REPEAT BANKRUPTCIES AND THE INTEGRITY OF THE CANADIAN BANKRUPTCY PROCESS

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> "In my view, a third bankruptcy is one too many."
> *Re Hardy* (1979), 30 C.B.R. (N.S.) 95 (Ont. S.C.), at para. 3.

> "And so a third discharge merely prepares the way for a fourth bankruptcy."
> *Re Resnick* (1990), 80 C.B.R. (N.S.) 223 (Ont. S.C.), at para. 4.

In 1965, Mr. Rogers filed for bankruptcy. It was not to be his last. Over 25 years, Rogers worked for a car dealership in Quebec. His career was rather unremarkable except that Rogers failed to remit proper amounts of income tax. Rogers was not bothered by the frequent tax arrears. He found a convenient way to deal with his taxes. Drawing on the 1965 bankruptcy experience, he made assignments in bankruptcy in 1975, 1979, 1984 and again in 1987.[1]

The court found that Rogers considered the Bankruptcy Act[2] to be "a convenient means" to "clear away the income tax arrears."[3]

> [N]othing useful would be gained by granting him a discharge, with or without conditions. He has shown repeatedly that he is unable to organize his affairs in such a way as to fulfill his fiscal responsibilities to his fellow citizens. He makes a mockery of the law and

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[1] *Rogers (Trustee of) v. Canada (AG)* (1989), 77 C.B.R. (N.S.) 315 (Que. Sup. Ct.), at para. 5.

[2] R.S.C. 1985, c. B-3.

[3] *Rogers*, *supra*, footnote 1, at para. 8.

> probably cannot be rehabilitated. At the hearing … he was asked what he proposed to do so as to avoid a sixth bankruptcy, if he were to be discharged from his fifth. No satisfactory answer was forthcoming.[4]

The court refused to grant Rogers a discharge since he had "severely tested" "the integrity of the bankruptcy process."[5] The case demonstrates the tension between rehabilitation, the fundamental goal of the bankruptcy discharge, and the integrity of the bankruptcy process.

While fifth time bankruptcies may be infrequent,[6] repeat bankruptcies are not. However, there have been no comprehensive studies of second, third, fourth and fifth time bankruptcies in Canada from a policy perspective or an empirical basis. The paper will combine recent empirical data from the Office of the Superintendent of Bankruptcy (OSB) with an analysis of case law on repeat bankrupts.

Rehabilitation has been a traditional and important theme in bankruptcy discharge proceedings. First time bankrupts are able to obtain an automatic discharge as early as 9 months after the date of bankruptcy.[7] However, Canadian bankruptcy law has traditionally taken the position that a prior bankruptcy will preclude an order of an absolute discharge.[8] Debtors with three or more bankruptcies are not entitled to an absolute discharge. In such a situation, the court must refuse, suspend or grant a

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[4] *Ibid* at para. 14.

[5] *Ibid* at para. 8.

[6] A review of reported case law on the subject only revealed one fifth time bankruptcy. See discussion below in Part V.

[7] Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, s. 168.1(1)(a)(i) [hereafter BIA].

[8] BIA, *supra*, footnote 7, at ss. 172, 173(1)(j). See Edouard Martel, "The Debtor's Discharge from Bankruptcy" (1971), 17:4 McGill L.J. 718, at p. 738. This provision can be traced back to the Bankruptcy Act of 1919. See Bankruptcy Act of 1919, S.C. 1919, c. 36, ss. 58-59.

conditional order of discharge.[9] Under recent reforms, second time bankrupts must wait either 24 or 36 months before being entitled to an automatic discharge.[10] The different treatment of repeat bankrupts suggests that there are other policy objectives at play beyond rehabilitation. Where there is a repeat bankruptcy, the preservation of the integrity of the Canadian bankruptcy process may well override the debtor rehabilitation rationale.[11] The integrity of the bankruptcy regime involves the protection of creditors and the public through suspensions, conditional discharges or refusals of discharge.

Part I of the paper relies upon recent OSB statistics to demonstrate the extent of the multiple bankruptcy problem. Part II examines the rehabilitation rationale in light of repeat bankruptcies. Part III considers the 2009 amendments to the BIA that deal with second time bankrupts. Part IV discusses third time bankrupts while Part V examines fourth and fifth time bankruptcies. Part VI asks whether the mandatory counselling requirements in the BIA are working to solve the problem of repeat bankruptcies. The paper concludes with Part VII which considers a possible solutions to the problem of repeat bankruptcies.

I. THE EMERGENCE OF THE REPEAT BANKRUPTCY PROBLEM AND RECENT STATISTICS

The 1980s marked a key turning point in the growth in the number of repeat bankruptcies in Canada. One source suggests that the repeat bankruptcy rate was limited

[9] BIA, *ibid*. These new provisions will be considered in a separate section.

[10] *Ibid*., at ss. 168.1(1)(b)(i),-(ii).

[11] *Re Pitre* (2009), 60 C.B.R. (5th) 108 (Sask. Q.B.), at para. 26. See also Frank Bennett, *Bennett on Bankruptcy*, 14th ed. (Toronto: CCH, 2012), at p. 536.

to about 2-3% in the late 1970s.[12] Indeed, there are only seven instances of reported cases involving a repeat bankruptcy that predate 1979.[13] The Audit and Evaluation Branch (AEB) 2013 report, *Evaluation of Mandatory Counselling*, notes that while repeat bankruptcies were "unusual in the 1970s" the rate grew to 10-12% in the 1980s "because of easier access to credit" and "the emergence of complex financial products."[14] In 2002, the Personal Insolvency Task Force estimated a 10% repeat filing rate.[15] While there have been numerous empirical studies on repeat bankruptcies under the US Bankruptcy Code,[16] there have been a few Canadian studies devoted to the specific issue of repeat bankruptcy.[17] Furthermore, there have been no Canadian studies that have assessed second, third, fourth and fifth time bankruptcies as separate categories.

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[12] George F. Redling, "Implementation Issues Regarding Bill C-22" (Ottawa: Department of Consumer and Corporate Affairs, 1992), at para. 12. See also Wally Clare, "Repeat Bankruptcies of Consumer Debtors" (1990),10:6-8 Insolvency Bulletin 201.

[13] *Re Beck* (1925), 7 C.B.R. 556 (Que. Sup. Ct.); *Re Cruickshanks* (1936), 18 C.B.R. 57 (N.S.S.C.); *Leger v. Hayes* (1938), 20 C.B.R. 19 (Que. Sup. Ct.); *Re Handler (Good Wear Shoe Co)* (1946), 27 C.B.R. 108 (Ont. S.C.); *Re Volkman* (1971), 18 C.B.R. (N.S.) 67 (Que. Sup. Ct.); *Re Cameron* (1972), 18 C.B.R. (N.S.) 99 (Que. Sup. Ct.); *Laramee v. Diamond* (1966), 10 C.B.R. (N.S.) 182 (Que. Sup. Ct.).

[14] Industry Canada, *Evaluation of Mandatory Counselling* (Audit and Evaluation Branch, 2013), at p. 1 [hereafter AEB Report]. Clare also identifies a 10% rate in 1990. See Clare, *supra*, footnote 12. J.M. Ferron further identifies a 10% rate in 1988. J.M. Ferron, "A Bankruptcy Policy" (1990), 78 C.B.R. (N.S.) 28, at para. 18.

[15] *Personal Insolvency Task Force Final Report* (2002), at p. 49, online: <http://strategis.ic.gc.ca/eic/site/bsf-osb.nsf/vwapj/pitf.pdf/$FILE/pitf.pdf> [hereafter PITF Report].

[16] See e.g., Lance Miller & Michelle M. Miller, "Repeat Filers Under the BAPCPA: A Legal and Economic Analysis" [2008], Norton Ann Survey of Bankr. L. 509, at p. 509; J.M. Lown & B. Llewellyn, "Repeat Bankruptcy Filers" (2004), 19 Papers of the Western Family Economics Association, at p. 37. J. Golmant & T. Ulrich, "Bankruptcy Repeat Filings" (2006), 14 A.B.I. L. Rev. 169, at p. 170; Jean Lown, "Serial Bankruptcy Filers No Problem" (2007), A.B.I. J. 36, at p. 36; Paul B. Lewis, "The Repeat Bankruptcy Filer: Some Economic Considerations" (2000), 10 New Directions in Bankruptcy 18, at p. 18.

[17] Clare, *supra*, footnote 12; Shelley Antel, *A Demographic and Financial Profile of Second Time Bankrupts* (M.Sc. Thesis, University of Manitoba, 1991) [unpublished]; Ian D.C. Ramsay, "Individual Bankruptcy: Preliminary Findings of a Socio-Legal Analysis" (1999), 37:1-2 Osgoode Hall L.J. 15; Judith K. Strand, Tahira K. Hira & Richard B. Carter, "Repeat Consumer Bankruptcy: A Comparative Analysis with One-time Petitioners in the United States and Canada" (Paper delivered at the AFCPE National Conference, Nashville, Tennessee, 8-12 November 1994).

Statistics from the Office of the Superintendent of Bankruptcy reveal that the Personal Insolvency Task Force's 2002 estimate of a 10% repeat filing rate is now out of date. The most recent 2012 statistics indicate that the Canadian repeat filing rate is 16.11% for consumer bankruptcies. This rate has increased from 2010 to 2012.[18]

Percentage of Total Bankruptcies Filed by Consumers with One or More Previous Bankruptcies:[19]

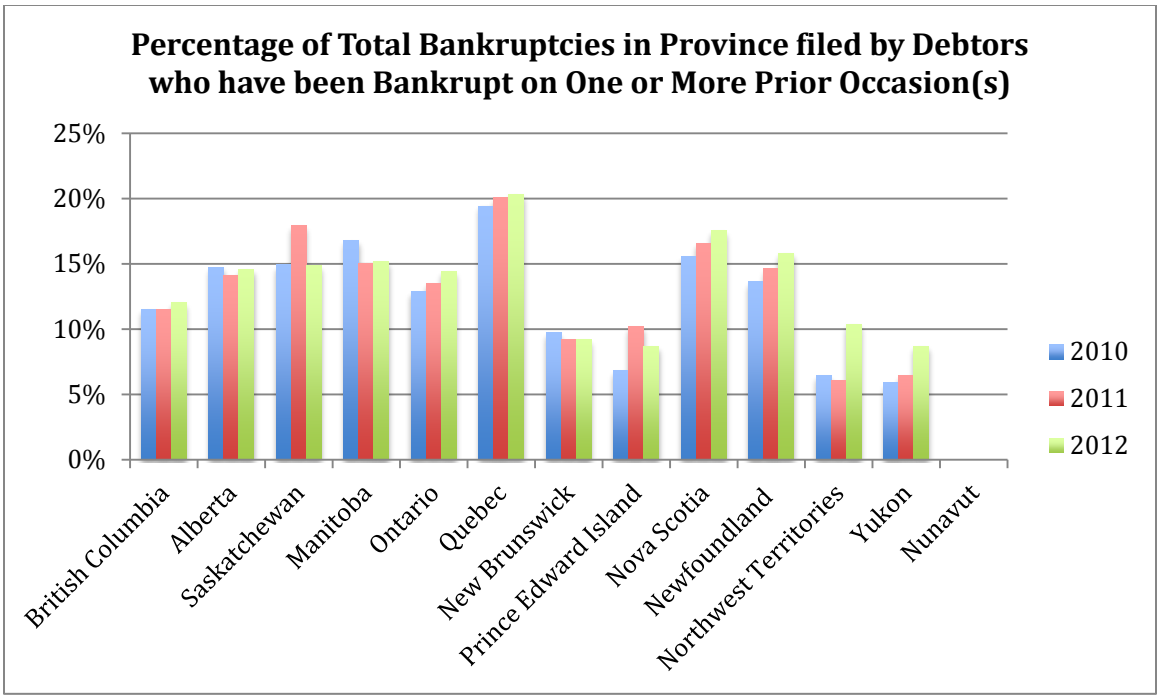
Year	% of Total Consumer Bankruptcies
2010	14.99%
2011	15.57%
2012	16.11%

Provincial statistics reveal that there is a variance in repeat filing rates across the country.[20]

[18] If the repeat filing rate takes into account debtors with a prior bankruptcy or a prior consumer proposal the repeat rate is higher. This rate stands at 20.5% for 2011-2012. AEB Report, *supra*, footnote 14, at p. 10.

[19] Office of the Superintendent of Bankruptcy, Draft Report BKHQRA-2157 (Revised), 28 March 2013 [hereafter OSB Statistics #1]. The number of repeat consumer bankruptcies are determined based on information provided in the Estate Information Summary (EIS) form filed by the trustee in bankruptcy. This information is captured electronically when the estate is e-filed. OSB analysis indicates that since September 2009, over 99% of estates are e-filed. Occasionally when estates are filed jointly, inconsistencies can occur when the EIS information is captured electronically in the database. This represents a very small percentage of the total number of consumer bankruptcies filed.

[20] Office of the Superintendent of Bankruptcy, Draft Report BKHQRA-2308, 20 August 2013 [hereafter OSB Statistics # 2]. Provincial statistics do not provide a regional breakdown or an urban rural analysis. See Janis P. Sarra, "Economic Rehabilitation: Understanding the Growth in Consumer Proposals" (2008), online: Insolvency Research Initiative, Office of the Superintendent of Bankruptcy Canada, at pp. 26-28 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1399610>.



Summary of OSB Statistics 2010-2012[21]

2010	Number of Filings	% of total filed
All consumer bankruptcies	92694	100%
One or more previous bankruptcies	13897	14.99%
2nd time filing bankruptcy	12773	13.78%
3rd time filing bankruptcy	1058	1.14%
4th time filing bankruptcy	59	0.06%
5th time filing bankruptcy	7	0.01%

2011	Number of Filings	% of total filed
All consumer bankruptcies	77993	100%
One or more previous bankruptcies	12145	15.57%
2nd time filing bankruptcy	11045	14.16%
3rd time filing bankruptcy	1010	1.29%
4th time filing bankruptcy	84	0.11%
5th time filing bankruptcy	6	0.01%

[21] OSB Statistics #1, *supra*, footnote 19.

2012	Number of Filings	% of total filed
All consumer bankruptcies	71495	100%
One or more previous bankruptcies	11518	16.11%
2nd time filing bankruptcy	10456	14.63%
3rd time filing bankruptcy	977	1.37%
4th time filing bankruptcy	74	0.10%
5th time filing bankruptcy	9	0.01

II. THE LEGISLATIVE FRAMEWORK AND COMPETING POLICY OBJECTIVES

1. The 2009 Amendments

Prior to the 2009 amendments, the BIA treated all repeat bankrupts in the same way. In the event of any repeat bankruptcy, a court could not award an absolute discharge. All repeat bankrupts faced the prospect of a court refusing the discharge or ordering a suspended or conditional discharge.[22] The 2009 amendments introduced a significant change with respect to the treatment of second time bankruptcies. The amendments to the BIA have extended the right of an automatic discharge[23] to second time bankrupts after waiting a period of either 24 or 36 months.[24] Second time bankrupts without surplus income are now entitled to an automatic discharge 24 months after the date of bankruptcy (unless there is an opposition). Second time bankrupts with surplus income may obtain an automatic discharge 36 months after the date of bankruptcy.

[22] BIA, *supra*, footnote 7, at ss. 173(1)(j), 172(2). Section 173(1)(j) can be traced back to s. 59 of the Bankruptcy Act of 1919. See Bankruptcy Act of 1919, S.C., c. 36, s. 59. This was based on the U.K. Bankruptcy Act of 1883. See Bankruptcy Act, 1883 (U.K.), c. 52, s. 28(3)(g). See U.K., H.C., Parliamentary Debates, vol. 277 col. 816 at 831-32 (19 March 1883) (Mr. Chamberlain).

[23] First time bankrupts without surplus income are entitled to an automatic discharge 9 months after the date of bankruptcy. See BIA, *supra*, footnote 7, s. 168.1(1)(a)(i). First time bankrupts with surplus income must wait 21 months before obtaining an automatic discharge. See BIA, *supra*, footnote 7, s. 168.1(1)(a)(ii). Stephanie Ben-Ishai, "Discharge" in Stephanie Ben-Ishai & Anthony Duggan, *Canadian Bankruptcy and Insolvency Law: Bill C-55, Statute c.47 and Beyond* (Toronto, LexisNexis, 2007), at p. 360.

[24] BIA, *supra*, footnote 7, s. 168.1(1)(b). See Ben-Ishai, *ibid* at p. 362.

The amendments can be traced back to the recommendations of the 2002 Personal Insolvency Task Force (PITF) and the 2003 Report of the Standing Senate Committee on Banking, Trade and Commerce.[25] The PITF recommended an automatic discharge for second time bankrupts with a 24 month waiting period. The waiting period was suggested so as to provide "a discernible and transparent consequence to individuals using the bankruptcy system for a second time"[26] and to "provide for greater consistency of sanction for second-time bankrupts where no opposition to discharge [was] filed."[27] The government's clause-by-clause analysis of Bill C-55 suggests that the new regime was designed to "streamline the bankruptcy process" [28] and eliminate court appearances in every case.[29] While creditors, the trustee or the OSB may object to the automatic discharge, the new second time bankruptcy provisions operate as a default system and set up "an administrative system without court supervision" for second time bankrupts.[30] Third, fourth and fifth time bankrupts continue to be governed by court supervision.

2. Competing Policy Objectives

[25] PITF Report, *supra*, footnote 15; Report of the Standing Senate Committee on Banking, Trade and Commerce, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (Ottawa: 2003), at p. 59.

[26] PITF Report, *ibid* at p. 49.

[27] *Ibid*.

[28] Bill C-55: clause by clause analysis, An Act to establish the *Wage Earner Protection Program Act*, to amend the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* and to make consequential amendments to other Acts at cl. 100. Online: http://www.ic.gc.ca/eic/site/cilp-pdci.nsf/eng/h_cl00790.html.

[29] *Ibid.*

[30] Bennett, *supra*, footnote 11, at p. 535.

One of the often-cited purposes of bankruptcy law is to permit the rehabilitation of the debtor "as a citizen, unfettered by past debts."[31] The bankruptcy regime thus allows an honest but unfortunate debtor to "reintegrate into the business life of the country as a useful citizen free from the crushing burden of his or her debts."[32] The Ontario Court of Appeal in *Bank of Montreal v Giannotti*[33] cited the following passage from Houlden and Morawetz's *Bankruptcy Law of Canada*: "The Act permits an honest debtor, who has been unfortunate in business, to secure a discharge so that he or she can make a fresh start and resume his or her place in the business community."[34]

The underlying assumption of rehabilitation is that the debtor will be able to make a "new start"[35] without the need to resort to bankruptcy again. The United States Supreme Court in *Local Loan Co v Hunt*[36] emphasized the nature of the fresh start:

> One of the primary purposes of the Bankruptcy Act is to 'relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.'…. This purpose of the act has been again and again emphasized by the courts as being of public as well as private interest, in that it gives to the honest but unfortunate debtor who surrenders for distribution the property which he owns at the time of bankruptcy, a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt.[37]

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[31] *Industrial Acceptance Corp v. Lalonde*, [1952] 2 S.C.R. 109, at para. 34, Estey J. See also *Vachon v. Canada (Employment & Immigration Commission)*, [1985] 2 S.C.R. 417 at para. 39, Beetz J.; *Royal Bank of Canada v. North American Life Assurance Co*, [1996] 1 S.C.R. 325, at para. 17, Gonthier J.

[32] Roderick J. Wood, *Bankruptcy and Insolvency Law*, (Toronto: Irwin Law, 2009), at p. 274. See also *Re Murray* (1971), 15 C.B.R. (N.S.) 252 (B.C.S.C.), at paras. 13-15.

[33] (2000), 51 O.R. (3d) 544 (C.A.), MacPherson J.A..

[34] *Ibid* at para. 11.

[35] *Re Newsome*, [1927] 3 D.L.R. 828, at para 11 (Ont. S.C.).

[36] 292 US 234 (1934), at p. 244.

[37] *Ibid*.

The "clear field for future effort" assumes that the debtor will be reintegrated into the economic life of society or will resume his or her place in the community without the need for another bankruptcy.

Rehabilitation often gives way when there is a repeat filing. The specific provisions in the BIA that deal with repeat bankruptcies suggest that other considerations beyond rehabilitation become relevant. In the case of multiple bankruptcies, "the Court's focus shifts from a rehabilitative one to one of concern for the integrity of the system, protection of creditors and as a brake against future assignment."[38] The British Columbia Supreme Court in *Re Willier*[39] recognized the change in policy objectives:

> By the time an individual has entered a third bankruptcy, the purpose and intent of the *Act* shifts from its remedial purpose of assisting well-intentioned but unfortunate debtors to one of protecting society, and in particular unsuspecting potential creditors. The best intentions and hopes of such bankrupts become subordinated to the need to protect others from the bankrupt's demonstrated financial incompetence, negligence, and carelessness.[40]

The competing objectives of rehabilitation and the protection of the integrity of the bankruptcy regime are difficult to reconcile. If one is to preserve the public interest or the integrity of the bankruptcy regime by refusing the discharge or by imposing a suspension or conditional order, it will be at the expense of the debtor's rehabilitation. Indeed "continued access to the bankruptcy process suggests that rehabilitation has not worked."[41] The new automatic discharge for second time bankrupts after 24 or 36 months

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[38] *Pitre*, *supra*, footnote 11, at para. 26. See also *Re Chaban* (1996), 143 Sask. R. 136 (Q.B.), at para. 7; *Marshall v. Bank of Nova Scotia* (1986), 62 C.B.R. (N.S.) 118 (B.C.C.A); *Nelson (Trustee of) v. Nelson* (1995), 33 C.B.R. (3d) 292 (Sask. Q.B.); *Re Alousis* (2000), 20 C.B.R. (4th) 169 (Ont. S.C.J.); *Re Atkin* (1987), 65 C.B.R. (N.S.) 296 (Ont. S.C.).

[39] (2005), 14 C.B.R. (5th) 130 (B.C.S.C).

[40] *Ibid* at para 12.

[41] Karen Gross, *Failure and Forgiveness: Rebalancing the Bankruptcy System*, (New Haven, CT: Yale University, 1997), at p. 110.

has however, provided a compromise in balancing the two objectives; rehabilitation and the integrity of the system. The automatic administrative discharge fulfills a rehabilitative function while the waiting period sends a signal that there is a consequence to using the bankruptcy regime for a second time. The shift from rehabilitation to the integrity of the bankruptcy regime represents a concern over the control of the moral hazard problem.

3. Moral Hazard and Repeat Bankruptcies

From an economic perspective, the bankruptcy discharge provides individual debtors with a form of consumption insurance.[42] This creates a moral hazard problem.[43] The bankruptcy discharge therefore "decreases individuals' incentives to constrain their consumption and to avoid incurring obligations that they may not be able to repay."[44] With the availability of the discharge, it is argued that debtors will be incentivized to "take on more debts and employ the fresh start benefit strategically."[45] Indeed the moral hazard problem may well be more prevalent in the event of a repeat bankruptcy. It has been argued that the moral hazard argument is "premised upon debtors possessing

[42] Anthony Duggan, "Consumer Bankruptcy in Canada and Australia: A Comparative Overview" (2006), Ann. Rev. Insol. L. 857, at p. 860 citing Michelle White, "Abuse or Protection? Economics of Bankruptcy Reform under BAPCAPA" [2007], Ill. L. Rev. 275, at p. 276. See also Giacomo Rojas Elgueta, "The Paradoxical Bankruptcy Discharge: Rereading the Common Law-Civil Law Relationship" (2013) (Available at SSRN 2298486), at pp. 37-38; Ning Zhu, "Household Consumption and Personal Bankruptcy" (2011), 40:1 J. Legal Stud. 1; Richard M. Hynes, "Optimal Bankruptcy in a Non-Optimal World" (2002), 44 B.C.L. Rev. 1, at p. 1; Michael D. Sousa, "The Principle of Consumer Utility: A Contemporary Theory of the Bankruptcy Discharge" (2009), 58 U. Kan. L. Rev. 553, at p. 608; Adam Feibelman, "Consumer Bankruptcy as Development Policy" (2009), 39 Seton Hall L. Rev. 63, at p. 92.

[43] For a definition of moral hazard see Thomas Jackson, "The Fresh Start Policy in Bankruptcy Law" (1985), 98 Harv. L. Rev. 1393, at p. 1402.

[44] Adam Feibelman, "Defining the Social Insurance Function of Consumer Bankruptcy" (2005), 13 A.B.I. L. Rev. 129, at p. 167; Richard M. Hynes, "Why (Consumer) Bankruptcy" (2004), 56 Ala. L. Rev. 121, at p. 154; Hynes, *supra*, footnote 42; Sousa, *supra*, footnote 42.

[45] Elgueta, *supra*, footnote 42; Zhu, *supra*, footnote 42.

information about the bankruptcy process and the ability to discharge debt."[46] While the moral hazard problem may well be diminished for a first time bankrupt without any detailed knowledge of the bankruptcy process[47] a repeat bankrupt may be able to draw upon his or her prior bankruptcy experience with the aim of filing a subsequent strategic bankruptcy.

Thus, the BIA seeks to avoid the moral hazard problem, establishing that "certain standards of commercial morality … must be maintained." [48] The standards of commercial morality are set out in s. 173(1) of the BIA. If any of the factors are proven, a court may not grant an absolute discharge and must either refuse, suspend or make a conditional order of discharge. [49] As Estey J. indicates in *Industrial Acceptance v. Lalonde*[50] "the discharge is, however, not a matter of right and the provisions of secs. [172] and [173] plainly indicate that in certain cases the debtor should suffer a period of probation."[51]

Thus, an absolute discharge may not be granted where the bankruptcy is brought on by "rash and hazardous speculations, by unjustifiable extravagance in living, by gambling, or by culpable neglect."[52] A prior bankruptcy or a proposal is a relevant factor

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[46] Sousa, *supra*, footnote 42, at p. 609. See also Feibelman, *supra*, footnote 42, at p. 94.

[47] Sousa, *ibid*.

[48] Wood, supra, footnote 32, at p. 275.

[49] BIA, *supra*, footnote 7, at s. 172(2).

[50] [1952] 2 S.C.R. 109.

[51] *Ibid* at para. 34.

[52] Wood, *supra*, footnote 32, at p. 275; Hynes, *supra*, footnote 44, at p. 154; Ben-Ishai, *supra*, footnote 23, at p. 359.

under s. 173(1)(j) and also breaches the BIA's standard of commercial morality. [53] It follows that a debtor who has filed for bankruptcy three or more times faces the prospect of a refusal, suspension or a conditional order. The 2009 amendments have altered the standards of commercial morality for second time bankrupts by offering an automatic discharge only after 24 or 36 months. The bar against an absolute discharge where there are three or more bankruptcies and the new second time bankruptcy provisions are in part a response to the moral hazard problem. However, whether or not there is a moral hazard problem in any particular case may well turn on the cause of the repeat bankruptcy.[54]

[53] See *Gurniak v. Royal Bank of Canada* (2011), 83 C.B.R. (5th) 87 (S.K.Q.B), at para. 27. (s. 173(1)(j) of the BIA is a "fault-based fact.")

[54] OSB Statistics #2, *supra*, footnote 20. Reasons for financial difficulties are provided in text format as the response to Question 14 "Give reasons for your financial difficulties" on Form 79 Statement of Affairs. The OSB has chosen 17 standard reasons for financial difficulties, as shown in Table 1. Data for student loans, loans to friends, cosigning loans for others or failure due to a garnishee action is not shown in Table 1. Using a data cleansing and parsing program, the responses provided to Question 14 are assigned reasons for financial difficulties by the OSB. Estates may have more than one reason for financial difficulties. For an earlier study on the causes of repeat bankruptcies see Strand, Hira & Carter, *supra*, footnote 17, at p. 28.

Table 1: Reasons Reported for Financial Difficulty: Value as a percentage of total number of reasons reported by bankrupts annually						
	2010		**2011**		**2012**	
	First time	**Repeat**	**First time**	**Repeat**	**First time**	**Repeat**
Overuse of credit, mismanagement, too much debt	30.33%	28.72%	29.93%	28.43%	29.35%	27.66%
Insufficient income	18.73%	18.94%	18.49%	18.54%	17.93%	18.96%
Unemployment	15.33%	13.39%	14.28%	12.85%	13.74%	12.13%
Health concerns, medical expenses, injuries, family deaths	9.86%	13.48%	10.37%	13.65%	10.71%	14.20%
Marital Breakdown/Divorce	8.51%	6.99%	9.08%	7.32%	9.69%	7.06%
Business failure, use of personal credit for business	5.76%	5.39%	5.88%	5.68%	6.23%	5.74%
Supporting parents, brothers-sisters, relatives	2.57%	1.90%	2.55%	1.72%	2.43%	1.57%
Tax liabilities	2.04%	3.54%	2.37%	4.26%	2.76%	5.08%
Accidents/emergencies related to property, i.e. fire, theft	1.13%	1.18%	1.22%	1.31%	1.27%	1.24%
Bad/poor investments	1.05%	1.05%	1.08%	0.88%	1.07%	0.77%
Moving, relocation of expenses, job change	0.82%	0.63%	0.81%	0.67%	0.80%	0.72%
Legal action	0.74%	0.90%	0.82%	0.98%	0.87%	0.89%
Alcoholism, drug addiction, substance abuse	0.71%	0.83%	0.76%	0.82%	0.74%	0.86%
Gambling	0.75%	1.10%	0.68%	0.94%	0.71%	0.97%

One argument is that there are two types of repeat bankrupts: "behavioural and structural repeat filers."[55] A behavioural debtor will "over-value current consumption and underestimate future costs." [56] In other words, the first type of repeat filer simply "cannot stop spending beyond their means."[57] As noted in Table 1, overuse of credit is the leading reason given as the cause of bankruptcy for both first time and repeat bankrupts. This suggests that there is a significant moral hazard problem when the cause of failure is misuse of credit.

In contrast, a structural repeat filing results from "external factors such as job loss, medical problems, and divorce."[58] This second type of repeat filer uses bankruptcy to "smooth consumption during economic distress"[59] which has been caused by one of the external factors. Unemployment, [60] health concerns[61] and marital breakdowns[62] have all

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[55] Miller & Miller, *supra*, footnote 16, at p. 516. See also Stephen J. Spurr & Kevin M. Ball, "The Effects of a Statute (BAPCPA) Designed to Make it More Difficult for People to File for Bankruptcy" (2013), 87 Amer. Bankr. L.J. 27, at p. 29.

[56] Miller & Miller, *ibid*. See also Saul Schwartz, "Personal Bankruptcy Law: A Behavioural Analysis" in J. Niemi-kiesilainen, I. Ramsay & W. Whitford eds. *Consumer Bankruptcy in a Global Perspective* (Oxford; Hart Publishing, 2003), at p. 66.

[57] Miller & Miller, *ibid*.

[58] *Ibid* at 517.

[59] *Ibid*. For an earlier study of the causes of repeat bankruptcies see Ramsay, *supra*, footnote 17.

[60] See e.g. *Re Hiebert*, [2008] 315 Sask. R. 118 (Q.B.), at paras. 4-6; *Re Sussman* (1990), 77 C.B.R. (N.S.) 310 (Ont. S.C.), at paras. 1-4; *Re Langill* (2006), 21 C.B.R (5th) 33 (B.C.S.C.), at paras. 6-8; *Re Pace* (2006), 246 N.S.R. (2d) 236 (S.C.), at para. 2; *Re Alonce* (2003), 48 C.B.R. (4th) 20 (Alta. Q.B.), at para. 3.

[61] See e.g. *Re Miller* (2007), 257 N.S.R. (2d) 318 (S.C.), at para. 4; *Re Judd* (1989), 76 C.B.R. (N.S.) 177 (B.C.S.C.), at para. 2; *Re Meek* (2009), 50 C.B.R. (5th) 135 (B.C.S.C.), at para. 1; *Re Mulligan* (2007), 38 C.B.R. (5th) 89 (B.C. S.C.), at para. 6; *Re Nelson* (2010), 69 C.B.R. (5th) 292 (B.C.S.C), at para. 6.

[62] See e.g. *Re Bernier*, 2012 QCCS 6166 at para. 14; *Re Williams* (2005), 10 C.B.R. (5th) 304 (B.C.S.C.), at para. 2; *Re Overly* (2002), 169 Man. R. (2d) 229 (Q.B.), at para. 5; *Re Randall* (1984), 54 C.B.R. (N.S.) 121 (Ont. S.C.), at para. 3; *Re Kusch* (2007), 33 C.B.R. (5th) 208 (B.C.S.C.), at para. 6.

been identified as causes of bankruptcy in Table 1. Financial failure in these situations may be unexpected, sudden or unanticipated. In these circumstances, the moral hazard problem may not be as significant as the bankruptcy may not be strategic. However, since more than one reason for failure may be recognized in any particular filing it may be difficult to measure the exact nature of the moral hazard problem. A debtor may identify, for example, health concerns or medical expenses together with the overuse of credit. Substance abuse[63] and gambling[64] have also been identified as causes of bankruptcy. This kind of so-called "compulsive behaviour"[65] accounts for less than two percent of the reported causes of bankruptcy for repeat bankrupts.[66]

III. SECOND TIME BANKRUPTS

1. The New Second Time Bankruptcy Regime

The 2009 amendments are having a profound the impact on the bankruptcy regime. For 2010 filings, 84% of all second time bankrupts received an automatic discharge after 24 months.[67] The 36 month surplus income provision, however, is having less of an impact. Although the 36 month provision was designed to substantially

[63] See e.g. *Re Loiselle*, 2013 QCCS 1391 at para. 14; *Re Perreault* (2011), 200 A.C.W.S. (3d) 317 (Que. Sup. Ct.), at para. 29; *Re Brown* (2008), 49 C.B.R. (5th) 35 (B.C.S.C.), at para. 3; *Re Bice* (2007), 38 C.B.R. (5th) 83 (Alta. Q.B.), at para. 1.

[64] See e.g. *Pitre*, *supra*, footnote 11, at para. 6; *Re Lok* (2010), 71 C.B.R. (5th) 98 (Sask. Q.B.), at para. 5; *Re Hosseini* (2008), 48 C.B.R. (5th) 222 (Ont. Sup. Ct.), at para. 2; *Re Bury* (2007), 34 C.B.R. (5th) 263 (Alta. Q.B.). at para. 1; *Re Tang* (2007), 29 C.B.R. (5th) 258 (Ont. Sup. Ct.), at para, 3.

[65] See Carole Anne Curnock "Insolvency Counselling – Innovation based on the Fourteenth Century" (1999), 37 Osgoode Hall L.J. 387, at p. 392.

[66] Curnock, *supra*, footnote 65, at p. 404. Curnock concludes that "bankruptcy resulting from psychosocial problems only applies to an extremely small minority of debtors." Curnock's conclusion is more consistent with OSB Statistics #2, *supra*, footnote 20, than an earlier OSB study which suggested that 30 percent of repeat bankrupts were related to substance abuse with a possible even greater percentage bankrupts having gambling debts. The author was unable to locate a copy of the earlier study but it is referenced in Ferron, *supra*, footnote 14, at para. 21.

[67] OSB Statistics #1, *supra*, footnote 19.

increase the "total funds payable to the trustee for distribution to creditors"[68] for 2010 filings, only 168 bankrupts with surplus income received an automatic discharge after 36 months. This represents 2% of all second time bankruptcies in 2010.

Automatic Discharges after 24 or 36 months[69]

2010 Filings	Auto. Discharge 24 months	Auto. Discharge 36 months
Total Number Discharged	7225	168
% of all second time bankruptcies	84%	2%

The BIA is silent on the issue of how much time must elapse before a debtor may file for bankruptcy again. In the United States, where a debtor has received a discharge in the first bankruptcy, the debtor "is absolutely precluded from receiving a discharge in a second case under chapter 7 within *eight years*."[70] There is no equivalent time bar in the BIA, however, it is OSB policy that "if a person has filed a second bankruptcy within a three year period subsequent to a previous discharge"[71] the file will automatically be flagged by the OSB for review to determine whether the OSB should intervene in the bankruptcy discharge hearing.

Prior to 2009, there was little consistency in the length of judicial suspensions for a second time bankrupt in the reported case law. At one end of the spectrum, some Alberta courts imposed lengthy suspensions ranging from 10[72] to 25 years. [73] At the other

[68] *Re Kuss* (2009),55 C.B.R. (5th) 289 (Atla. Q.B.), at para. 10.

[69] OSB Statistics #1, *supra*, footnote 19.

[70] Charles Jordan Tabb, *The Law of Bankruptcy*, 2d ed. (New York, NY: Thomson Reuters/Foundation Press, 2009), at p. 970. "The eight-year period is computed from the date of *commencement* of case 1 to the commencement of case 2, *not* from discharge to discharge." See also Hon William L. Norton Jr. & William L. Norton III, *Norton Bankruptcy Law and Practice*, 3d ed. (Thomson Reuters, 2013), § 86:18 (Westlaw).

[71] Email from Leona Luk, Senior Bankruptcy Analyst, OSB to Thomas Telfer, 24 September 2013. The OSB will also determine whether a referral should be made to the Special Investigations Unit (SIU). The SIU may in turn pass the file to the RCMP.

[72] *Re Zapisocki* (2002), 316 A.R. 207 (Q.B. Reg.).

end of the scale in *Re Doe,*[74] an Ontario court imposed a 1 month suspension where the first bankruptcy had preceded the second by 13 years. [75] In fact, outside of Alberta, suspensions ranged from 1 month[76] to 3 years.[77]

Parliament chose to replace the judicial discretionary regime with a default rule-based automatic discharge system.[78] On the one hand, the second time discharge system avoids costly discharge hearings and imposes a national standard that will be applied wherever the bankrupt is residing. [79] On the other hand, bright-line rules may not always do justice on the merits of each case. Unless there is an objection, the new regime is not able to discern whether or not the bankruptcy arose from a moral hazard problem.

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[73] *Re O'Dell* (2000), 269 A.R. 199 (Q.B. Reg.); *Re Cardinal* (2000), 267 A.R. 199 (Q.B. Reg.). The Alberta Court of Queen's Bench in *Re Walterhouse* reduced a 25 year suspension to a 5 year suspension on the basis that such a lengthy suspension was tantamount to a refusal of a discharge. *Re Walterhouse* (2002), 318 A.R. 394 (Q.B.).

[74] (1992), 15 C.B.R. (3d) 105 (Ont. Ct. of J.).

[75] *Ibid.* See also *Sussman*, *supra*, footnote 60 (court imposed a 3 month suspension); *Re Perpich*, 2006 CarswellOnt 6821 (Ont. Sup. Ct. J.), at para. 13 (6 month suspension); *Re Steward*, 2000 CarswellOnt 5465 (Ont. Sup. Ct. J.) (6 month suspension).

[76] *Re Kolody* (1999), 178 Sask. R. 137 (Q.B. Reg.); *Re Rubin* (2011), 74 C.B.R. (5th) 231 (B.C.S.C.).

[77] See *Re Maurer* (2001), 31 C.B.R. (4th) 69 (B.C.S.C.) (2 months); *Re Côté* 2010 QCCS 412 (3 months); *Re Ducas*, 2010 QCSC 413 (3 months); *Re Handfield*, 2010 QCSC 415 (3 months); *Re Grier* (1998), 132 Man. R. (2d) 26 (Man. Q.B.) (4 months); *Re Brown* (2010), 364 Sask. R. 300 (Q.B.) (conditional order combined with a 6 months); *Re Giera* (2008), 172 A.C.W.S. (3d) 292 (Ont. Sup. Ct. J.) (conditional order combined with 6 months); *Gurniak*, *supra*, footnote 53 (conditional order combined with 6 months); *Re Muzlera* (2011), 81 C.B.R. (5th) 113 (Ont. Sup. Ct. J.) (6 months); *Overly*, *supra*, footnote 62 (6 months); *Re Kaufman*, 2005 CarswellOnt 3405 (Sup. Ct. J.) (9 months with conditional order); *Re Cookson*, 1996 CarswellOnt 1416 (Ont. Bankr.) (9 months); *Re White*, 1997 CarswellNS 570 (N.S.S.C.) (1 year); *Re Beaule*, (1985) 47 Sask. R. 159 (Q.B.) (conditional order combined with a 1 year); *Re Grandoni* (2007), 31 C.B.R. (5th) 282 (B.C.S.C.) (1 year); *Re Steeves* (2009), 61 C.B.R. (5th) 84 (B.C.S.C.) (1 year); *Re Robson* (2009), 59 C.B.R. (5th) 274 (B.C.S.C.) (18 months); *Beck*, *supra*, footnote 13 (2 years); *Re Baldwin*, 1997 CarswellBC 607 (S.C.) (2 years); *Re Freeman* (1984), 54 C.B.R. (N.S.) 181 (B.C.S.C.) (3 years); *Re Wortsman* (1984), 53 C.B.R. (N.S.) 45 (Ont. S.C.) (3 years).

[78] On the difference between rules and standards see Thomas G.W. Telfer, "Voidable Preference Reform: A New Zealand Perspective on Shifting Standards and Goalposts" (2002), 12 Int. Insolv. Rev. 55, at p. 62.

[79] PITF Report, *supra*, footnote 15, at p. 49.

Creditors, trustees and the Superintendent of Bankruptcy[80] must be diligent in deciding whether to oppose an automatic discharge. Will an automatic discharge in the second case set the stage for a third bankruptcy?

2. Second Time Bankruptcies Pre 2009 Amendments

As creditors, trustees or the Superintendent of Bankruptcy can object to the automatic discharge and force a hearing, second time jurisprudence that pre-dates the amendments remains relevant. Stephanie Ben-Ishai, writing in 2007 suggested that the "rhetoric found in decisions on discharge would aid in providing further insight into the role and form of dispute resolution in consumer bankruptcy."[81] The case law reveals judicial attitudes towards second time bankrupts.

There are some common themes in second time bankruptcy jurisprudence. Courts have been reluctant to allow debtors to periodically use the BIA to obtain a release of their debts.[82] In *Re Lebel*[83] Anderson J. concluded that the Bankruptcy Act was "not to be considered a process which can be had resort to on a regular basis with a view to washing out one's debts."[84] A further theme is the emphasis upon the maintenance of the integrity of the bankruptcy system. In *Re Bury*[85] the court concluded that where there is a repeat or

[80] BIA, *supra*, footnote 7, s. 168.2 on oppositions to an automatic discharge.

[81] Ben-Ishai, *supra*, footnote 23, at p. 370.

[82] *Re Walker* (1998), 226 A.R. 212 (Q.B.); *Re Ross* (2001), 22 C.B.R. (4th) 138 (Alta. Q.B.); *Re Czaja*, 2000 ABQB 949; *Re Unrau* (2001), 26 C.B.R. (4th) 106 (Alta. Q.B.), at para. 6; *Re Hatton* (1979), 32 C.B.R. (N.S.) 77 (Ont. S.C.), at para. 2.

[83] (1979), 31 C.B.R. (N.S.) 320 (Ont. S.C.).

[84] *Ibid* at para 2.

[85] *Bury supra*, footnote 64.

dishonest bankrupt, "the purpose of the Act shifts toward the protection of society, the upholding of the integrity of the Act and the sanctioning of inappropriate behavior." [86]

The balance between rehabilitation and the integrity of the system is tested when a debtor repeats patterns of financial misbehavior over two bankruptcies. Perhaps the most common and overriding theme in the reported case law is the tendency of a debtor to fail a second time for the same or similar reasons as the first bankruptcy. [87] In *Re Tang*[88] the court refused a discharge:

> It would be one thing if this second bankruptcy were the result of misfortune. It is not. It is solely the result of the Bankrupt engaging in the same reckless and destructive behaviour as led to his first bankruptcy. Not only that, but he engaged in business practices which, although clearly legal, effectively preyed on the very weakness in others which has led him into bankruptcy not once but twice….This is not the hallmark of either an honest or unfortunate debtor, and such a debtor is not deserving, I find, of the fresh start afforded by the BIA.[89]

In *Re Martens*[90] both bankruptcies were "tax driven". The bankrupt decided not to file tax returns or pay income tax "and periodically absolve[d] herself of her legal obligations by going to the bankruptcy trough, not once but twice."[91] "Having struck

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[86] *Ibid* at para.10. See also *Re Fraser* (2009), 53 C.B.R. (5th) 80 (B.C.S.C.), at para. 18.

[87] *Kealey v. Minister of National Revenue*, 1999 CarswellOnt 2188 at para. 64 (Ct. J.). See also *Bury*, *ibid* at para. 10; *Fraser*, *ibid* at para. 18;, *Re Owen* (2010), 71 C.B.R. (5th) 297, (N.B.Q.B.), at para. 9; *Re Evans* (1997), 211 A.R. 76 (Q.B.), at para. 14; *Re Hockenhull*, [2001] O.J. No. 3061 (Sup. Ct. J.); *Re Ngoka* (1998), 174 Sask. R. 3 (Q.B.); *Re Jolin* (2008), 170 A.C.W.S. (3d) 237 (Ont. Sup. Ct. J.), at para. 12; *Re Chronopoulos*, 2007 CarswellOnt 6981 (S.C.); *Williams*, *supra*, footnote 62, at para. 12; *Re Patrick*, [2000] O.J. No. 3150 (Sup. Ct. J.).

[88] *Supra*, footnote 64.

[89] *Ibid* at para. 7.

[90] [1994] A.J. No. 1265 (Q.B.).

[91] *Ibid* at para. 3.

upon what she thought was a good scheme the bankrupt simply continued her obdurate conduct." [92]

> In this extreme case the overriding principle must be a message. The message is that tax cheaters are free riders and they should not be absolved from that. The bankrupt refused to "rehabilitate" herself after the first bankruptcy. She just carried on in the same pattern. The Act is to be just a convenient ink remover, she thinks, removing what is in the Minister's ledger sheets against her.[93]

The AEB survey of Trustees, Creditors and the OSB confirms this important theme found in the jurisprudence. A common problem with repeats "is that they fall back into their bad practices once they get out. They convince themselves they won't make the same mistake."[94] Debtors simply do not "learn from the initial bankruptcy"[95] and "fail again for the same reasons as their first bankruptcy."[96]

In many situations the rehabilitative aspects of the first bankruptcy have no impact on the bankrupt. In *Re Gleeson*[97] Registrar Ferron came to this conclusion:

> The extinguishment of the bankrupt's debts as a result of the discharge in his first bankruptcy was meant to give the debtor a fresh start. The rehabilitative aspects of that process were lost on the bankrupt and there is no reason to think that a discharge at this point in the second bankruptcy would have the effect which the bankruptcy is supposed to have.[98]

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[92] *Ibid* at paras. 6-8.

[93] *Ibid* at para. 31.

[94] Trustee #3, Trustee Responses to Question Four, Appendix C, AEB Report, *supra*, footnote 14. Answers disclosed pursuant to Access to Information Act, Letter from Kimberly Eadie, Director, Information & Privacy Rights Administration to Thomas Telfer, 26 August 2013 [hereafter Access to Information Act].

[95] Creditor #3, Creditor Responses to Question Four, Appendix C, AEB Report, *supra*, footnote 14; Access to Information Act, *ibid*.

[96] OSB #6, OSB Responses to Question Four, Appendix C, AEB Report, *supra*, footnote 14; Access to Information Act, *ibid*.

[97] (1990), 80 C.B.R. (N.S.) 127 (Ont. S.C.).

[98] *Ibid* at para. 7. See also *Re Osesky* (2002), 31 C.B.R. (4th) 80 (Man. Q.B.), at para. 17 (refusal of discharge); *Hatton*, *supra*, footnote 82, at para. 2; *Re Snihur* (1985), 53 C.B.R. (N.S.) 149 (Ont. S.C.), at para. 5; *Re Lloyd*, 2000 ABQB 497 at para. 5. See also *Re O'Keefe*, 2001 ABQB 335 at para. 11; *Re Koehler* (2001), 24 C.B.R. (4th) 59 (Alta. Q.B.); *Ross*, *supra*, footnote 82, at para. 8.

Indeed evidence of altered behavior may be key to a favourable order of discharge in a second bankruptcy. In *Re Hatton*[99] Anderson J concluded that a second or subsequent bankrupt bears a heavy onus "to establish some change in his financial pattern which warrants the court making the order sought."[100]

IV. THIRD TIME BANKRUPTCIES

While the BIA makes it clear that where there is a prior bankruptcy the court shall refuse, suspend or impose a conditional discharge,[101] there are no other specific provisions dealing with third, fourth and fifth time bankrupts. However, where there are three or more bankruptcies the OSB will automatically flag the file for review to determine whether or not to intervene in the discharge hearing.[102] Further, it is the OSB's position that where there are three or more bankruptcies, the debtor should remain in bankruptcy for a minimum of 36 months.[103] Third time bankrupts represent a small percentage of total consumer filings. However, one should not easily dismiss the fact that over the past three years there have been 3045 third time bankruptcies.

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[99] *Supra*, footnote 82.

[100] *Hatton*, *supra*, footnote 82, at para. 2. See also *Snihur*, *supra*, footnote 98, at para. 5; *Hosseini*, *supra*, footnote 64, at para. 16.

[101] BIA, *supra*, footnote 7, at ss. 173(1)(j), 172(2).

[102] Luk, *supra*, footnote 71. The OSB will also determine whether a referral should be made to the Special Investigations Unit (SIU). The SIU may in turn pass the file to the RCMP.

[103] *Ibid.*

Summary of OSB Statistics 2010-2012 Third Time Bankruptcies[104]

2010	Number of Filings	% of total filed
All consumer bankruptcies	92694	100%
One or more previous bankruptcies	13897	14.99%
3rd time filing bankruptcy	1058	1.14%

2011	Number of Filings	% of total filed
All consumer bankruptcies	77993	100%
One or more previous bankruptcies	12145	15.57%
3rd time filing bankruptcy	1010	1.29%

2012	Number of Filings	% of total filed
All consumer bankruptcies	71495	100%
One or more previous bankruptcies	11518	16.11%
3rd time filing bankruptcy	977	1.37%

In *Re Lynn*[105] Suche J. concluded that "third time bankruptcies are of grave concern, often demonstrating a degree of irresponsibility that justifies simply refusing a discharge."[106] Justice Anderson in *Re Hardy*[107] concluded that a "third bankruptcy is one too many."[108] Justice Anderson's comment has been characterized as a "'three strikes'" rule."[109] While it has been held that "there is no rule of law that a third time bankruptcy

[104] OSB Statistics #1, *supra*, footnote 19.

[105] (2012), 278 Man. R. (2d) 101 (Q.B.).

[106] *Ibid* at para. 22; *Re Willier* (2005), 14 C.B.R. (5th) 130 (B.C.S.C.), at para. 8. See also *Re Grasdal* (2001), 290 A.R. 389 (Q.B.), at para. 8.

[107] (1979), 30 C.B.R. (N.S.) 95 (Ont. S.C.).

[108] *Ibid* at para. 3.

[109] *Willier*, *supra*, footnote 106, at para. 8.

must result in refusal of discharge… the court must nevertheless pay very careful attention to the future prospects of a third time bankrupt."[110]

The grave concern over third time bankruptcies is reflected in the judicial rhetoric in the case law. In refusing a discharge in *Re Garness,*[111] the court characterized the bankrupt as having "a SARS-like presence in the local economic community."[112] Over three bankruptcies, the debtor had incurred debts of over $579,000. According to the court, the bankrupt and the economic community needed "further economic quarantine before discharge [could] be possible."[113] In *Re Frolick*[114] the trustee recommended that a third time bankrupt be discharged without conditions. In refusing the application for the discharge, Registrar Funduk stated: "Why not go the extra step and also recommend that the bankrupt be given a medal for his ability to fornicate the bankruptcy laws."[115]

The British Columbia Supreme Court in *Re Willier*[116] acknowledged that an important shift occurs when there is a third time bankruptcy:

> By the time an individual has entered a third bankruptcy, the purpose and intent of the *Act* shifts from its remedial purpose of assisting well-intentioned but unfortunate debtors to one of protecting society, and in particular unsuspecting potential creditors. The best intentions and hopes of such bankrupts become subordinated to the need to protect others from the bankrupt's demonstrated financial incompetence, negligence, and carelessness. If there can be a concept of debtors' recidivism, it is demonstrated in stark relief by a third-time bankrupt.[117]

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[110] *Pace*, *supra*, footnote 60, at para. 14. See also *Re Randall*, *supra*, footnote 62, at para. 10.

[111] (2004), 5 C.B.R. (5th) 51 (B.C.S.C.).

[112] *Ibid* at para. 21.

[113] *Ibid.*

[114] (2001), 294 A.R. 198 (Q.B.).

[115] *Ibid* at para. 16.

[116] *Supra*, footnote 106.

[117] *Willier*, *supra*, footnote 106, at para. 12.

The integrity of the bankruptcy system involves the protection of creditors and the public through a refusal of a discharge, suspension or a conditional order.[118]

Third time bankruptcy jurisprudence also reveals judicial concern for debtors who make the same mistakes again. In the context of the third bankruptcy, *Re Lynn*[119] defined rehabilitation in this way:

> "Rehabilitation", in a behavioral context… is comprised of two elements: recognition of wrongdoing and a willingness to change. It is a means of establishing some trust that…there is a "realistic and reliable likelihood that the mistakes will not be repeated."[120]

To consider a discharge for a third time bankrupt "the court must be satisfied that the bankrupt has gained sufficient insight and made sufficient changes in his or her life that it is not reasonably possible that further bankruptcy will occur."[121] An acknowledgement of "blame and acceptance of individual responsibility for the consequences"[122] of the bankruptcy is essential. Without this acknowledgment the bankrupt may simply repeat past practices. The court must be convinced that "something has been learned by the bankrupt that will give some sense of assurance that the cycle of bankruptcy has been broken."[123] Creditors of a third time bankrupt are "absolutely entitled to a realistic and reliable likelihood that the mistakes will not be repeated."[124]

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[118] *Pitre*, *supra*, footnote 11, at para. 26; *Chaban*, *supra*, footnote 38, at para. 7. See also *Re Beauregard*, 2012 QCSC 6401.

[119] (2012), 278 Man. R. (2d) 101 (Q.B.).

[120] *Ibid* at para. 34. See also *Re Scattergood* (2010), 66 C.B.R. (5th) 103 (B.C. Master), at para. 4; *Re Resnick* (1990), 80 C.B.R. (N.S.) 223 (Ont. S.C.), at para. 4.

[121] *Willier*, *supra*, footnote 106, at para. 13.

[122] *Re Garness* (2004), 5 C.B.R. (5th) 51 (B.C.S.C.), at para. 19.

[123] *Pace*, *supra*, footnote 60, at para. 14; *Miller*, *supra*, footnote 61, at para. 15.

[124] *Garness*, *supra*, footnote 122, at para. 19.

Registrar Ferron refused to grant a discharge to a third time bankrupt in *Re Flowerday.*[125] The court identified a pattern of abuse and concluded that rehabilitation was not possible in this situation:

> The pattern is obvious. Debts are accumulated over a five-year period and then the debtor files in order to receive a fiscal clearance. This is an abuse of the system which is not to be tolerated. The bankrupt has obviously learned nothing from his previous experiences and is probably incapable of rehabilitation.[126]

Registrar Baker in *Re Brown*[127] expressed the hope that multiple bankrupts become bankrupt "for differing reasons."[128] However, Brown "[dashed] that hope: he [had] been bankrupt three times, all for the same reason: over-extension of credit."[129] In 22 years, Brown had not made "concrete and demonstrable changes"[130] on a long-term basis. There was no sense that the discharge order would involve notions of rehabilitation. Thus, the court held that the "world at large [had] to be protected from him."[131]

Despite the judicial rhetoric in the reported case law, statistics reveal that refusals of a discharge are rare for third time bankruptcies:[132]

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[125] (1992), 14 C.B.R. (3d) 297 (Ont. Ct. J.).

[126] *Ibid* at paras. 5-6.

[127] *Brown*, *supra*, footnote 63.

[128] *Ibid* at para. 1.

[129] *Ibid* at para. 2.

[130] *Ibid* at para. 6.

[131] *Ibid at* para. 9. The court suspended the discharge for a period of three years and barred the bankrupt from making applications for credit (except for a personal residence) for a period of 15 years.

[132] OSB Statistics #1, *supra*, footnote 19.

Suspensions, Conditional Orders and Refusals of Discharge

3rd Time Bankruptcies	% Suspensions	% Conditional Orders	% Refusals
2010	58.19	40.96	0.85
2011	51.38	47.25	1.38

V Fourth and Fifth Time Bankruptcies

The OSB statistics reveal that fourth and fifth time bankruptcies account for less than one percent of all consumer bankruptcies. While one might argue that the percentage of fifth time bankrupts to total filings is statistically insignificant, it is of greater concern that in 2012, there were 9 fifth time bankruptcies filed.

Summary of OSB Statistics 2010-2012[133]

2010	Number of Filings	% of total filed
All consumer bankruptcies	92694	100%
One or more previous bankruptcies	13897	14.99%
4th time filing bankruptcy	59	0.06%
5th time filing bankruptcy	7	0.01%

2011	Number of Filings	% of total filed
All consumer bankruptcies	77993	100%
One or more previous bankruptcies	12145	15.57%
4th time filing bankruptcy	84	0.11%
5th time filing bankruptcy	6	0.01%

2012	Number of Filings	% of total filed
All consumer bankruptcies	71495	100%
One or more previous bankruptcies	11518	16.11%
4th time filing bankruptcy	74	0.10%
5th time filing bankruptcy	9	0.01

In a fourth bankruptcy, courts generally apply the same test that is used in a third bankruptcy:

[133] *Ibid.*

> the test to be applied on a third or fourth bankruptcy shifts from rehabilitating a well-intentioned but unfortunate debtor to one of protecting society generally and unsuspecting creditors in particular.[134]

By the time a fourth bankruptcy is reached:

> the primary purpose of any order is to ensure that future creditors are protected while the bankrupt attempts such rehabilitation. The order must also serve as a deterrent to others in like circumstances.[135]

In many of the reported cases the courts refused to grant a discharge. However, the actual refusal rate is much lower than that represented in the reported case law. Statistics from the OSB demonstrate that in 2011 refusals of discharges are also rare for fourth and fifth time bankruptcies.[136]

Suspensions, Conditional Orders and Refusals of Discharge

	% Suspensions	**% Conditional Orders**	**% Refusals**
2010	47.37	26.32	26.32
2011	40.54	54.05	5.41

Like other repeat bankruptcy cases, four time bankrupts follow patterns of past behavior. In *Re Mulligan*[137] the court concluded that the bankrupt had not learned from "her past bankruptcies" and "society [needed] to be protected from Mrs. Mulligan's incompetent use of credit."[138] The court was of the view that the bankrupt "[had] repeatedly shown that she [could not] budget within her means."[139] The court suspended the discharge for a period of 15 years.

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[134] *Hiebert, supra,* footnote 60, at para. 19. See also *Kusch, supra,* footnote 62, at para. 12.

[135] *Re Herd* (2009), 60 C.B.R. (5th) 158 (B.C.S.C.), at para. 20.

[136] OSB Statistics #1, *supra,* footnote 19.

[137] *Supra,* footnote 61.

[138] *Ibid* at para. 15.

[139] *Ibid* at para. 16. See also *Re Tomkins* (1990), 80 C.B.R. (N.S.) 35 (Ont. S.C.), at para. 1.

In *Re Kusch*[140] the bankrupt claimed that he was not at fault for his first three bankruptcies. While the court acknowledged that the bankrupt "had some misfortune"[141] there was "no indication that he [accepted] any personal responsibility for it."[142] The court refused his discharge:

> The number of bankruptcies and his apparent inability to see how his actions may have contributed to the circumstance leading to the bankruptcy gives me reason to believe that if I discharge him, I will be setting the stage for bankruptcy number 5.[143]

The court concluded that the bankrupt had not "learned anything from [the] past bankruptcies, other than he was a hapless victim of circumstance."[144] Master Young stipulated that the bankrupt could not reapply for a discharge for a period of two years. If the bankrupt wanted to apply at that time:

> then he will have to demonstrate at that time that he has learned something about financial management and that he can demonstrate financial prudence. The court would, at that time, be looking for a clear plan as to how he would plan to avoid future financial problems and some indication that he is implementing that plan.[145]

VI. MANDATORY COUNSELLING

In 1992, Parliament amended the BIA to require mandatory counselling for all bankrupts.[146] Parliament added the mandatory counselling provisions in order to reduce

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[140] *Kusch*, *supra*, footnote 62.

[141] *Ibid* at para. 8.

[142] *Ibid*.

[143] *Ibid* at para. 9.

[144] *Ibid* at para. 13.

[145] *Ibid* at para. 14. See also *Hiebert*, *supra*, footnote 60; *Herd*, *supra*, footnote 135; *Re Dennison* (2013), 230 A.C.W.S (3d) 966 (Sask. Q.B.).

[146] BIA, *supra*, footnote 7, s.157.1. See OSB Directive IR3. On the origins of mandatory counselling see Iain Ramsay, "Mandatory Bankruptcy Counselling: The Canadian Experience" (2002), 7:2 Fordham J. Corp. & Fin. L. 525; Curnock, *supra*, footnote 65; Saul Schwartz, "The Effect of Bankruptcy Counseling on Future Creditworthiness: Evidence from a Natural Experiment" (2003), 77 Am. Bankr. L.J. 257, at p.

the number of repeat bankrupts.[147] The 2013 AEB Report on Mandatory Counselling concludes that Parliament introduced mandatory counselling "to help avoid repeat personal bankruptcies by providing debtors with information and education on financial management."[148]

Writing in 1999, Berry and McGregor optimistically claimed that the introduction of mandatory counselling "could lead to fewer repeat bankruptcies, better educated consumers, and rehabilitation of those debtors teetering on the edge, or in the cycle, of bankruptcy."[149] In *Re Newsham*[150] the court identified the underlying goal of mandatory counselling:

> In bankruptcy the debtor is required to attend two counselling sessions. A recognition of the cause of bankruptcy and the prevention of a repeat bankruptcy is a necessary ingredient of counselling. Budget preparation and the proper use of credit cards must be an important component of most counselling sessions. Because of the rise in second, third and fourth time bankruptcies, counselling to avoid repeat assignments is viewed by the courts as an important and necessary ingredient in the process.[151]

Given the increasing rate of repeat bankruptcies one has to ask whether mandatory counselling has been effective in preventing repeat bankruptcies. The AEB Report on Mandatory Counselling concluded that "mandatory counselling addresses a continued need by contributing to the rehabilitation of debtors and helping them avoid future

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[147] Iain Ramsay, "Interest Groups and the Politics of Consumer Bankruptcy Reform in Canada" (2003), 53:4 U.T.L.J. 379, at pp. 406-407; Ruth E. Berry & Sue L.T. McGregor, "Evolution of Statutory Consumer Counseling in Canada and Europe: Counseling Consumer Debtors Under Canada's Bankruptcy and Insolvency Act" (1999), 37 Osgoode Hall L.J. 369, at p. 371; Schwartz, *ibid*, at p. 267.

[148] AEB Report, *supra*, footnote 14, at p. 1. See also Julio Caruso & Éric Archambault, *Measuring the Effectiveness of Credit Counselling: An Enviornmental Scan*, (Montreal: Science-Metrix Inc, 1992) at p.1 (Appendix B to AEB Report).

[149] Berry & McGregor, *supra*, footnote 147, at pp. 384-385.

[150] (2003), 48 C.B.R. (4th) 121 (Alta. Q.B.).

[151] *Ibid* at para. 10.

financial difficulties."[152] According to the Report, "mandatory counselling had a positive impact on debtors."[153] The Report specifically assessed mandatory counselling in light of evidence of repeat bankruptcies. The AEB Report concluded that "debtors who cited the overuse of credit as a reason for their financial difficulties were less likely to be repeats."[154] The Report also concluded that debtors who reported overuse of credit as the reason for failure "were less likely to be repeat filers."[155] The AEB Report found that where a debtor reported overuse of credit "then the probability that the debtor had a previous bankruptcy or insolvency dropped by 3.7%."[156]

However, the effectiveness of mandatory counselling to combat repeat filings must be considered in light of the causes of bankruptcies for repeat bankrupts. If bankrupts were truly gaining financial skills through the mandatory counselling program, one would expect that misuse of credit would play a much lesser role in the cause of a repeat filing. OSB data on the causes of bankruptcies demonstrates that for repeats and first time bankrupts, overuse of credit is the leading cause of bankruptcy and there is similarity in the response rate.[157] In 2012, repeat bankrupts identified overuse of credit as the cause of bankruptcy 27.6 percent of the time while first time bankrupts reported overuse of credit as a reason for financial failure 29.35 percent of the time.

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[152] AEB Report, *supra,* footnote 14, at p. 27.

[153] *Ibid*.

[154] *Ibid* at p. 18.

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[155] *Ibid* at p. 27.

[156] *Ibid* at p. 18.

[157] See Table 1.

Beyond misuse of credit a there may be structural[158] reasons for failure. Debtors may fail for reasons beyond their control. As noted in Table 1, bankrupts have identified for example, medical concerns as a cause of bankruptcy. One has to ask whether credit counselling has any impact in this situation. As Saul Schwartz notes "there is no reason to believe that credit counseling is effective for debtors who file for bankruptcy because illness prevents them from working."[159]

Further, a review of the jurisprudence confirms that rehabilitation played little role in preventing subsequent bankruptcies as debtors simply made the same financial mistakes over and over again. One has to ask whether mandatory counselling will ever have the potential to prevent repeat bankruptcies. Saul Schwartz's study indicates that counselling does not lead to "any appreciable improvement in future creditworthiness."[160] His study concludes that "counseling has little effect on repeat bankruptcy in the first five years after an initial bankruptcy filing."[161] Indeed repeat bankruptcies may be "an indication that our bankruptcy system is not responding effectively to the inadequate knowledge and financial skills of first-time bankrupts."[162]

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[158] Miller & Miller, *supra*, footnote 16, at p. 516.

[159] Schwartz, *supra*, footnote 146, at pp. 267-268. Table 1 indicates that repeat bankrupts report health concerns as a cause of bankruptcy more often than first time bankrupts.

[160] Schwartz, *supra*, footnote 146, at p. 277.

[161] *Ibid* at 274.

[162] Clare, *supra*, footnote 12.

It is not clear that bankrupts are gaining the necessary skills to avoid a repeat bankruptcy. In refusing a discharge in a fourth time bankruptcy case, the court in *Re Hiebert*[163] concluded:

> I am not satisfied that Hiebert has gained sufficient insight into proper financial management, budgeting and use of credit, nor am I persuaded that he has made appropriate changes in his life to prevent another bankruptcy from occurring. Regrettably, I conclude that the protection of society and unsuspecting creditors can only be achieved by refusing his discharge application.[164]

In another fourth time bankruptcy case, Mr. Boivin indicated that "during the current bankruptcy he had attended credit counselling of a type he had not received before."[165] Boivin alleged that from the counselling "he [felt] he [had] made tremendous progress he in understanding how to live within his means."[166] Notwithstanding the bankrupt's reference to credit counselling, the court was "not satisfied that the bankrupt [had] gained sufficient insight and made sufficient changes in his life that it [was] not reasonably possible that a further bankruptcy [would] occur."[167]

> Over a period of 30 years this bankrupt has left unpaid creditors with total debts of about $834,000 due to his profligate and utterly irresponsible use of credit or failure to pay taxes....[H]e has...had a financially pestilential effect on those unpaid creditors he has left in his wake.[168]

Finally, if mandatory counselling was serving its intended purpose, one would expect that the overall repeat filing rate would be decreasing and not increasing.

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[163] *Supra*, footnote 60.

[164] *Ibid* at para 20.

[165] *Re Boivin* (2008), 40 C.B.R. (5th) 281, at para. 12.

[166] *Ibid*.

[167] *Ibid* at para 19.

[168] *Ibid* at para 18.

VII. POSSIBLE SOLUTIONS?

Over time a number of solutions have been proposed to deal with the ongoing problem of repeat bankruptcies. For example, provisions relating to repeat bankruptcies may be traced back to a 1732 English statute.[169] Under this provision, a bankrupt was entitled to a discharge for a second time only if a 75% dividend was paid in the second case.[170] Given this high dividend threshold it seems likely that under such a regime few bankrupts received a discharge in the second case. The current US solution, which prevents a debtor from receiving a discharge in a second chapter 7 case within eight years,[171] is over inclusive. The eight year time bar does not distinguish between behavioural debtors and structural debtors (ie debtors who failed for reasons beyond their control.) All debtors are equally barred.

Any Canadian reforms might target second time bankrupts. Second time bankruptcies represent the highest proportion of all repeat bankruptcies. Further, initial data on the 2009 amendments suggests that a significant percentage of those second time bankrupts are receiving an automatic discharge after 24 months. If there is concern second time bankrupts are flowing through the automatic discharge regime unopposed, one might look to current OSB policy on second time bankrupts for a possible reform solution. It is current OSB policy that "if a person has filed a second bankruptcy within a three year period subsequent to a previous discharge"[172] the file will automatically be

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[169] 5 Geo 2, c 30, s 9. See Charles Jordan Tabb, "The Historical Evolution of the Bankruptcy Discharge" (1991), 65 Am. Bankr. L.J. 325, at pp. 341-342.

[170] Tabb, *ibid.*

[171] Tabb, *supra*, footnote 70, at p. 970.

[172] Luk, *supra*, footnote 71.

flagged by the OSB for review to determine whether the OSB should intervene in the bankruptcy discharge hearing. If the high rate of second time automatic discharges continues unabated one might translate OSB policy into legislation. Where a person has filed a second bankruptcy within a three year period subsequent to a previous discharge the BIA could be amended to provide that the person is not entitled to an automatic discharge and the matter should be referred to the court for a discharge hearing. In that situation the court shall either refuse the discharge, suspend the discharge or impose a conditional order.[173]

While such an approach would be able to remedy an abusive second filing, the court would also have the discretion to fashion an appropriate solution where the debtor had failed for reasons beyond his or her control. Unlike the US provision, the proposal does not set up an automatic three year time bar. The reform proposal would merely trigger a discharge hearing when that second bankruptcy falls within three years of the prior discharge.

CONCLUSION

Repeat bankruptcies come with certain costs. In particular they can contribute to slower economic growth by "increasing the costs for goods, services and credit."[174] Indeed, creditors interviewed in the AEB study indicated a lower repeat filing rate could lead to lower consumer credit costs.[175] Additionally, repeat bankruptcies "can lead to increased ... administration costs due to the processing of filings and the monitoring of

[173] BIA, *supra*, footnote 7, at s. 172(2). Where there is no surplus income the suspension should be for a minimum of 24 months. If there is surplus income the suspension should be for a minimum of 36 months.

[174] AEB Report, *supra*, footnote 14, at p. 11. See Lewis, *supra*, footnote 16, at p. 22.

[175] AEB Report, *ibid*.

the debtor."[176] Repeat bankruptcies also come with economic costs for the debtor.[177] A repeat bankrupt may remain an undischarged bankrupt for a substantial period of time. This will have a significant impact on the debtor's ability to obtain credit. The BIA makes it an offence for a bankrupt to obtain credit of $1000 or more from any person "without informing them that the undischarged bankrupt is an undischarged bankrupt."[178]

In particular, abusive repeat filings (i.e. where moral hazard problems are present) create problems for the bankruptcy system in Canada and elsewhere.[179] The task, however, is to separate the abusive repeat filings from the repeat filings that arise from circumstances that may be beyond the control of the debtor.[180] It is important to distinguish between those debtors who require more than one bankruptcy to obtain a release of their debts and a debtor who is "abusing the system to escape their credit obligations."[181] Given the high percentage of second time bankrupts receiving an automatic discharge, one must ask whether the new second time regime is able to draw this distinction.

Mandatory counselling may not be the solution to the problem of repeat bankruptcies. Although counselling seeks to provide bankrupts with necessary financial

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[176] *Ibid*.

[177] Bankruptcy also affects the credit ratings of the debtor as information about the bankruptcy will be kept on the credit files of bankrupts for six years after the date of the discharge. See Schwartz, *supra*, footnote 146, at p. 257.

[178] BIA, *supra*, footnote 7, at s. 199(b). See e.g. *Tomkins*, *supra*, footnote 139, at para. 4; *Hiebert*, *supra*, footnote 60, at para. 21. On the origins of s. 199 see Bankruptcy Act, 1883 (U.K.), c. 52, s. 31. U.K., H.C., Parliamentary Debates, vol. 277 col. 816, at 831-32 (19 March 1883) (Mr. Chamberlain).

[179] Lewis, *supra,* footnote 16, at p. 18.

[180] *Ibid* at 22.

[181] Lown & Llewellyn, *supra*, footnote 16, at p. 37.

skills for financial success, repeat bankrupts still identify the misuse of credit as the leading cause of failure. Further, the fact that many bankrupts repeat patterns of financial mismanagement suggests that mandatory counselling may not be an effective way to reduce multiple filings. Indeed, bankrupts must learn something from the counselling sessions or they risk the chance of return.[182] Repeat filings also raise questions about the role that creditors play in making credit available to former bankrupts. To what extent should lenders bear some responsibility for the repeat bankruptcy problem?[183]

[182] See results of trusee survey found in Stephanie Ben-Ishai & Saul Schwartz, "Bankruptcy for the Poor?" (2007), 45 Osgoode Hall L.J. 471, at p. 501.

[183] Creditor #2, Creditor Responses to Question Four, Appendix C, AEB Report, *supra,* footnote 14; Access to Information Act, *supra*, footnote 94; Strand, Hira & Carter, *supra*, footnote 17, at p.35. On the issue of responsible lending see Jacob Ziegel, "Consumer Insolvencies, Consumer Credit and Responsible Lending," online: <http://www.cairp.ca/canadian-insolvency-foundation/houlden-fellowship/>.