

PERSONAL INSOLVENCY IN AUSTRALIA: AN INCREASINGLY MIDDLE CLASS PHENOMENON

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Under the Bankruptcy Act 1966 (Cth), there are three regulated forms of personal insolvency: bankruptcy, debt agreements, and personal insolvency agreements. Between 1990 and 2008 there was a 261% increase in the number of personal insolvencies in Australia. We suggest one important aspect of this increase is that Australian personal insolvency has become an increasingly middle class phenomenon. Whilst the concept of middle class is not readily quantifiable, we suggest that several factors reveal that personal insolvency is affecting those who might generally be considered middle class. Our findings have implications for Australia's personal insolvency laws. The findings also raise for consideration the connections between personal insolvency laws and broader social issues such as rising debt levels, spending habits and social welfare benefits.

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I INTRODUCTION

In 2008, Australia experienced a record high of 32,865 personal insolvencies.¹ The magnitude of this figure is augmented when placed in the context of the 261% increase seen in the number of Australian personal insolvencies between 1990 and 2008. This growth far exceeded the 24% increase in the Australian population during that period.² It is indisputable that personal insolvency is affecting a growing number of Australians.

This rise in the number of personal insolvencies took place over periods of economic expansion and low interest rates (as well as the converse), which indicates that the increase is not attributable solely to prevailing economic conditions. In this article we suggest that one important feature of the significant increase is that personal insolvency in Australia has become an increasingly middle class phenomenon. Whilst the concept of middle class is not readily quantifiable, we suggest that increases in the proportion of insolvents with certain characteristics reveals that personal insolvency is affecting a broad section of the population, and increasingly it is affecting those who might commonly be perceived to represent middle class Australians.

We begin with a brief explanation of Australian personal insolvency law. Then we provide background information including details on the methodology of our study; the increasing rate of Australian personal insolvencies; and the results of similar studies conducted in the US. Then we evaluate the concept of middle class, before considering several factors which we suggest indicate that personal insolvency in Australia is becoming a middle class phenomenon. We detail how insolvents are increasingly coming from higher status occupations; have increasing levels of personal income and household income; and have increasing asset and property

¹ Insolvency and Trustee Service Australia, *Annual Report by the Inspector-General in Bankruptcy on the Operation of the Bankruptcy Act 2007-2008*, 9. This figure relates to the financial year 2007-2008. Provisional statistics for the financial year 2008-2009 reveal that this figure is likely to increase. On these provisional statistics, there were 36,479 personal insolvencies in 2009, which would represent an 11% increase on 2008 figures, and a 300% increase in the number of personal insolvencies between 1990 and 2009. See further <www.itsa.gov.au>.

² This article draws in part on the findings of our research report on Australian personal insolvency: see Ian Ramsay and Cameron Sim, *Trends in Personal Insolvency in Australia* (Research Report, Centre for Corporate Law and Securities Regulation, The University of Melbourne, 2009). The report is available online at <<http://cclsr.law.unimelb.edu.au>>. The report outlines the data on trends in personal insolvency. In this article, we analyse the key implications of the data.

ownership levels. Finally, we consider some implications of our findings for the role, function and importance of Australian personal insolvency laws and we also consider the connections between personal insolvency laws and broader social issues such as rising debt levels.

II AUSTRALIAN PERSONAL INSOLVENCY LAW

The *Bankruptcy Act 1966* (Cth) (“the Act”) sets out Australian law relating to the insolvency of individuals, deceased debtors and partnerships.³ Under the Act, there are three regulated forms of personal insolvency: bankruptcies under Part IV and Part XI; debt agreements under Part IX; and Part X arrangements. Whilst bankruptcies make up the large majority of personal insolvencies (25,970 or 79.02% in 2008), the popularity of debt agreements has risen sharply following their introduction in 1996. In 2008 there were 6,618 debt agreements, accounting for 20.14% of personal insolvencies. Personal insolvency agreements under Part X of the Act are less commonplace; in 2008, there were only 277, accounting for 0.84% of personal insolvencies. In this section we set out a summary of Australian personal insolvency law relating to Part IV bankruptcies and Part IX debt agreements.⁴

A *Bankruptcy (Part IV of the Bankruptcy Act)*

Bankruptcy offers debtors protection from creditors, however this protection comes with serious consequences for the debtor involved. A debtor may become bankrupt on either a voluntary or involuntary basis. If certain requirements are fulfilled,⁵ then a creditor may petition the court to make a sequestration order against the estate of a debtor.⁶ It is at the discretion of the court to make such an order, declaring the debtor to be bankrupt.⁷ Alternatively, an individual debtor, partnership,⁸ or joint debtors,⁹

³ Corporate insolvency is governed by the *Corporations Act 2001* (Cth).

⁴ We exclude Part X insolvents from this article as a result of their small numbers. A more detailed explanation of the Australian personal insolvency regime, including further detail on Part IV bankruptcies, Part IX debt agreements, bankruptcies under Part XI, and current and former Part X arrangements, is available in our report: see Ramsay and Sim, above n 2, 29-38. See further Michael Murray, *Keay's Insolvency: Personal and Corporate Law and Practice* (6th ed, 2008).

⁵ *Bankruptcy Act 1966* (Cth) ss 40, 43, 44, 52.

⁶ *Bankruptcy Act 1966* (Cth) s 43(1). The debtor must have committed an act of bankruptcy within six months before presentation of the petition (ss 40, 44(1)(c)), and the debt owed must be for a minimum of \$2000 (s 44(1)(a)).

⁷ *Bankruptcy Act 1966* (Cth) ss 43(2), 52.

⁸ *Bankruptcy Act 1966* (Cth) s 56A(1).

⁹ *Bankruptcy Act 1966* (Cth) s 57(1).

may voluntarily present a bankruptcy petition to the Official Receiver.¹⁰ The debtor becomes bankrupt on the day of acceptance of the petition by the Official Receiver.¹¹

Upon bankruptcy, the property of the debtor vests in a trustee in bankruptcy,¹² subject to certain exemptions,¹³ such as most ordinary household or personal items,¹⁴ and limited tools of trade.¹⁵ Aside from exemptions, all other property of the debtor vests in the trustee in bankruptcy. The trustee will also investigate assets owned prior to bankruptcy.¹⁶ Certain conduct committed prior to and after bankruptcy may constitute an offence under the Act.¹⁷

In addition, limitations are placed on the personal lives of bankrupts. A bankrupt is required to give their passport to the trustee,¹⁸ and is unable to continue or commence legal proceedings.¹⁹ Bankruptcy is also a bar to certain occupations, such as holding a parliamentary seat, or the management of a corporation,²⁰ and it may result in termination of the holding of a statutory office, or membership of a statutory authority. If the after-tax income of a bankrupt exceeds a certain amount, they must pay contributions from this income to the trustee.²¹ Details of the bankruptcy are permanently entered onto the National Personal Insolvency Index, available for public inspection.²² When entering into certain transactions of \$3,000 or more, for example when obtaining credit,²³ bankrupts must inform other parties that they are an undischarged bankrupt.²⁴

¹⁰ *Bankruptcy Act 1966* (Cth) s 55.

¹¹ *Bankruptcy Act 1966* (Cth) ss 55(4A), 55(8).

¹² *Bankruptcy Act 1966* (Cth) s 54(1).

¹³ *Bankruptcy Act 1966* (Cth) ss 5(1), 58, 116. See also *Bankruptcy Regulations 1996* (Cth) Division 4A.

¹⁴ *Bankruptcy Act 1966* (Cth) s 116(2)(b).

¹⁵ *Bankruptcy Act 1966* (Cth) s 116(2)(c).

¹⁶ *Bankruptcy Act 1966* (Cth) ss 120, 121, 121A, 122.

¹⁷ *Bankruptcy Act 1966* (Cth) s 271.

¹⁸ *Bankruptcy Act 1966* (Cth) s 77(1)(a)(ii).

¹⁹ *Bankruptcy Act 1966* (Cth) s 60.

²⁰ *Corporations Act 2001* (Cth) s 206B(3).

²¹ *Bankruptcy Act 1966* (Cth) s 139P. On 22 October 2008, the indexed income threshold amount for a bankrupt with no dependants was \$41,250.30; for a bankrupt with over four dependants, this amount was \$56,100.41.

²² *Bankruptcy Regulations 1996* (Cth) Part 13.

²³ *Bankruptcy Act 1966* (Cth) s 269(1)(a).

²⁴ *Bankruptcy Act 1966* (Cth) s 269.

Bankruptcy does not affect the rights of secured creditors to realise or otherwise deal with their security.²⁵ The main consequences for unsecured creditors are, subject to certain exceptions,²⁶ that they are unable to enforce a remedy in respect of provable debts against the bankrupt or their property,²⁷ and, except with the leave of the court, they are unable to commence or take any fresh steps in legal proceedings against the bankrupt in respect of provable debts.²⁸

There are several grounds on which a bankruptcy may be annulled.²⁹ In essence, the effect of annulment is that the bankrupt is treated as if they had not been bankrupt. Otherwise, a bankrupt may be discharged from bankruptcy. In the absence of an objection to the discharge, a bankrupt is automatically discharged from bankruptcy three years after filing their Statement of Affairs.³⁰ An objection by the trustee to an automatic discharge may extend the bankruptcy to five years,³¹ or to eight years in more severe cases.³² Discharge from bankruptcy releases the bankrupt from all provable debts in relation to the bankruptcy, subject to exceptions.³³ Unsold assets in the bankruptcy are not automatically returned to the bankrupt and may still be sold by the trustee.

Following discharge, the National Personal Insolvency Index is updated to reflect that the person is now a discharged bankrupt. Records of bankruptcies are also kept by credit reporting organisations. Discharged bankrupts might experience difficulty in borrowing money or making purchases on credit, and often a bond will be required before a discharged bankrupt is able to rent, or obtain connection to electricity, water, or telephone services.

²⁵ *Bankruptcy Act 1966* (Cth) s 58(5).

²⁶ *Bankruptcy Act 1966* (Cth) ss 58(4), 58(5A)(a), 58(5A)(b).

²⁷ *Bankruptcy Act 1966* (Cth) s 58A(3)(a).

²⁸ *Bankruptcy Act 1966* (Cth) s 58A(3)(b).

²⁹ These grounds include where the debts have been paid in full (s 153A(1)); where creditors accept a composition or scheme of arrangement (s 74(5)); or where a court is satisfied either that a sequestration order ought not to have been made in the first place, or that a debtor's petition ought not to have been accepted by the Official Receiver (s 153B).

³⁰ *Bankruptcy Act 1966* (Cth) s 149.

³¹ *Bankruptcy Act 1966* (Cth) s 149A(2)(a)(i).

³² *Bankruptcy Act 1966* (Cth) s 149A(2)(a)(ii).

³³ *Bankruptcy Act 1966* (Cth) s 153. These exceptions include penalties and fines imposed by a court, child support debts, and debts incurred by fraud.

B Debt Agreements (Part IX of the Bankruptcy Act)

One alternative to bankruptcy available for some insolvent debtors is to enter into a debt agreement under Part IX of the Act. Debt agreements were introduced on 16 December 1996 to allow those with low levels of debt, few assets, low incomes, and an inability to afford to enter into arrangements under Part X of the Act, to avoid the consequences of bankruptcy.³⁴

An insolvent debtor³⁵ may propose a debt agreement to the Official Receiver,³⁶ in which the debtor makes a ‘best offer’ to their creditors, who in turn vote on that offer.³⁷ The debtor must have a future expected after tax income,³⁸ unsecured debts,³⁹ and divisible property,⁴⁰ falling under prescribed limitations.⁴¹ On 20 September 2008, these limitations were a future expected after tax income of less than \$61,875.45;⁴² unsecured debts of less than \$82,500.60;⁴³ and divisible property valued at less than \$82,500.60.⁴⁴ The proposal of a debt agreement is an act of bankruptcy, which may be used by a creditor to apply to court for a sequestration order, even before creditors vote on the debt agreement.⁴⁵

If the Official Receiver accepts the proposal for processing,⁴⁶ the proposal is sent to all creditors for voting by postal vote.⁴⁷ A majority of creditors representing a majority in number and at least 75% in value must vote in favour for the proposal to be accepted.⁴⁸ If this majority is secured then all creditors are bound by the debt

³⁴ Commonwealth, *Parliamentary Debates*, House of Representatives, 26 June 1996, 2827-8 (Daryl Williams, Attorney-General and Minister for Justice).

³⁵ In the past ten years the debtor must not have been a bankrupt, had a debt agreement, or had a Part X arrangement: *Bankruptcy Act 1966* (Cth) s 185C(4)(a)(i)-(iii).

³⁶ *Bankruptcy Act 1966* (Cth) s 185C(1).

³⁷ The proposal may provide for any matter relating to the debtor’s financial affairs: s 185C(3). However, the proposal must meet several requirements: *Bankruptcy Act 1966* (Cth) s 185C(2). One such requirement is that all provable debts in relation to the debt agreement must rank equally: s 185C(2)(d)(i).

³⁸ *Bankruptcy Act 1966* (Cth) s 185C(4)(d).

³⁹ *Bankruptcy Act 1966* (Cth) s 185C(4)(b).

⁴⁰ *Bankruptcy Act 1966* (Cth) s 185C(4)(c).

⁴¹ *Bankruptcy Act 1966* (Cth) s 185C(4).

⁴² *Bankruptcy Act 1966* (Cth) s 185C(4)(d).

⁴³ *Bankruptcy Act 1966* (Cth) s 185C(4)(b).

⁴⁴ *Bankruptcy Act 1966* (Cth) s 185C(4)(c). Divisible property includes any equity held in property, which would include any equity held in the family home.

⁴⁵ *Bankruptcy Act 1966* (Cth) s 40(1)(ha).

⁴⁶ *Bankruptcy Act 1966* (Cth) s 185E(2).

⁴⁷ *Bankruptcy Act 1966* (Cth) s 185EA.

⁴⁸ *Bankruptcy Act 1966* (Cth) s 185EC.

agreement.⁴⁹ Details of the debt agreement are entered onto the National Personal Insolvency Index.⁵⁰ While in force, creditors cannot present or proceed with an existing creditor's petition against the debtor;⁵¹ enforce a remedy against the debtor or their property; nor take a fresh step in legal proceedings in respect of a provable debt.⁵² However, secured creditors may still seize and sell any assets which the debtor had offered as security for credit if the debtor is in default under the original agreement with the secured creditor.

Once in place, the debtor or a creditor may propose a variation or termination of the debt agreement to the Official Receiver,⁵³ which may then be voted on in the same manner as for the initial debt agreement proposal.⁵⁴ The debtor, creditors, or the Official Receiver may also apply to the court for an order declaring that the debt agreement is void.⁵⁵ A debt agreement may also be terminated by order of the court,⁵⁶ or if the debtor becomes a bankrupt.⁵⁷ Otherwise, a debt agreement ends when the obligations it created have been discharged.⁵⁸ The debtor is released from provable debts in the same way as if the debtor had been discharged from bankruptcy immediately after the debt agreement proposal was recorded on the National Personal Insolvency Index.⁵⁹ The debtor is entitled to any property that was subject to the debt agreement but that was not distributed to creditors.⁶⁰ On a practical level, the debtor's credit rating will be affected, which will diminish the ability of the debtor to obtain further credit.

III BACKGROUND TO THE STUDY

In this section we set out information which forms the background for our contention on Australian personal insolvency and the middle class. First, we outline the

⁴⁹ *Bankruptcy Act 1966* (Cth) s 185EC.

⁵⁰ *Bankruptcy Act 1966* (Cth) s 185H.

⁵¹ *Bankruptcy Act 1966* (Cth) ss 185K(1)(a), 185K(1)(b).

⁵² *Bankruptcy Act 1966* (Cth) s 185K(1)(c). However, this does not prevent a creditor from enforcing a remedy under a maintenance agreement, a maintenance order, or a proceeds of crime law: see *Bankruptcy Act 1966* (Cth) s 185K(1)(2).

⁵³ *Bankruptcy Act 1966* (Cth) ss 185M, 185P.

⁵⁴ *Bankruptcy Act 1966* (Cth) ss 185MA, 185MC, 185PA, 185PC.

⁵⁵ *Bankruptcy Act 1966* (Cth) s 185T.

⁵⁶ *Bankruptcy Act 1966* (Cth) s 185Q.

⁵⁷ *Bankruptcy Act 1966* (Cth) s 185R.

⁵⁸ *Bankruptcy Act 1966* (Cth) s 185N(1).

⁵⁹ *Bankruptcy Act 1966* (Cth) s 185NA(1).

⁶⁰ *Bankruptcy Act 1966* (Cth) s 185N(2).

methodology of our study. Second, we detail the growing rate of Australian personal insolvencies. Third, we consider research on bankrupts from the US, where a similar argument on bankruptcy and the middle class has been advanced.

A *Methodology of the study*

We obtained data from two sets of publications of the Insolvency and Trustee Service Australia ('ITSA'), the executive agency responsible for the administration and regulation of Australia's personal insolvency system. These were the 'Annual Report of the Inspector-General in Bankruptcy on the operation of the Bankruptcy Act' ('the Annual Reports') for each year between 1990 and 2008, as well as all 'Profiles of Debtors' ('the Profiles') in existence.⁶¹ We also obtained data from Australian Bureau of Statistics and Reserve Bank of Australia publications.

The socio-economic data in both the Annual Reports and the Profiles to which we refer is based on information contained in the Statements of Affairs of personal insolvents. These are lodged at different times in the process of the personal insolvency, depending on the nature of both the application for and form of insolvency.⁶² For our purposes, we assume that information given in the Statement of Affairs is truthful, as it is an offence to sign a false declaration made in the Statement of Affairs.⁶³

We base our analysis on the characteristics of personal insolvents using data between 1997 and 2008 for two reasons. First, debt agreements came into existence on 16 December 1996, and so data from both the calendar and financial year 1997 represents the first data available for debt agreement debtors. Second, 1997 is the first year for which data contained in the Profiles is available.

In this article, all data relating to the characteristics of personal insolvents comes from the Profiles and relates to the calendar year in question with certain exceptions. First, all data relating to the occupational status of insolvents, the causes of personal

⁶¹ The Annual Reports are published pursuant to the *Bankruptcy Act 1966* (Cth) s 12. Copies of the Annual Reports from 1999 onwards and the Profiles of Debtors in 2002, 2003, 2005, and 2007, are available at www.itsa.gov.au.

⁶² See *Bankruptcy Act 1966* (Cth) ss 54(1)(a), 54(2)(a), 55(2)(b), 556B(1), 56F(1)(a), 56F(1)(b), 57(1), 185C(2B), 185D, 185M(1B), 185P(1B), 188(2C), 188(2D).

⁶³ *Bankruptcy Act 1966* (Cth) s 267.

insolvency, the business/non-business classification of insolvency, and the number of personal insolvencies, comes from the Annual Reports and is based on the financial year in which the Annual Report was released. Second, all data from the Profiles in 2002 is based on financial year figures for the financial year 2001-2002.

Further, we refer only to *new* personal insolvency administrations commencing in the relevant year. We do not refer to cumulative data. For example, whilst personal insolvencies from the Profiles in 2005 might still be in force in 2007, data relating to these existing administrations is not included in the 2007 data. It is therefore important to keep in mind that when we refer to a certain number of personal insolvents in a given year this is a reference to new personal insolvencies in that year and not the total number of personal insolvencies. Finally, data in the Profiles is based on whole numbers, and so occasionally data from the Profiles may not always add to 100%.⁶⁴

B *Growing rate of Australian personal insolvencies*

Over the last two decades in Australia, growth in personal insolvency activity has averaged almost 6.5% per annum.⁶⁵ Between 1990 and 2008 there was a 261% increase in the number of Australian personal insolvencies, significantly greater than the 24% increase in the Australian population during that period. In 1990, 0.05% of the Australian population entered into personal insolvency, compared to 0.15% in 2008. This increase constitutes the background for our argument that Australian personal insolvency is becoming an increasingly middle class phenomenon, and therefore further discussion of this overall increase in personal insolvency is warranted.⁶⁶

Personal insolvency numbers were rising significantly even before the introduction of debt agreements on 16 December 1996.⁶⁷ In 1990 there were 8,552 bankruptcies, compared to 21,830 bankruptcies in 1997 and 25,970 bankruptcies in 2008. Whilst it appears there were several factors behind the increase in personal insolvencies

⁶⁴ Further details on methodology are available in our research report: see Ramsay and Sim, above n 2, 27-8.

⁶⁵ Insolvency and Trustee Service Australia, *Annual Report by the Inspector-General in Bankruptcy on the Operation of the Bankruptcy Act 2007-2008*, 7.

⁶⁶ See further Ramsay and Sim, above n 2, 9-26, 130-42.

⁶⁷ See further *ibid*, 39-44.

(including, among other factors, significant increases in bankruptcies in New South Wales and in personal insolvencies caused by excessive use of credit, ill health, and gambling or speculation),⁶⁸ perhaps the most influential factor behind the rise has been the increase in non-business related personal insolvencies.

Personal insolvency is business related if the personal insolvency is considered by the insolvent to be directly related to their proprietary interest in a business; otherwise it is non-business related.⁶⁹ The number of business related bankruptcies did not increase significantly between 1991 and 2008, in contrast to the increase in the number of non-business related bankruptcies. There were 387 more business related bankruptcies in 2008 than in 1991, compared to 12,492 more non-business related bankruptcies in 2008 than in 1991. On the figures available for debt agreements, there were 261 less business related debt agreements in 2003 than in 2008, yet there were 2,329 more non-business related debt agreements in 2008 than in 2003. Therefore, the rise in the number of personal insolvencies is substantially attributable to an increase in the number of non-business related personal insolvencies.

The question then arises: why has Australia seen such a significant increase in personal insolvencies and, more specifically, non-business related personal insolvencies? Is the increase explicable in some broader context? We suggest that a feature of this increase in Australian personal insolvencies is that personal insolvency is increasingly affecting middle class Australians. Before exploring this argument in further detail, it is useful to comment on similar findings made in the US.

C *Bankrupts in the US*

In depth studies on bankrupts in the US have been conducted for over three decades,⁷⁰ in stark contrast to a dearth of Australian research.⁷¹ As a result of those studies in the

⁶⁸ See further *ibid*, 130-7.

⁶⁹ See further *ibid*, 54.

⁷⁰ There have been four major studies on consumer bankruptcy in the US: Consumer Bankruptcy Project I (1981); Consumer Bankruptcy Project II (1991); Consumer Bankruptcy Project III (2001); and Consumer Bankruptcy Project IV (2007). For a useful description of the Consumer Bankruptcy Projects, see Robert M Lawless, Angela K Littwin, Katherine M Porter, John A E Pottow, Deborah K Thorne and Elizabeth Warren, 'Did Bankruptcy Reforms Fail? An Empirical Study of Consumer Debtors' (2008) 82 *American Bankruptcy Law Journal* 349, 387-98. See further Teresa A Sullivan, Elizabeth Warren and Jay Lawrence Westbrook, *As We Forgive Our Debtors: Bankruptcy and Consumer Credit in America* (1989); Teresa A Sullivan, Elizabeth Warren and Jay Lawrence Westbrook, *The Fragile Middle Class: Americans in Debt* (2000).

US, it has been argued by Professor Elizabeth Warren and others that bankruptcy is a middle class phenomenon.⁷² Based on educational achievements, occupational status, and the ability to buy homes, those who file for bankruptcy in the US are thought to be ‘an overwhelmingly middle-class group, a cross-section of America that concentrates its numbers in the middle’.⁷³

The three indicia of middle class used to come to this conclusion were, first, whether bankrupts were homeowners or former homeowners; second, whether bankrupts had college or graduate school education level; and third, whether bankrupts had occupational prestige in the upper 80%. The study found that 91.8% of those filing for bankruptcy fulfilled at least one of those three criteria; 66.6% met two or more criteria; and 27.4% met all three criteria.⁷⁴ Bankrupts in the US were found to have educational achievements keeping pace with those of other Americans;⁷⁵ becoming more likely to be homeowners;⁷⁶ although remaining more concentrated in lower prestige jobs.⁷⁷ For this reason, Professor Warren has argued that her studies on bankruptcy reveal that Americans in the worst financial trouble are not the ‘usual suspects’.⁷⁸

⁷¹ Others have pointed out this lack of research. See, eg, Rosalind Mason, ‘Consumer Bankruptcy: An Australian Perspective’ (1999) 37 *Osgoode Hall Law Journal* 449, 458; Rosalind Mason and John Duns, ‘Developments in Consumer Bankruptcy in Australia’ in Johanna Niemi-Kiesiläinen, Iain Ramsay and William Whitford (eds), *Consumer Bankruptcy in Global Perspective* (2003) 227, 227-8. We found one study including empirical research on consumer bankrupts in Melbourne between 1986 and 1987: see Martin Ryan, ‘Consumer Bankrupts in Melbourne’ (1993) 28 *Australian Journal of Social Issues* 34.

⁷² Sullivan, Warren and Westbrook, *The Fragile Middle Class*, above n 70, 27. See further Sullivan, Warren and Westbrook, *As We Forgive Our Debtors*, above n 70; Elizabeth Warren, ‘Bankrupt Children’ (2002) 86 *Minnesota Law Review* 1003; Elizabeth Warren, ‘Financial Collapse and Class Status: Who Goes Bankrupt?’ (2003) 41 *Osgoode Hall Law Journal* 115; Elizabeth Warren, ‘The Growing Threat to Middle Class Families’ (2003) 69 *Brooklyn Law Review* 401; David U Himmelstein, Elizabeth Warren, Deborah Thorne and Steffie J Woolhandler, *Illness and Injury as Contributors to Bankruptcy* (February 2005); Teresa A Sullivan, Elizabeth Warren and Jay Lawrence Westbrook, *Less Stigma or More Financial Distress: An Empirical Analysis of the Extraordinary Increase in Bankruptcy Filings* (May 2006).

⁷³ Elizabeth Warren, ‘Financial Collapse and Class Status: Who Goes Bankrupt?’ (2003) 41 *Osgoode Hall Law Journal* 115, 118-9.

⁷⁴ *Ibid* 143-4.

⁷⁵ *Ibid* 128.

⁷⁶ *Ibid* 137. A recent study in the US found that parents were more likely than non-parents to file for bankruptcy in order to save their homes: see Eric S Nguyen, ‘Parents in Financial Crisis: Fighting to Keep the Family Home’ (2008) 82 *American Bankruptcy Law Journal* 229.

⁷⁷ *Ibid* 134.

⁷⁸ Elizabeth Warren, ‘The Growing Threat to Middle Class Families’ (2003) 69 *Brooklyn Law Review* 401, 402.

According to Professor Warren, Americans who encounter the greatest financial difficulties:

are not the very young, tempted by the freedom of their first credit cards. They are not the elderly, trapped by failing bodies and declining savings accounts. And they are not a random assortment of Americans who lack the self-control to keep their spending in check.⁷⁹

Taken as a whole, the studies reached the conclusion that US bankrupts were ‘likely to be middle class people in terrible financial trouble’.⁸⁰

We are limited in our ability to draw comparisons between our data and the US data from which this conclusion was drawn. While we have data on occupations and property ownership, we do not have data on educational achievements.⁸¹ Moreover, the data is not broken down for each individual insolvent, which means that we cannot verify how many insolvents would fulfil one or more criteria. Furthermore, the personal insolvency systems of Australia and the US vary, and comparisons between them are inherently difficult to make. There exist not only differences in the administration and regulation of personal insolvency, but also different statistical methodologies employed in the collation of data. Therefore, although the US findings are of interest, it is not possible to make direct comparisons between the Australian and US data.

IV MIDDLE CLASS PHENOMENON

In light of this background information, we now turn to develop our argument that personal insolvency in Australia is becoming an increasingly middle class phenomenon. First, we consider the concept of middle class. Second, we outline evidence to support our contention, by providing characteristics of personal insolvents vis-à-vis what in our view might commonly be perceived as middle class characteristics.

⁷⁹ Ibid.

⁸⁰ Warren, ‘Bankrupt Children’, above n 72, 1005.

⁸¹ See further above Part III(A) on methodology.

A *The concept of middle class*

The concept of middle class is not readily quantifiable. Many factors might be considered in defining middle class. These might include tangible factors, such as education, occupation, and income. They might also include intangible factors, such as beliefs, cultural factors, and social status. Class analysis is a political exercise insofar as it is concerned with the political nature of the social structure,⁸² and in this sense it is an analysis of power.⁸³ Perhaps for these reasons, and despite being a term with such wide usage, the problem of defining and understanding the middle class has been described as an ‘old’⁸⁴ and ‘vexatious’⁸⁵ dilemma, part of a ‘conceptual muddle’⁸⁶ in a ‘sociological minefield of conflicting analyses, ideologies and criticisms’.⁸⁷ Are classes to be defined in the Marxist conception as the relations between groups of people within the system of production, or should Weberian notions prevail, under which classes are seen as aggregations of individuals who receive similar rewards from the systems of distribution and consumption?⁸⁸ Or is Australian society becoming so homogenous that it is no longer useful to analyse it in class terms?

We do not intend to contribute to debates concerning the definition of middle class.⁸⁹ The concept of middle class evidently is not definitive. One alternative way to deal with the concept of middle class has been put forward to avoid asserting rival definitions. This is to present social class ‘as authors’ definitions rather than *the* definition’.⁹⁰ This approach allows the development of argument on phenomena affecting particular groups within society without being overly obstructed by a protracted definitional debate. Furthermore, this approach accords with common

⁸² R W Connell and T H Irving, *Class Structure in Australian History* (1980) 1.

⁸³ *Ibid* 17.

⁸⁴ Tim Butler, ‘The Debate Over the Middle Classes’ in Tim Butler and Mike Savage (eds), *Social Change and the Middle Classes* (1995) 26-39, 26.

⁸⁵ John S Western, *Social Inequality in Australian Society* (1983) 10.

⁸⁶ K Roberts, F G Cook, S C Clark, and E Semeonoff, *The Fragmentary Class Structure* (1977) 16.

⁸⁷ Craig McGregor, *Class in Australia* (2nd ed, 2001) 33.

⁸⁸ Carolyn Howe, *Political Ideology and Class Formation: A Study of the Middle Class* (1992) 6.

⁸⁹ For different conceptions of ‘middle class’ in Australian society see further Connell and Irving, above n 82, 1-30; Western, above n 85, 9-40; Leonard Broom and F L Jones, *Opportunity and Attainment in Australia* (1976) 60-84; R A Wild, *Social Stratification in Australia* (1978) 40-67; Leonard Broom, F L Jones, Patrick McDonnell and Trevor Williams, *The Inheritance of Inequality* (1980) 20-56. See generally McGregor, above n 87.

⁹⁰ Roberts, Cook, Clark and Semeonoff, above n 86, 17. See also Chris Chamberlain, *Class Consciousness in Australia* (1983) x – xi (emphasis in original).

perception. It is arguable that significant numbers of Australians readily identify with the concept of middle class, even if perceptions over its boundaries may differ. Whilst there does not appear to be broad evidence on identification with class terms,⁹¹ there does seem to be some acceptance that there is an Australian middle class,⁹² even if it is divided between upper and lower middle class.⁹³ Indeed, Australia has even been labelled the most middle-class nation in the world.⁹⁴

Professor Warren based her middle class criteria for US bankrupts on educational achievements, occupational status, and the ability to buy homes.⁹⁵ Australian data on education levels of personal insolvents is not available. However, we have obtained data on occupational status and property ownership for personal insolvents, and these seem to be important middle class indicators. Other Australian studies have identified the significance of occupational status, not least because occupational aspirations sometimes depend on family background and school experience,⁹⁶ but also because occupation plays a large role in socio-economic stratification.⁹⁷ We have also obtained data on both personal and household income levels for personal insolvents, which might play a role in class status.⁹⁸ A 2007 study defined middle class solely on disposable household income,⁹⁹ and a study in the year 2000 found that 93% of Australians believed they were in the middle-income bracket.¹⁰⁰ Finally, we have obtained data on levels of realisable assets of personal insolvents, which might also be seen as relevant to determining class status insofar as these levels concern the potential wealth of insolvents. Whilst these five characteristics of personal insolvents are by no means definitive factors in the determination of middle class status, we

⁹¹ Clive Hamilton, Christian Downie and Yi-Hua Lu, *The State of the Australian Middle Class* (The Australia Institute, Discussion Paper No 98, October 2007) 9.

⁹² See the various studies cited above n 89.

⁹³ McGregor, above n 87, 36-7; R A Wild, above n 89, 53; Chamberlain, above n 90, 39-42; Western, above n 85, 36-44.

⁹⁴ McGregor, above n 87, 19.

⁹⁵ Warren, 'Financial Collapse and Class Status: Who Goes Bankrupt?', above n 73, 118-9.

⁹⁶ Broom, Jones, McDonnell and Williams, above n 89, 13.

⁹⁷ Broom and Jones, above n 89, 118.

⁹⁸ See also Warren, 'Financial Collapse and Class Status: Who Goes Bankrupt?', above n 73, 123-7.

⁹⁹ In that study, the middle class was defined as those with disposable incomes higher than the bottom 30% and lower than the richest 20%. See Hamilton, Downie and Yi-Hua Lu, above n 91, 9.

¹⁰⁰ A further 6.4% believed they were in the bottom 20% income bracket, and 0.7% believed they were in the top 20% income bracket. See P Saunders, C Thomson and C Evans, *Social Change and Social Policy: Results From a National Survey of Public Opinion* (Discussion Paper No 106, Social Policy Research Centre, University of New South Wales, Sydney, 2000) 19.

place reliance on these factors to argue that personal insolvency in Australia has become an increasingly middle class phenomenon.

B *Middle class factors*

During a time of significantly increasing numbers of personal insolvencies, simultaneous increases in the proportion of bankrupts and debt agreement debtors who are from higher prestige occupations and who have higher levels of personal income, household income, property ownership, and realisable assets, reveal that personal insolvency is spreading across many areas of Australian society and is upwardly mobile.

1 *Occupation*

Australia has seen significant increases in the proportion of personal insolvents from higher prestige occupational groups. These insolvents are managers and administrators, professionals, and associate professionals, classified according to the Australian Standard Classification of Occupations.¹⁰¹ Professionals include occupations such as accountants, lawyers, doctors, dentists, and teachers. Associate professionals include occupations such as shop managers, hotel and motel managers, and financial dealers and brokers. These occupations might be seen as having typically middle class qualities.¹⁰²

In 1999, there were 26,045 bankrupts, of whom 2,937 or 11.28% were managers and administrators, professionals, or associate professionals. In 2008, there were 26,137 bankrupts, of whom 7,147 or 27.34% came from these occupational groups. There were only 92 more bankrupts in 2008 than in 1999, however there were 4,210 more bankrupts from these occupational groups in 2008 than in 1999. This represents an increase of 142% between 1999 and 2008. The greatest increase occurred in the proportion of bankrupts who are managers or administrators. In 1999, 840 or 3.23% of bankrupts were managers and administrators, compared to 3,279 or 12.55% in 2008. The increase in the proportion of bankrupts who are professionals and associate professionals is also significant. In 1999, 1,065 bankrupts or 4.09% were

¹⁰¹ *Australian Standard Classification of Occupations* (2nd ed, 1997).

¹⁰² See, eg, Western, above n 85, 36-39, 44; Chamberlain, above n 90, 39-42.

professionals, compared to 1,614 or 6.18% in 2008. In 1999, 1,032 bankrupts or 3.96% were associates professionals, compared to 2,254 bankrupts or 8.62% in 2008.

Similarly, an increasing proportion of debt agreement debtors come from these occupational groups. In 2002, there were 4,056 debt agreement debtors, of whom 606 or 14.94% were managers and administrators, professionals, or associate professionals. In 2008, there were 6,620 debt agreement debtors, of whom 1,800 or 27.19% came from these occupational groups, which represents an increase of 82% between 2002 and 2008. There were 2,564 more debt agreement debtors in 2008 than in 2002, and there were 1,194 more debt agreement debtors from these occupational groups in 2008 than in 2002.

2 *Personal income*

Personal insolvents have increasing levels of personal income. These increases in personal income levels may be related to increases in the proportion of insolvents who are employed (between 1997 and 2007 there was a 70% increase in the employment rate of bankrupts and a 46% increase in the employment rate of debt agreement debtors)¹⁰³ and who are from higher prestige occupational groups. Our data relates to personal gross income between 1997 and 2007 and is declared by insolvents on their Statement of Affairs. In 1997, Australian real net disposable income per person was \$29,400, compared to \$39,000 in 2007, an increase of around 33%.¹⁰⁴

In 1997, 37% of bankrupts had personal income of less than \$10,000, and 13% had personal income of \$30,000 or more. In 2007, these proportions were almost inverted: 15% of bankrupts had personal income of less than \$10,000, and 38% had personal income of \$30,000 or more. Further, 9% of bankrupts had personal income of \$50,000 or more in 2005, compared to 13% in 2007.

Income levels of debt agreement debtors are based on actual income in the past twelve months, excluding data from 2007, which relates to expected income in the 12 months following entry into the debt agreement. In 1997, 85% of debt agreement debtors had personal income less than \$30,000, and 15% had personal income of \$30,000 or more.

¹⁰³ In 1997, 33% of bankrupts were employed, compared to 56% in 2007. In 1997, 63% of debt agreement debtors were employed, compared to 92% in 2007.

¹⁰⁴ Australian Bureau of Statistics, *Australian Social Trends 4102.0* (March 2009).

In 2007, 31% of debt agreement debtors expected personal income less than \$30,000, and 69% expected personal income of \$30,000 or more. Further, 12% of debt agreement debtors had personal income of \$50,000 or more in 2005, compared to 17% in 2007 who expected personal income of \$50,000 or more.

It is clear from this data that significant increases occurred between 1997 and 2007 in the personal income levels of personal insolvents. These higher incomes are possibly being generated from those in higher prestige occupational positions, which strengthens our contention that personal insolvency has become an increasingly middle class phenomenon.

3 *Household income*

Similarly, between 1997 and 2007 there were increases in the levels of insolvents' household income. In 2002, 28% of bankrupts had household income of \$30,000 or more, compared to 49% in 2007. The greatest increase occurred in the proportion of bankrupts with household income of \$50,000 or more. These represented 9% of bankrupts in 2002, compared to 24% in 2007. As with bankrupts, the household income levels of debt agreement debtors increased. In 2002, 55% of debt agreement debtors had household income of \$30,000 or more, compared to 73% in 2007. Again, the most significant increase occurred in the proportion of debt agreement debtors with household income of \$50,000 or more. These represented 16% of debt agreement debtors in 2002, compared to 36% in 2007. Evidently, levels of household income of personal insolvents are increasing.

4 *Realisable assets*

There have also been increases in the levels of realisable assets of bankrupts and debt agreement debtors, which indicates that these insolvents are coming from wealthier sections of the community than was previously the case.

The majority of bankrupts declare they have either no or very modest levels of realisable assets, although bankrupts' realisable asset levels increased between 2003 and 2007. In 2003, 3% of bankrupts declared realisable assets of \$50,000 or more, compared to 7% in 2007. In 2003, 2% of bankrupts declared between \$50,000 and

\$199,999 in realisable assets, compared to 4% in 2007. In 2003, only 1% of bankrupts declared realisable assets of \$200,000 or more, compared to 3% in 2007.

Similarly, the majority of debt agreement debtors declare they have either no or very modest levels of realisable assets.¹⁰⁵ However, the proportion of debt agreement debtors with higher levels of realisable assets increased between 2003 and 2007. In 2003, 5% of debt agreement debtors declared realisable assets of \$20,000 or more, compared to 9% in 2007. In 2003, 2% of debt agreement debtors declared realisable assets of \$50,000 or more, compared to 4% in 2007.

5 *Property ownership*

Between 2003 and 2007 there was an increase in the proportion of insolvents with property ownership. Property ownership is declared by insolvents in their Statement of Affairs. Insolvents must state whether they own or are purchasing any land or buildings in Australia or overseas, which includes any interest in vacant land, houses, units, or commercial properties (we refer to these interests collectively as ‘property ownership’). Between 2003 and 2007 there was a 120% increase in the proportion of bankrupts and a 200% increase in the proportion of debt agreement debtors who declared property ownership. In 2003, 5% of bankrupts declared property ownership, compared to 11% in 2007. In 2003, 5% of debt agreement debtors declared property ownership, compared to 15% in 2007.

V IMPLICATIONS OF FINDINGS

It is clear from this data that Australian personal insolvents are coming from higher status occupations; have increasing levels of personal and household income; and have increasing levels of property ownership and realisable assets. These changing characteristics of Australian personal insolvents, coupled with the 261% increase in personal insolvencies between 1990 and 2008, raise for consideration the policy underpinning the current Australian personal insolvency regime. We now discuss the role, function and importance of personal insolvency laws. We then consider

¹⁰⁵ Debt agreement debtors must have divisible property falling under prescribed limitations: *Bankruptcy Act 1966* (Cth) s 185C(4)(c).

connections between personal insolvency laws and broader social issues including rising debt levels and spending habits.

A *The role, function and importance of personal insolvency laws*

The changing demographics of Australian personal insolvents raise for consideration the role, function and importance of personal insolvency laws. The core policy objectives of the three forms of Australian personal insolvency administration (bankruptcies, debt agreements, and personal insolvency agreements) are the same, although these objectives are achieved in different ways.¹⁰⁶ All three forms of administration regulate the management of insolvent debtors and seek to balance the interests of debtors and creditors. The role of personal insolvency laws in balancing the interests of debtors and creditors means that these laws fulfil an important economic and social function, but one that is inevitably contested. Treatment of insolvent debtors has been said to constitute ‘the heart of what a society values’.¹⁰⁷ The change in the demographics of Australian personal insolvents has implications for the merits of particular views on the core policy objectives of personal insolvency laws.

The function of personal insolvency laws depends upon what their ultimate goal should be.¹⁰⁸ Australia has been placed in the liberal category of bankruptcy jurisdictions.¹⁰⁹ These jurisdictions are seen as offering levels of debt forgiveness with both a high degree of certainty and relative haste.¹¹⁰ This is in contrast to many other jurisdictions, which have been categorised as taking either a conservative or moderate approach to debt forgiveness, under which there is an absence of debt forgiveness provisions,¹¹¹ or the offer of debt forgiveness exists but is tempered by great

¹⁰⁶ See further above Section II for discussion of these forms of insolvency.

¹⁰⁷ Bruce H Mann, ‘Failure in the Land of the Free’ (2003) 77 *American Bankruptcy Law Journal* 1, 1.

¹⁰⁸ For a useful summary of varying positions, see Ziad Raymond Azar, ‘Bankruptcy Policy: An Empirical Investigation of 50 Jurisdictions Worldwide’ (2008) 82 *American Bankruptcy Law Journal* 407, 407-10.

¹⁰⁹ Rafael Efrat, ‘Global Trends in Personal Bankruptcy’ (2002) 76 *American Bankruptcy Law Journal* 81, 87-91

¹¹⁰ *Ibid.* Efrat identifies several other jurisdictions which have a similar approach, including the US, England and Wales, Canada, Hong Kong, New Zealand, Russia, Scotland, Taiwan, and The Netherlands.

¹¹¹ *Ibid.* 82-84. Efrat includes jurisdictions such as China, Vietnam, Mongolia, Bulgaria, Ukraine, Hungary, Turkey, Saudi Arabia, Italy, Greece, Brazil, Mexico, Argentina, Bolivia, El Salvador, Honduras, Panama, Venezuela, the Czech Republic, Chile, and Egypt.

uncertainty as to whether it will be granted.¹¹² Whereas these conservative or moderate approaches might be oriented towards creditors and informed by anti-debtor sentiment in societies that are intolerant of and punitive towards debtors,¹¹³ the liberal approach prioritises the concept of a ‘fresh start’ for debtors.¹¹⁴ Accordant with this observation, Australian courts have viewed the intention of Australia’s bankruptcy laws as serving a fair distribution of bankrupt’s assets among creditors, as well as allowing bankrupt debtors to start afresh.¹¹⁵ Consequently, personal insolvency laws reflect attempted reconciliation of two competing goals: a fresh start for debtors and protection of the interests of creditors (together with equality of distribution for creditors).¹¹⁶

This liberal categorisation of Australia’s personal insolvency laws reflects the approach taken to reform of these laws. In its first report on bankruptcy, the Australian Law Reform Commission (‘ALRC’) identified the need to strike a balance between the rehabilitation of debtors and the protection of the interests of creditors.¹¹⁷ In respect of the policy underpinning bankruptcy, the ALRC argued that the prime concern of the process should be the rehabilitation of debtors.¹¹⁸ It stated that honest bankrupts require education and assistance, not punishment.¹¹⁹ In making its recommendations,¹²⁰ the ALRC stated that in cases of over-commitment on the part of debtors, and also in cases where debtors experience a sudden change in financial circumstances:

the law must achieve a fair balance between the interests of the creditor and the debtor. It must uphold the general principle that debts which have been fairly incurred should be paid. But it must also deal humanely with those who suffer from overburdening debts. It must recognise that most insolvent debtors are honest and

¹¹² Ibid 84-87. Efrat includes jurisdictions such as India, Pakistan, Japan, Singapore, The Philippines, Denmark, Norway, Sweden, Finland, Austria, Germany, France, Portugal, Spain, Israel, South Africa, Kenya, and Uganda.

¹¹³ Ibid 91.

¹¹⁴ Ibid 91-109.

¹¹⁵ See, eg, *Storey v Lane* (1981) 147 CLR 549, 556-7; *Re McMaster; Ex parte McMaster* (1991) 33 FCR 70, 72-3.

¹¹⁶ Elizabeth Warren, ‘A Principled Approach to Consumer Bankruptcy’ (1997) 71 *American Bankruptcy Law Journal* 483, 483.

¹¹⁷ Australian Law Reform Commission, *Insolvency: The Regular Payment of Debts*, Report No 6 (1977).

¹¹⁸ Ibid [142].

¹¹⁹ Ibid.

¹²⁰ These included that non-business bankrupts should be discharged from bankruptcy six months after its commencement (and subject to objections to discharge): ibid [144] – [148].

wish to pay their debts if they can. It must also recognise that their failure to seek help usually indicates ignorance, shame or embarrassment, not fraud or dishonesty.¹²¹

This approach prioritises giving debtors a second chance and a clean slate with which to conduct their future financial affairs. Following the ALRC's report, the *Bankruptcy Amendment Act 1980* (Cth) liberalised Australia's bankruptcy laws, creating an automatic discharge from bankruptcy after a period of three years (subject to objections).¹²² It has been noted that this liberal approach corresponded to the deregulation of Australia's financial markets.¹²³

Issues associated with the timing of this liberalisation and deregulation shifts policy debate regarding personal insolvency laws away from a focus solely on balancing the interests of debtors and creditors to a broader debate in which personal insolvency laws might be seen, in part, as a substitute for consumer protection. In other words, personal insolvency laws might represent part of the regulation of consumer credit and its effects.¹²⁴ If liberalised consumer credit laws permit greater access to credit and this greater access leads to bankruptcy for some individuals, then personal insolvency laws allow a fresh start for debtors. However, this imposes a greater risk on credit providers who may not get paid all of the outstanding debt owed to them by personal insolvents. Credit providers may seek to pass this risk on to their customers in the form of higher interest rates. They may also seek more creditor friendly personal insolvency laws. Consequently, there exists a dynamic tension between personal insolvency laws and the credit industry.

Personal insolvency laws might also be seen as functioning to a certain extent as a form of social insurance.¹²⁵ This is either because personal insolvency transfers risk from a debtor (the insured) to their creditor (the insurer), or because personal insolvency provides protection to individuals who miss out on economic security

¹²¹ Ibid 1-2.

¹²² *Bankruptcy Amendment Act 1980* (Cth) s 72.

¹²³ Efrat, above n 109, 92.

¹²⁴ See, eg, David A Lander, 'It Is the Best of Times, It Is the Worst of Times: A Short Essay on Consumer Bankruptcy after the Revolution' (2004) 78 *American Bankruptcy Law Journal* 201. The issue of credit is considered further below in Section V(B)(2).

¹²⁵ See, eg, Adam Feibelman, 'Social Insurance Function of Consumer Bankruptcy' (2005) 13 *American Bankruptcy Institute Law Review* 129; Richard M Hynes, 'Non-Procrustean Bankruptcy' (2004) *University of Illinois Law Review* 301, 350-9.

through other private and public institutions and legal regimes.¹²⁶ In this sense, personal insolvency laws might be seen as a safety net, which fill in gaps in social insurance programs.¹²⁷ Debtors who turn to personal insolvency administration may have encountered financial difficulties due to a lack of unemployment benefits or health coverage, or due to family breakups. In 2008, 31.17% of non-business related bankrupts and 35.58% of non-business related debt agreement debtors cited unemployment as the cause of their insolvency.¹²⁸ A further 11.78% of non-business related bankrupts and 7.51% of non-business related debt agreement debtors cited ill health as the cause of their insolvency. In addition, 12.37% of non-business related bankrupts and 13.17% of non-business related debt agreement debtors cited domestic discord as the cause of their insolvency. The use of Australia's personal insolvency regime by such insolvents might mean that the regime at times functions as a form of social insurance for those who experience gaps in their financial safety nets during times of hardship.

That personal insolvency laws might function as a form of consumer credit regulation, or provide a form of social insurance, indicates that personal insolvency laws have wide societal implications. More is at stake in the drafting and application of these laws than the traditional focus on the competing interests of creditors and debtors. The interpretation of the core policy objectives of Australia's bankruptcy laws may have fallen into this dichotomous state,¹²⁹ but attention needs to be drawn to other rationales personal insolvency laws might serve.

The ALRC's final report on insolvency laws included several guiding principles of contemporary Australian insolvency law which were used by the ALRC to formulate its specific recommendations.¹³⁰ The fundamental purpose was seen as provision of a fair and orderly process for insolvent individuals and companies.¹³¹ The ALRC placed further emphasis on allowing debtors and creditors to participate with the least possibly delay and expense in an impartial, efficient, and expeditious insolvency

¹²⁶ Feibelman, above n 125, 130.

¹²⁷ Jean Bracher, 'Consumer Bankruptcy as Part of the Social Safety Net: Fresh Start or Treadmill?' (2004) 44 *Santa Clara Law Review* 1065, 1065-73.

¹²⁸ The statistics in this paragraph are from Ramsay and Sim, above n 2.

¹²⁹ See, eg, *Storey v Lane* (1981) 147 CLR 549, 556-7; *Re McMaster; Ex parte McMaster* (1991) 33 FCR 70, 72-3.

¹³⁰ Australian Law Reform Commission, *General Insolvency Inquiry*, Report No 45 (1988).

¹³¹ *Ibid* [33].

administration, with the end result, particularly for individual insolvents, of effective relief or release from the insolvent's financial liabilities and obligations.¹³² At the same time, the ALRC felt that insolvency laws should support the commercial and economic processes of the community.¹³³

There is now an important question whether the original policy of Australian personal insolvency laws, as articulated by the ALRC and also by some courts, is still valid given the changing demographics of Australian personal insolvents. Australia's personal insolvency laws are affecting increasing numbers of Australians and therefore the role these laws play in regulating the relationship between creditors and insolvent debtors and balancing the respective interests of creditors and debtors remains important. However, personal insolvency laws accomplish more than balancing these interests and this arguably includes credit market regulation and providing a form of social insurance. In order to understand the wider role that personal insolvency laws might play, it is important that connections between personal insolvency laws and broader social issues are analysed. This is the purpose of the following section where our intention is to place Australia's personal insolvency laws in a broader social context.

B *Connections between personal insolvency laws and broader social issues*

Our findings indicate that personal insolvency is having a growing presence within Australian society. Determining the causes of personal insolvency in Australia is not something that has attracted much academic attention. There is a pressing need for more detailed research on personal insolvency and related issues. The urgency of this call for further research is amplified not solely because of the significant increase in personal insolvency numbers, but also because there has been speculation that the federal government is considering important reform of Australia's personal insolvency system.¹³⁴ If any reform is to take place, it must reflect detailed research and consultation, as well as a good understanding of the policy and function of

¹³² Ibid.

¹³³ Ibid

¹³⁴ See, eg, Alex Boxsell, 'Bankruptcy move found wanting', *The Australian Financial Review*, 15 June 2009, 52; Dennis Turner, 'Bankruptcy reform needs reform', *The Age*, 26 June 2009, 8; Jason Bryce, 'Cast off debt's load', *The Sunday Mail*, 26 July 2009, 61.

personal insolvency laws. It has been viewed as potentially dangerous to make changes to bankruptcy laws based on ‘possibly mistaken diagnoses’, for these may result in the opposite results to those the reform intended to achieve.¹³⁵ In our view, any broad reform of the current Australian personal insolvency regime should include consideration of issues relating to the need for improved personal insolvency data; rising levels of debt; the spending habits of Australians; and the relationship between personal insolvency and social security. We now consider each of these issues.

1 *The need for improved personal insolvency data*

Understanding the connections between personal insolvency laws and broader social issues requires detailed data on the characteristics of personal insolvents and the causes of personal insolvency. There is a need for more research, beyond what has already been done, on the causes of personal insolvency and the characteristics of personal insolvents. This research is necessary in order to obtain a more comprehensive profile of Australian personal insolvents.

At present, some information is not requested of insolvents in their Statement of Affairs, and some data collated by ITSA from the Statement of Affairs is not released to the public.¹³⁶ In the absence of broad empirical studies into Australian personal insolvency, it is desirable that ITSA capture and release further data on the characteristics of personal insolvents in order to enable further research in this area. Additionally, information profiling the socio-economic characteristics of personal insolvents can inform research on the economic progress of social groups, and how vulnerable certain groups are in an economic sense.¹³⁷ Personal insolvency is affecting more Australians and there are strong reasons to enhance current reporting of the characteristics of Australian personal insolvents.

First, it would be useful for data to be reported in such a manner that would enable the determination as to what proportion of insolvents has a combination of certain characteristics. This might involve reporting on the characteristics of each individual

¹³⁵ David A Moss and Gibbs A Johnson, ‘Rise of Consumer Bankruptcy: Evolution, Revolution, or Both?’ (1999) 73 *American Bankruptcy Law Journal* 311, 343.

¹³⁶ For information on Statements of Affairs, see above nn 61-63 and accompanying text.

¹³⁷ Warren, ‘Financial Collapse and Class Status’, above n 72, 118.

debtor. This would then allow, for example, determination of the proportion of bankrupts who are professionals in the highest income bracket and declare property ownership, or what proportion of debt agreement debtors are aged less than 35 and have dependants. Warren was able to make such classifications on the US data (notably, by determining what proportion of bankrupts fulfilled the three criteria relating to middle class status).¹³⁸ Availability of such data would be beneficial to the study of Australian personal insolvents.

Second, the current Statement of Affairs should be expanded to include further socio-economic details of insolvents. The level of education reached is one of the three criteria used by Warren to determine the middle-class status of US bankrupts,¹³⁹ and such information would be useful in expanding the profile of Australian personal insolvents. The Statement of Affairs already contains questions on certain aspects of the ethnicity of Australian personal insolvents, such as whether insolvents are of Aboriginal or Torres Strait Islander origin; which country insolvents were born in; and which languages are spoken at home. Aside from making this information publicly available, a direct question on the ethnicity of the insolvent should be included, as important observations on ethnicity and bankruptcy have been made in the US.¹⁴⁰ Furthermore, an additional question should be included in the Statement of Affairs as to whether the insolvent has used the services of a financial adviser, to assist in determining what financial resources, if any, have been used by Australian personal insolvents.

Third, existing data collected in the Statement of Affairs should be included within ITSA's relevant publications to assist in enabling a better profile of Australian personal insolvents. Whilst information is available on the state and territory breakdowns of personal insolvencies, this data should be expanded to include a breakdown of figures based on federal constituencies and urban/rural areas. This

¹³⁸ See above Section III(C).

¹³⁹ Ibid 128.

¹⁴⁰ A study in the US found that the self-employed in bankruptcy did not differ from the non-bankrupt self-employed on age, gender, or marital status, but that African Americans were overrepresented and Asian-Americans were underrepresented among the self-employed in bankruptcy. See Robert M Lawless, 'Who Are the Self-Employed in Bankruptcy?' (Working Draft, Social Science Research Network, May 2008). Another study found that immigrant entrepreneurs are less likely to file for bankruptcy: see Rafael Efrat, 'Immigrant Entrepreneurs in Bankruptcy' (2008) 82 *American Bankruptcy Law Journal* 693.

would enable a fuller understanding of the location of Australian personal insolvents. In addition, whilst some information is available on the proportion of insolvents with and without dependants, this data should be expanded to include the number of dependants, which would enable insight into whether the risk of personal insolvency increases with the number of dependants.¹⁴¹ Data should be released on the proportion of insolvents with government benefits and pensions, as well as private patient hospital cover, which would help ascertain the role that welfare and insurance plays in ameliorating financial difficulties.¹⁴² Data currently collected by ITSA on the duration for which insolvents have experienced difficulty paying their debts would also be insightful, as it would assist in determining the period of time insolvents are able or prepared to experience financial difficulties before becoming a personal insolvent, with the consequences this entails.¹⁴³

2 *Incurring of debt*

In exploring connections between Australia's personal insolvency laws and broader social issues, one important matter is how central to the increase in Australian personal insolvency numbers are rising debt levels. A question is whether Australians are being forced to access credit as a short-term solution to financial difficulties, or whether increases in credit usage are part of a problem of overconsumption. The financial vulnerability of individuals is heightened through greater access to credit, and it appears there is a connection between the rate of personal insolvencies and the extent of deregulation in the consumer credit market.¹⁴⁴ This gives rise to the need for further research on the incurring of debt. At present, it remains unclear precisely what type of debt is being incurred by insolvents, and in what circumstances this is

¹⁴¹ A study in the US found an increased risk of bankruptcies for families with more children: see Warren, 'Bankrupt Children', above n 72.

¹⁴² A study in the US found an increased risk of bankruptcy for those with inadequate health insurance: see David U Himmelstein, Elizabeth Warren, Deborah Thorne, and Steffie Woolhandler, 'Illness and Injury as Contributors to Bankruptcy' (Social Science Research Network, February 2005).

¹⁴³ Information on the realisable asset levels of insolvents would be enhanced by ITSA releasing data on the proportion of insolvents who declare vehicle or share ownership or entitlements. In addition, data on the proportions of insolvents with accountants and solicitors should be published, as this would indicate the proportion of insolvents receiving financial and legal assistance in organising their affairs.

¹⁴⁴ Mason, 'Consumer Bankruptcy: An Australian Perspective', above n 71; Jayendra Kumar, Rosalind Mason, and Deborah Ralston, 'Consumer Bankruptcies: Causes and Implications for the Credit Industry' (1998) 17 (3) *Economic Papers* 18; Deborah Ralston, Rosalind Mason and Jayendra Kumar, 'Causes of Consumer Bankruptcy in Australia: A Macroeconomic Analysis' (Working Paper No 01/1, University of the Sunshine Coast Faculty of Business, 2001).

occurring. Whilst debt might be incurred as part of overconsumption, it might also be the case that debt is incurred in the lead up to personal insolvency as part of an attempt to avoid some form of personal insolvency administration.

It has been suggested that bankruptcy represents one of the costs stemming from the extension of consumer credit,¹⁴⁵ and that bankruptcies are a by-product of excessive borrowing.¹⁴⁶ For this reason, it has been suggested that before amendments to bankruptcy laws are made, consideration should be given to whether reform to consumer borrowing and credit regulations might be more appropriate.¹⁴⁷ It has been argued that reforms to bankruptcy laws in the US, designed to make bankruptcy less desirable for consumers, have resulted in increased costs to consumers of credit cards.¹⁴⁸

It is possible that some unsecured debt declared by Australian personal insolvents has been incurred to fund basic living essentials. Available data indicates that even modest levels of unsecured debt can result in bankruptcy. In 2002 and 2007, 5% of bankrupts had unsecured debt less than \$2,000, compared to 4% in both 2003 and 2005.¹⁴⁹ In 2002, 49% of bankrupts had more than \$2,000 but less than \$20,000 in unsecured debt, compared to 28% in 2007. However, levels of unsecured debt greater than \$20,000 among bankrupts increased between 2002 and 2007.

Related to the incurring of debt, there exists the need for more research on the credit industry and its practices.¹⁵⁰ Between 1997 and 2008, there was a 106% increase in the proportion of non-business related bankruptcies caused by excessive use of credit.¹⁵¹ Between 2002 and 2008, there was a 20% increase in the proportion of debt agreements caused by excessive use of credit. In 2008, 27.55% of non-business related bankruptcies and 39.41% of non-business related debt agreements were caused by excessive use of credit. Further, in 2007, 52% of bankrupts' creditors and 61% of

¹⁴⁵ Moss and Johnson, above n 135, 349.

¹⁴⁶ Ibid 350.

¹⁴⁷ Ibid 351.

¹⁴⁸ Michael Simkovic, 'The Effect of BAPCPA on Credit Card Industry Profits and Prices' (2009) 83 *American Bankruptcy Law Journal* 1.

¹⁴⁹ The statistics in this paragraph are from Ramsay and Sim, above n 2.

¹⁵⁰ See, eg, Ralston, Mason and Kumar, 'Consumer Bankruptcies: Causes and Implications for the Credit Industry', above n 144.

¹⁵¹ The statistics in this paragraph are from Ramsay and Sim, above n 2.

debt agreement debtors' creditors were finance organisations. Of creditors among finance organisations, the creditor subtype of cards (i.e. store cards and credit cards) in 2007 was high for both bankrupts (36%) and debt agreement debtors (50%). The increase in personal insolvencies caused by excessive use of credit, and the high proportions of financial organisation creditors, coincides with increases in several forms of Australians' debt.

One issue relating to credit industry practices is the prevalence and expansion of the credit card industry. In January 1997, combined credit limits for credit cards (excluding charge cards and cards issued to businesses) with an interest-free period reached \$19,585 million, with total value of outstanding balances owed on credit cards of \$6,581 million.¹⁵² In January 2009, these credit limits had increased to \$112,161 million with outstanding balances of \$39,526 million.¹⁵³ Over these 12 years, and not taking into account the effect of inflation, this represents a 473% increase in credit limits and a 501% increase in the amount of outstanding balances.

Another factor, resulting in part from this increase in credit card debt, is the increase in Australian household debt. Between 2000 and 2008, the total amount of debt owed by Australian households rose almost six-fold.¹⁵⁴ In September 1990, Australian households were \$190 billion in debt. In September 2008, Australian households were \$1.1 trillion in debt in real terms (i.e. adjusted to remove the effect of inflation).¹⁵⁵

A further example of the growing ease of access to credit is the increasing incidence of margin lending, which is a form of debt. Margin lending involves borrowing to acquire financial products such as shares in companies. In September 2000, margin lending in Australia totalled \$6,379 million, with an aggregate credit limit of \$8,437 million and 84,000 client accounts.¹⁵⁶ In September 2008, margin lending totalled \$27,553 million, with an aggregate credit limit of \$64,732 million and 202,000 client accounts.¹⁵⁷ In September 2000, there was an average of 1.28 margin calls per day per

¹⁵² Reserve Bank of Australia, *Credit Card Statistics* (May 2009).

¹⁵³ Ibid.

¹⁵⁴ Australian Bureau of Statistics, *Australian Social Trends 4102.0* (2009) 30-8.

¹⁵⁵ Ibid.

¹⁵⁶ Reserve Bank of Australia, *Bulletin Statistical Tables: Margin Lending* (March 2009) <<http://www.rba.gov.au/Statistics/Bulletin/D10hist.xls>>.

¹⁵⁷ Ibid.

1000 clients, compared to 4.32 in September 2008.¹⁵⁸ By December 2008, this rate had increased to 9.77 margin calls per day.¹⁵⁹ It may be that some margin calls have led to personal insolvency when the amount borrowed was excessive.

There is, therefore, an important issue regarding links between increases in debt (such as credit card debt, household debt, and in margin lending), on the one hand, and the increase in personal insolvencies caused by excessive use of credit and the higher proportion of financial organisation creditors of personal insolvents, on the other hand. Consequently, rising levels of debt and the circumstances in which this debt is incurred and by whom is part of the broader social context in which personal insolvency laws operate.

3 *Spending habits*

Understanding the connections between personal insolvency laws and broader social issues requires exploration of spending habits. There is a relationship between personal insolvency and spending habits. Australians have increased levels of debt, and it seems logical that spending habits would form part of the equation as to why the demographics of Australian personal insolvents are changing. It is unclear how personal insolvents spent their money in the lead up to insolvency. Are Australians taking part in overconsumption and frivolous spending?¹⁶⁰ Or are Australians being forced to access credit to buy essential household items as a short-term solution to financial difficulties? As mentioned above, a significant proportion of personal insolvents declare their insolvency to have been caused by excessive use of credit, but this does not determine that utilisation of credit is part of a problem of overconsumption. However, between 1997 and 2008 there was a 229% increase in the proportion of non-business related bankruptcies caused by gambling or speculation. In 1997, gambling or speculation caused 1.30% of non-business related bankruptcies, compared to 4.28% in 2008.¹⁶¹ This indicates that, to a certain extent,

¹⁵⁸ Ibid.

¹⁵⁹ Ibid.

¹⁶⁰ See, eg, Clive Hamilton and Richard Denniss, *Affluenza: When Too Much Is Never Enough* (2005).

¹⁶¹ The statistics in this paragraph are from Ramsay and Sim, above n 2. For further discussion of gambling and bankruptcy, see John Duns, 'Other People's Money: Gambling and Bankruptcy' (2007) 31 *Melbourne University Law Review* 87.

overconsumption, as typified by gambling and other forms of speculation, has contributed to the increase in personal insolvencies.

In the US, vociferous debate has taken place regarding whether increases in bankruptcy in that country are the result of increases in expenses for families, or increases in unnecessary overspending.¹⁶² An understanding of the relationship between the spending habits of Australians and personal insolvency is relevant to consideration of the role and function of personal insolvency laws. If personal insolvency laws serve a social insurance function, or assist in the regulation of the credit market, then information on the spending habits of personal insolvents will assist in determining whether the policy objectives of personal insolvency law require reconsideration. There are important policy questions relevant to spending habits that result in personal insolvency. For example, where gambling debts lead to personal insolvency, should this result in a longer period before discharge from personal insolvency than would be the case with other forms of debt, or should there be an exemption from release on discharge for gambling debts, based on the policy objective of deterring misuse of the personal insolvency regime?¹⁶³ Answering these types of questions requires an understanding of the broader social context in which personal insolvency laws operate.

4 *Social welfare benefits*

One final issue relates to the interaction between social welfare benefits and personal insolvency. As mentioned above, data on government benefits and pensions paid to personal insolvents prior to their insolvency is collected by ITSA, and this data should be made available to enhance understanding of the role that social welfare benefits might have in ameliorating financial difficulties. It may be the case that welfare benefits have become less sufficient at assisting those who previously might have been able to avoid personal insolvency.

¹⁶² See further the debate on 'What's Hurting the Middle Class' on the Boston Review Forum <<http://bostonreview.net/forums/>> at 30 July 2009.

¹⁶³ See further, Duns above n 161, who discusses these questions in the context of his analysis of bankruptcy and gambling.

Australia has a limited social welfare regime compared to some other developed countries. A 2008 OECD report found that in a typical OECD country, 22% of total income is from the government in the form of cash benefits, compared to 14% in Australia.¹⁶⁴ Further, in Australia these cash benefits are concentrated more on low-income households than in any other OECD country, with 40% of cash benefits going to the poorest 20% of the population.¹⁶⁵ That welfare is targeted at these lower-socio economic groups might explain in part why Australian personal insolvency is becoming an increasingly middle class phenomenon.¹⁶⁶

One potential link between social welfare benefits and bankruptcy can be considered on already available data. Between 2005 and 2007, there was a significant rise in the proportion of bankrupts with dependants, rising from 35% to 49%, which represents an increase of 40% in two years.¹⁶⁷ During this time, there was also an increase in the number of bankruptcies, from 20,501 in 2005 to 25,238 in 2007, an increase of 23%. Whilst single bankrupts without dependants constituted the greatest proportion of bankrupts in 2002 (44%), 2003 (44%), 2005 (47%) and 2007 (37%), the proportion of bankrupts who were members of a couple with dependants increased from 20% in 2005 to 32% in 2007. This might constitute evidence that welfare benefits are becoming less sufficient at assisting those with dependants. An enhanced understanding of the interaction between social welfare benefits and personal insolvency is important to determine the sufficiency of welfare benefits at assisting those in financial need. One issue is whether greater financial support should be provided to those raising children, or whether assistance should be provided in bankruptcy by further restricting the items the trustee may seize.¹⁶⁸

VI CONCLUSION

Financial stress is affecting a growing number of Australians to the extent that an increasing proportion are entering into bankruptcy and debt agreements, despite the

¹⁶⁴ Organisation for Economic Co-operation and Development, *Growing Unequal? Income Distribution and Poverty in OECD Countries* (2008).

¹⁶⁵ *Ibid.*

¹⁶⁶ Many welfare payments in Australia are subject to income and assets tests, including the Age Pension, the Carer Payment, the Child Care Benefit and Tax Rebate, the Disability Support Pension, the Family Tax Benefit, the Newstart Allowance, the Parenting Payment, the Sickness Allowance, the Special Benefit, and the Youth Allowance.

¹⁶⁷ The statistics in this paragraph are from Ramsay and Sim, above n 2.

¹⁶⁸ See further Warren, 'Bankrupt Children', above n 72, 1024-5.

consequences these entail. Whilst the rise in personal insolvencies is not attributable solely to prevailing economic conditions, we expect in the context of the global financial crisis that the number of personal insolvencies will rise over the coming period. Personal insolvency is affecting, and will continue to affect, a growing number of Australians. This article has considered one important feature of the increase in personal insolvency – the way in which it is affecting to a greater degree the Australian middle class.

This finding should displace any assumptions informing stereotypical images of personal insolvents. If personal insolvency is becoming an increasingly middle class phenomenon, then it is not correct to assume that personal insolvents are only the chronically poor who have no other options, such as pensioners; neither is it correct to assume that personal insolvents are only the very wealthy who are avoiding meeting their financial obligations. Rather, personal insolvency is affecting a broader section of Australian society, and our analysis indicates that one feature of this increase is that this section is increasingly the middle class.

Personal insolvents are increasingly coming from higher prestige occupations, such as managers and administrators, professionals, and associate professionals. Between 1999 and 2008 there was a 142% increase in the proportion of bankrupts and an 82% increase in the proportion of debt agreement debtors from these occupations. Personal insolvents have increasing levels of personal income. Between 1997 and 2007 there was a 192% increase in the proportion of bankrupts and a 360% increase in the proportion of debt agreement debtors with personal income of \$30,000 or more. There have also been significant increases between 2005 and 2007 in the proportions of bankrupts (44% increase) and debt agreement debtors (42% increase) with personal income of \$50,000 or more. Similarly, personal insolvents are coming from households with greater levels of income. Between 2002 and 2007 there was a 167% increase in the proportion of bankrupts and a 125% increase in the proportion of debt agreement debtors with household income of \$50,000 or more. Personal insolvents also have increasing levels of realisable assets, with a 133% increase in the proportion of bankrupts and a 100% increase in the proportion of debt agreement debtors between 2003 and 2007 declaring realisable assets of \$50,000 or more. Finally, property ownership levels increased between 2003 and 2007, with a 120% increase in

the proportion of bankrupts and a 200% increase in the proportion of debt agreement debtors declaring property ownership.

Our findings have implications for the Australian personal insolvency regime, notably the policy underpinning personal insolvency laws. Whilst debate on Australian personal insolvency laws has usually focussed on balancing the interests of debtors and creditors, with emphasis on giving debtors a fresh start, personal insolvency laws might have broader societal functions, including regulating credit markets and providing a form of social insurance. In order to further investigate these functions, improvements should be made to the current Australian data on personal insolvency. It is also important to understand the broader social context in which personal insolvency laws operate. We have, in this article, explored the connections between personal insolvency and rising levels of debt; the spending habits of Australians; and social welfare benefits. Undoubtedly, more research is required. However, what is unambiguous is that the reach of Australian personal insolvency has been expanding and is altering the demographics of Australian personal insolvents.