilities and 61% of all these debtors had bank loans

However, the amount of bank loan debt varies across cohort, as indicated below:

Amount owed under bank loans (excluding mortgages)

	Mean	Median
Division II consumer	$ 16,605	$ 13,218
Division II business	$ 22,263	$ 18,192
Division I	$ 51,361	$ 35,467
Bankruptcy	$ 23,478	$ 14,137

Hence, Division I proposal debtors had more than double the mean and median amount of bank loans. Bankrupts had just under 1,000 CAD more median bank loans than Division II consumers and less than Division II business proposal debtors. While bank loans are a contributing cause of insolvency, there is no evidence in this study to suggest that they influence choice of proceeding.

As noted above, some trustees have attributed the high amount of unsecured bank loan debt to the introduction of on-line credit applications and approvals, increasing the ease with which debtors acquire such loans. This amount represents the greatest amount of median debt after mortgage debt, but about the same median as credit card debt owed when credit card debt of all types are tallied. The data did not indicate whether the bank loans pre-date credit card debt, coincide with acquisition of credit card debt, or were taken out as consolidating loans once credit card debt became unmanageable. Further study of this issue would be helpful to discerning how particular combinations of debt arrangements lead to financial distress.

Another issue that the data set identified for further research was the intersection between type of debt, for example bank loan or credit card debt, and age. The facility with which debtors can acquire particular kinds of debt may be a significant contributing factor; however, the information provided for this study did not offer these data.

5. Are finance company loans a factor in consumer insolvency in Canada?

Finance company loans comprise a smaller percentage of total liabilities than credit card debt or bank loans across all cohorts, 6% of total liabilities for Division II consumer, Division II business and Division I proposals and 7% for bankrupts. However, a significant number of debtors hold such loans: 44% of all Division II consumer debtors; 57% of all Division II business debtors; 43% of all Division I debtors; and 45% of all bankrupts. The mean and medium for all groups are set out below:

Amount owed under finance company loans

	Mean	Median
Division II consumer	$ 11,380	$ 9,000
Division II business	$ 13,231	$ 10,000
Division I	$ 36,965	$ 16,000
Bankruptcy	$ 14,723	$ 9,000

Division I debtors again have significantly higher mean and median amounts owing under finance company loans. There are more consistent amounts across the three other cohorts, particularly the median amount.

Trustees have reported that finance company loans are often consolidating loans whereby debtors get credit card debt consolidated, and that this effort to control debt is frequently undertaken when consumer debtors experience financial distress, but often well before any insolvency filing. Hence, some portion of these amounts may reflect old credit card debt.

The OSB advises that this category also captures a number of pay day loans, although several other categories catch pay day loans as well. While the introduction of payday loans has raised a number of issues in consumer insolvencies, particularly in respect of service and interest charges, and a potential cycle of increasing debt through multiple rollover loans, the OSB data on sources of debt does not precisely capture pay day loans as they are scattered across several categories of OSB data, including finance company debt.[74] Such loans require further study, particularly in respect of the extent to which they contribute to consumer insolvency. As noted earlier, one study has found that 25% of insolvent consumer debtors owed more than 25% of their monthly income to payday lenders.[75] Only after there is a clearer empirical picture of the alternative financing market will there be data on which to consider reform of the consumer lending system.

6. Are there differences in the amount of tax owing between proposal debtors and bankrupts?

Tax liability is not a critical cause of filing for Division II proposal debtors. While 31% of all Division II consumer proposal debtors and 40% of all Division II business proposal debtors had some tax debt on filing, it comprised only 2% and 1% respectively of total liabilities. For bankrupts, 37% of bankrupts had outstanding tax debt on filing, comprising 8% of their total liabilities.

In contrast, for Division I debtors, almost one half, 48% had outstanding tax liabilities, amounting to 17% of their total liabilities, representing a significant amount of their debt. The median amount of tax debt for Division I proposal debtors was ten times that of the other cohorts:

Amount owed for outstanding taxes

	Mean	Median
Division II consumer	$ 6,181	$ 2,000
Division II business	$ 4,428	$ 1,964
Division I	$ 91,627	$ 30,300
Bankruptcy	$ 22,334	$ 3,204

Hence, median amounts owed for tax liabilities at the time of filing were modest for Division II proposals and bankruptcy, but significant for Division I proposals.

The government enacted legislative reform to address issues arising from what it viewed as high tax debtors using bankruptcy proceedings to avoid debt tax. Section 172.1 of the *BIA* introduced a new procedure in 2008 for discharging bankrupts with high personal income tax debt. It is aimed at those individuals who have an outstanding personal income tax debt (federal and/or provincial) in excess of $200,000, including principal, interest and penalties, where the amount owing represents 75% or more of the bankrupt's total unsecured proven claims. The new section was designed to ensure that bankrupts with significant personal income tax debt do not misuse the insolvency system by paying their other creditors to the exclusion of the government. These

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[74] However, see the research of Ruth Berry and Karen Duncan, *supra*, note 24, in terms of data in relation to pay day loans.
[75] *Ibid.*

bankrupts will not be eligible for an automatic discharge and an application for discharge will be required. The onus will be on the debtor to justify any relief to be granted by the court. The legislation sets out the timing of bankruptcy relief and the types of orders that the court may make on the hearing of a bankrupt's application for discharge. The options available to the court include: refusing the discharge; suspending the discharge; requiring the bankrupt to perform any acts, pay any moneys, consent to any judgements or comply with any other terms that the court may direct. There are new statutory provisions setting out the factors the court shall take into account when making a decision with respect to the bankrupt's discharge, including: the bankrupt's circumstances at the time the personal income tax debt was incurred; the efforts made by the bankrupt to pay the personal income tax; whether the bankrupt paid other debts while failing to make reasonable efforts to pay the personal income tax debt; and the bankrupt's financial prospects for the future.[76] The onus is on the bankrupt to justify the relief requested of the court. The court has authority to modify the order if the bankrupt satisfies the court that there is no reasonable probability that he or she will be in a position to comply with the terms of the order.

Interestingly, the 5,773 cohort in this study did not identify bankrupts as having tax debt of an amount that would bring them within these new provisions; rather, the mean and median were higher for Division I proposal debtors than bankrupts. These new provisions, therefore, may be aimed at a very small segment of the bankrupt population.

7. Are student loans a factor in consumer insolvency in Canada?

Overall, student loans are not a significant factor in either proposals or bankruptcies, as indicated by the figures below. This insignificance was likely due to the fact that student loans were not discharged in bankruptcy for ten years and hence there is no incentive on creditors to compromise these loans in a proposal. However, the median amounts owed were between 7,000 CAD and 11,300 CAD at the time of filing, suggesting that while not a primary cause of insolvency, the outstanding amounts of these loans were a contributing factor to the financial distress.

The importance of this type of liability may or may not change with the softening of the length of period from ten to seven years and the hardship exemption to five year. Section 178(1)(g) of the *BIA* was amended effective July 7, 2008 to reduce the waiting period from ten years to seven years and section 178(1.1) was amended to reduce the waiting period before a hardship application could be made from ten years to five years. Ten years was generally thought to be too long a period before former students could apply for relief from the provisions. Even with these amendments, there will be a considerable period of time before student loans can be forgiven in the fresh-start programs.

Student loans as percentage of total liabilities

Division II consumer	1%	(31% of all debtors)
Division II business	0.7%	(8% of all debtors)
Division I	0.6%	(8% of all debtors)
Bankruptcy	1.4%	(13% of all debtors)

Amount owed under student loans

	Mean	Median
Division II consumer	$ 11,374	$ 7,547
Division II business	$ 10,396	$ 7,367
Division I	$ 20,405	$ 11,383

[76] Section 172.1(4), *BIA*.

Bankruptcy	$ 11,039	$ 8,500

8. What impact does the different timing period for rehabilitating one's credit rating have on the decision to make a proposal or not?

The data sets in this project did not offer any indication one way or another as to the answer to this question. However, in the interviews with trustees, it seemed apparent that all other factors being equal, the timeliness of bankruptcy discharge, particularly for first time bankrupts, was a factor in the choice of proceeding. The availability of discharge and fresh start in credit rating rehabilitation at nine months, compared with a payment period of three to five years, during which time a debtor's credit rating does not begin to rehabilitate, does influence choice of proceeding. This choice based on timing period does not bear out where there are non-exempt assets to protect, which was a principal reason for opting for a proposal.

The other timing issue that was identified, but the study was not able to explore, was an issue in respect of timing of filing an insolvency proceeding. One possible explanation for the growth in credit card debt and other loans is that individual debtors are waiting for longer periods before accessing the formal insolvency system. Only a broad based national longitudinal study would be able to discern whether or not this lag is a broad based phenomenon. Interestingly, there has been considerable scholarship on the problems of deferred liquidation for business insolvency, but little, if any, research on how deferred filing may harm consumer debtors through further erosion of their assets and deepening debt before they access the rehabilitation provisions of the *BIA.* Since this information was anecdotal, further research, through direct survey of consumer debtors, would shed greater light on this question.

9. Are there sociological reasons why consumer debtors may opt for proposals rather than bankruptcy, in terms of continuing stigma associated with bankruptcy?

It is evident, again from the trustee interviews, that proposals are viewed with less social stigma than bankruptcy, particularly in smaller communities. Here again, the need for further research, directly with consumer debtors, would assist in understanding choice of proceeding. There is evidence in US studies to suggest that individuals continue to hide the circumstances of their financial distress and that they believe there is considerable negative sentiment against debtors that seek recourse to bankruptcy procedures.[77] The study of elderly bankrupts in Canada found similar evidence that there continues to be considerable stigma associated with making an assignment in bankruptcy.[78]

10. Will current proposed amendments encourage more debtors to undertake proposals?

Many of the proposal provisions have remained intact with the proposed legislative reform. However, there are two significant amendments that should encourage more successful proposals.

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[77] Deborah Thorne and Leon Anderson, "Managing the Stigma of Personal Bankruptcy" (2006) 39 Soc. Focus 77 at 80-97.

[78] Sarra, *supra*, note 7. Another research question was whether enhanced counselling at the commencement of the process had an impact on choice of insolvency proceeding. The data available for this study was not able to answer this research question. The anecdotal information from trustees was varied and did not point in any particular direction. An area of future research would be to conduct some survey and other study to discern the impact of counselling.

First, the proposed amendment to the definition of "consumer debtor" will increase the amount of debts that an individual may have to be eligible to make a Division II consumer proposal from $75,000 to $250,000. The previous indebtedness ceiling of $75,000 was likely too low and forced many self-employed individuals and higher-income debtors to make a more costly and more complicated Division I proposal, in turn, reducing recovery for creditors. In addition, failure of a Division I proposal results in an automatic bankruptcy, whereas failure of a consumer proposal does not. The increase in the indebtedness ceiling was aimed at making the simpler and more cost-effective consumer proposal scheme available to a greater number of people and thus should encourage more proposals.

The proposed amendments should also assist with the failure rate of proposals. As discussed above, the second greatest number of proposals fail when they are deemed annulled after some period of making payments under the proposal.

Under the new amendments, there is a new procedure to be able to revive a deemed annulled proposal. Section 66.31 sets out the rules by which a deemed annulled consumer proposal can be revived. The provisions provide the administrator with the discretion to revive a consumer proposal that has been deemed annulled under subsection 66.31(1). Previously, there was no way to revive a consumer proposal that was in default. The new section allows an administrator to rectify the default by providing notice to the creditors. It assists in situations where the debtor faces a temporary problem meeting payments, for example, due to illness or temporary unemployment, but otherwise is making good faith efforts to comply with the terms of the proposal. Creditors have the opportunity to object to the revival. The creditors' rights to the amount of their claims less any dividends received are revived between the day on which the proposal is deemed to be annulled and the day on which it is revived, a period of 45 days.

Under ss. 66.31(6), in the case of a deemed annulment of a consumer proposal made by a person other than a bankrupt, if the administrator considers it appropriate to do so in the circumstances, it may, with notice to the official receiver, send to the creditors, within 30 days,[79] , after the day on which the consumer proposal was deemed annulled, a notice informing them that the consumer proposal will be automatically revived 60 days after the day on which it was deemed to be annulled,[80] unless a creditor with the administrator files a notice of objection to the revival. If no notice of objection is filed within the time period, the consumer proposal is automatically revived on the expiry of that period.[81] Under s. 66.31(8), if a notice of objection is filed, the administrator is to send, without delay, to the official receiver and to each creditor a notice informing them that the consumer proposal is not going to be automatically revived on the expiry of that period.

Pursuant to s. 66.31(9), the administrator may at any time apply to the court, with notice to the official receiver and the creditors, for an order reviving any consumer proposal of a consumer debtor who is not a bankrupt that was deemed to be annulled, and the court, if it considers it appropriate to do so in the circumstances, may make an order reviving the consumer proposal, on any terms that the court considers appropriate.

The revival provisions should make a significant improvement in the current failure rate of proposals, as it allows the administrator, and in some instances the court, to relieve against unforeseen obstacles that temporarily hindered the debtor's ability to meet the conditions of the proposal.

However, the above discussion assumes that individual debtors have the income to undertake a proposal and payments to creditors. The reforms do not address a significant underlying cause of insolvency, specifically, inadequate income, job loss and lack of skills training for opportunities

[79] Or any other number of days that is prescribed.
[80] Or any other number of days that is prescribed.
[81] Proposed s. 66.31(7).

in the changing economic landscape. While these issues are broader public policy issues, it is important to take note of the limitations of insolvency law to address some of the most fundamental problems facing individual debtors.

X. Conclusion

The data analysed in this study have both shed some light on consumer insolvency proceedings and raised further questions for research, as discussed throughout this paper. Canada has been undergoing insolvency reform for almost five years. Included in the proposed reforms are amendments to consumer insolvency legislation, aimed in part in encouraging a greater number of proposals. This research project supports the continuing reform process in trying to measure some of the factors that currently contribute to consumer insolvency and choice of relief. It can be used as a baseline for future study, once the amendments are fully proclaimed in force.

The study has identified some data points that should be better collected, which could enhance the ability to discern trends, including measurement of income to debt as another indicator of financial distress; data on how long individuals struggle under their debt load before they access remedies under the *BIA* and whether that length of time contributes somehow to a deepening financial distress that is then more difficult to recover from. Most important, is the need for broad based multidisciplinary longitudinal studies that can measure the impact of policy choices over time and create a fuller picture of the obstacles facing consumer debtors. Only then will public policy be truly responsive to the needs of both consumer debtors and their creditors.