

De (ex-) ondernemer in de Wsnp
Hoofdstuk 8 - Comparative Law
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8.1 Introduction

The treatment of ex-entrepreneurs under the *Wsnp* is quite similar to practices under other prominent national individual insolvency laws, though this chapter will focus on the important contrasts between the laws in the Netherlands and those in the US, England and Wales, Germany, Denmark, France, Belgium and Luxembourg. This chapter compares only the treatment under provisions applicable to individuals, whether or not engaged in business, the *Wsnp*-equivalent. No treatment of individuals under the general business bankruptcy law will be presented here (*e.g.*, Chapter 11 of the US Bankruptcy Code, a much more complex and therefore expensive procedure that is sometimes used by individuals, though rarely). This chapter will draw particular attention to provisions that would theoretically apply most prominently to ex-entrepreneurs, even if the specific group of such debtors cannot readily be distinguished empirically from the bulk of “pure consumer” filers.

8.2 United States

8.2.1 Introductory overview

Developments in the past few years have raised particularly interesting contrasts between practice under the US Bankruptcy Code and the Dutch *Wsnp*. Functionally, in terms of returns to creditors, the two systems produce very similar results, though the very different structure of US law seems to achieve this result in a significantly more efficient way in the majority of cases. On the other hand, while each system has something valuable to learn from the other,¹ the lessons coming from the US in recent years have concerned primarily illustrations of mistakes to avoid. In particular, the new “means test” has powerfully undermined system efficiency and has proven over time to be almost entirely unjustified, and the US “fresh start” has been eroded by numerous exceptions that render it not nearly so fresh as outside observers often assume. For former small business owners and entrepreneurs, in particular, the US system reflects some of the most positive aspects of Dutch practice, but it has done so in a way that has undermined, rather than leveraged, its otherwise more efficient approach.

8.2.2 *Het minnelijk traject in the US*

Unlike the Dutch *Wsnp*, US bankruptcy law before 2005 contained no requirement at all that debtors attempt to achieve an out-of-court solution to their debt problems before seeking formal relief. Even after the substantial reform of 2005, individual US debtors are now required only to consult a credit counselor before filing a petition for relief. These counselors seldom suggest - let alone attempt to negotiate - any compromise solution with creditors. This requirement is thus little more than a wasteful and usually pointless pre-filing formality, and it represents perhaps the only real hurdle that individual debtors must clear to gain entry to the formal relief process.

¹ See Jason J. Kilborn, “The Hidden Life of Consumer Bankruptcy Reform: Danger Signs for the New US Law From Unexpected Parallels in the Netherlands,” *Vanderbilt Journal of Transnational Law* 39 (2006): 77, <http://ssrn.com/abstract=772705>.

Quite similar to the network of *gemeentlijke kredietbanken* in the Netherlands, a substantial number of credit counseling centres pepper the United States. These centres have long been in the business of helping debtors to take control of their financial distress and make informal compromise arrangements with creditors to avoid bankruptcy. While these centres still enjoy some success in mediating the financial straits of some debtors, their efforts have become less and less successful since the mid-1990s in light of a spectacular rise in debt levels, stagnating real incomes for all but the wealthiest Americans, and an increasing unwillingness by institutional creditors (primarily credit card banks) to offer consumers the scope and nature of relief that could stave off a bankruptcy filing. This constellation of challenges impacts small business people particularly. They often face very large debts to a quite significant number of creditors. Coordinating a successful workout with the debt figures and numerous creditors involved in such cases is next to impossible under the best of circumstances, and the credit counseling industry in the US today does not enjoy the best of circumstances.

Credit counseling in the United States is a business, largely dependent on private funding (usually donations) to support its operations. The few for-profit credit counseling agencies (yes, there were for-profit companies advertising such services on cable television until recently) were all but completely driven out of business when their sharp practices and patent conflicts of interest with debt servicing companies were challenged by regulatory authorities in the 1990s and early 2000s. The great bulk of counseling agencies in the US today, then, are the remnant of the original US concept of credit counseling, established not by social service-oriented agencies, but by commercial banks. As default rates and personal bankruptcy filings rose in the latter portion of the 20th century, commercial banks funded the initial setup of a network of credit counseling agencies in an effort to redirect consumers away from a quick discharge of debt and toward repayment arrangements. Participating banks funded the operations of these counseling centres with so-called “fair share” payments of 12-15% of the amounts paid by debtors to creditors through centre-administered payment plans. By the late 1990s, however, advances in technology and consolidation in the banking industry made it more economical for large banks to support their own captive, internal collections departments. Consequently, many key creditors, especially the primary lenders to small business, slashed or discontinued their fair share payments to the credit counseling industry, pushing the industry to the edge.

Even if the counseling centres were properly funded, creditors have become increasingly unwilling to agree to the sorts of compromises needed by debtors to reestablish their financial footing. Sophisticated statistical modeling has allowed large lenders to figure the cost of significant default rates into their credit pricing. With losses already recouped in the ordinary business model, many banks see little purpose in compromising with debtors. In the best of circumstances, creditors have historically offered only to reduce accruing interest and late fees, though almost without exception, they have demanded that the entire outstanding debt principal be repaid over three to five years (likely excluding larger secured debts, such as home mortgage and car loans). As mentioned above, these terms are largely unachievable by most former small business debtors with extremely large loan balances and many creditors. By 2001, economically irrational creditor rejections of proposed debt management plans had become quite common, and creditors were offering fewer interest-rate reductions and other concessions to facilitate such plans.

Despite the ineffectiveness of a negotiated alternative to bankruptcy relief, the 2005 reform incorporated a requirement that all individual debtors seek information about bankruptcy alternatives as a condition to filing a bankruptcy petition. Supported by little more than anecdotes by banking industry lobbyists, lawmakers had developed the perception that debtors were choosing bankruptcy too hastily, without proper consideration of alternatives. To remedy this imagined information deficit, the US Bankruptcy Code as revised in 2005 requires that an individual can seek relief under any chapter only after having received “an individual or group briefing (including a briefing conducted by telephone or on the Internet) that outlined the opportunities for available credit counseling and assisted such individual in performing a related budget analysis” within 180 days before the bankruptcy filing.² To prevent abuse of this captive market for counseling, the law also restricted the fees that “approved” agencies could charge debtors. It required that counseling be offered for a “reasonable fee” and that fees be waived for debtors who could not afford to pay.³

These fee restriction resulted in a retreat to an absolutely minimalist level of counseling that today generally represents little more than a pure formality. Only a few months after implementation of the reform law, US counseling agencies began to complain of losing millions of dollars to mandatory cost-controlled pre-bankruptcy counseling. Counselors reported that the average cost to agencies to offer the required counseling was over \$50 per session, while the average fee collected from consumer debtors was just over \$38, causing an ongoing nearly 25% shortfall in necessary operating revenue. To remedy their own financial predicament, many centres concluded that the notion of offering labor-intensive face-to-face counseling was out of the question. Remote counseling by telephone or internet soon became the standard, for both reasons of financial expediency for agencies and convenience for debtors. The largely ceremonial “counseling” offered today usually consists of a less-than-one-hour session by telephone or internet, usually prompted by the debtor’s bankruptcy lawyer, and often accessed from the lawyer’s office as an immediate prelude to filing the bankruptcy petition. The content of this ritualistic counseling is all but devoid of any useful substance. The counseling agency offers a generalized outline of available techniques for dealing with financial distress, the debtor inputs financial information that inevitably demonstrates that bankruptcy is the only workable solution to financial trouble spiraling out of control, and the counseling agency produces (and emails to the bankruptcy lawyer) a certificate of completion in exchange for a \$50 fee (often paid by credit card by the bankruptcy lawyer, who recoups the charge from the debtor before filing the bankruptcy petition). This charade is required of all individual debtors.

8.2.3 The half-hearted US version of *dwangakkoord*

In a faint suggestion of support for facilitating informal compromises, the reformed US law contains a provision distantly analogous to the *dwangakkoord* provisions in the *Wsnp*. The resemblance is only very distant, however, as this completely superfluous provision is nothing more than window dressing, offering virtually no incentive to creditors to avoid unreasonable rejection of out-of-court compromise offers. In a section entitled “Promotion of Alternative Dispute Resolution,” the reform law inserted a provision allowing the bankruptcy court ultimately to reduce a creditor’s claim if that creditor had “unreasonably refused to negotiate a

² 11 U.S.C. § 109(h)(1).

³ 11 U.S.C. § 111.

reasonable alternative repayment schedule proposed on behalf of the debtor by an approved nonprofit budget and credit counseling agency.”⁴

Several caveats and limitations all but eliminate the effective menace of this potential reduction of a creditor’s claims. First, it applies only to “a claim . . . based in whole on an unsecured consumer debt.” Business debts of former small business debtors are not eligible for forced reduction, no matter how unreasonably the creditor might have acted. Second, the offer of a “reasonable alternative repayment schedule” must have been made at least 60 days before the debtor’s bankruptcy filing. Creditors are free to refuse reasonable offers in compromise if the debtor files for bankruptcy shortly after the refusal, and debtors are not likely to wait 60 days to file for bankruptcy relief after a creditor has rejected an attempt to settle. Third, the debtor must have offered to pay at least 60% of the creditor’s claim within a “reasonable extension” of the original contractual repayment period. Given sky-high US debt levels and stagnant income, few debtors are likely to be able to offer 60% payment without a substantial repayment period, which would doubtless exceed “a reasonable extension.” Finally, the sanction for unreasonable refusal to negotiate is laughably unrealistic. As punishment for having unreasonably refused to negotiate a 40% remission of debt, the creditor faces reduction of its claim by a *maximum* of only 20%. One can hardly imagine that the threat of losing 20% of the creditor’s claim will “promote alternative dispute resolution” that would not already have been successful. Not a single case has applied this new provision in the debtor’s favor to date.

8.2.4 Few barriers to entry

Aside from the credit counseling requirement just discussed, US law imposes virtually no entry barriers to the formal bankruptcy system. No distinction is made between “business” and “non-business” debtors, and no debtor need claim or prove “overindebtedness,” though few debtors even in the generous US system will face the stigma of financial failure and the restrictions of post-bankruptcy financial life unless they really need relief. An “overindebtedness” test has not proven necessary, and its absence has been almost entirely uncontroversial. Moreover, a debtor’s petition cannot be rejected for lack of “good faith.” As will be discussed below, in certain limited cases, lack of good faith or failure to maintain adequate business records might lead to denial of plan confirmation and the *benefit* of the system, but this decision would be made nearer to the conclusion of the proceedings. At the front end, all but a handful of petitions are automatically accepted for admission into the system, unlike the situation in the Netherlands.

The only significant hindrance to entry to the US bankruptcy system is the cost of a lawyer. Debtors must seek relief either *pro se* (on their own behalf, without representation) or through a lawyer, and given the complexity of the paperwork and other burdens in this system, especially for cases involving former small business people, the overwhelming majority of successful debtors are represented by counsel. While the filing fee amounts to only about \$300 (€200), lawyer fees for a simple liquidation case generally range from \$2000 to as much as \$5000 (€1350-€3350), and for a more complex repayment plan case, lawyer fees can climb even higher. While the fees for a payment plan case can be paid through the payment plan in most cases, the fee for a liquidation case generally must be paid in advance (to avoid this debt to the lawyer being discharged in the case). Former small business people are likely more able to consolidate

⁴ 11 U.S.C. § 502(k).

the remains of their business cash to finance lawyer fees, but many individual liquidation bankruptcy cases are at least delayed while the debtor collects the necessary fee.

8.2.5 Relief options: Chapter 7 liquidation v. Chapter 13 payment plans

While broadly open *access* to relief has been largely uncontroversial, significant controversy has arisen as to how relief should be delivered and on what conditions. Since 1898, individual debtors, perhaps especially former small business people, have been able to seek relief under what is today styled “Chapter 7” of the US Bankruptcy Code. The traditional form of relief was a simple liquidation of the debtor’s unprotected (non-exempt) and unencumbered assets for distribution to unsecured creditors, followed by a prompt and automatic discharge of most of the debtor’s unpaid obligations. Property exemptions are for all practical purposes an issue of individual state law, not federal law, as a result of a legislative compromise, and the range of property exempted for the debtor varies widely from state to state. Some states, like Texas, exempt vast amounts of property (up to \$60 000 in value in movable property and an *unlimited* “homestead” exemption in the debtor’s residence), while others exempt only minimal property, such as the family Bible, clothing, and perhaps tools of the debtor’s trade up to a low value. Most state exemption laws fall somewhere between these two extremes. Retirement savings and other specially segregated pension assets are fully exempt under federal law.

Because former small business debtors seldom have any assets not protected by law or encumbered by security interests and similar charges, Chapter 7 liquidation bankruptcy is essentially a “get out of jail free” card for these and most other debtors. In the overwhelming majority of these cases, the appointed trustee reports that the debtor owns no property that may be lawfully seized by unsecured claimants, and the case concludes with a discharge and “fresh start” for the debtor after a total duration of about four months. Chapter 7 has historically produced very low returns for unsecured creditors, functioning primarily as a mechanism for reinvigorating the debtor’s productive energies and reintroducing the debtor into the “open credit economy.”

In the 1930s, lawmakers sought to increase returns to unsecured creditors and offer debtors a more “honorable” method of obtaining relief. The predecessor to what today is called “Chapter 13” was introduced into the Bankruptcy Code as an alternative to liquidation bankruptcy, a so-called “wage earner reorganization.” A Chapter 13 case more closely resembles a case under the Dutch *Wsnp*. Usually the debtor’s nonexempt property is not liquidated, and small business debtors are explicitly allowed to continue to conduct their business, including taking on trade debt in the ordinary course with court permission.⁵ In exchange for preserving existing property interests, the debtor (that is, the debtor’s lawyer) draws up a payment plan promising to pay part of the debtor’s anticipated future income to creditors. Creditors do not vote on this plan; rather, the court confirms the plan and imposes it on creditors if the plan meets the few requirements in Chapter 13.⁶

The most notable requirement is that the plan must promise to turn over to creditors the value of all of the debtor’s “disposable income” anticipated over the next three- to five-year period.

⁵ 11 U.S.C. § 1304.

⁶ 11 U.S.C. §§ 1322(a), 1325.

While Dutch practice evolved to require plans on the *lower* end of the 3- to 5-year scale, US practice developed in the opposite direction; that is, all but a small handful of Chapter 13 plans propose a term of 60 months.⁷ Before 2005, the notion of “disposable income” was defined vaguely to allow the court significant discretion in allocating the debtor’s budget. Still today, for debtors with below-median income according to the means test (see below), income is “disposable” if it exceeds “amounts reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor,” or for debtors engaged in business, “for the payment of expenditures necessary for the continuation, preservation, and operation of such business.”⁸ In addition, the plan must be proposed “in good faith,”⁹ a concept left entirely undefined in the statute. Some courts in the past have required a minimum payment to creditors to establish the debtor’s “good faith,” and the amount of the required minimum dividend - or the lack of a required minimum - has varied significantly from district to district, even within the same state.¹⁰

Because the promise in the plan is based on anticipated income and expenses, it is susceptible to over- or under-estimation of *actual* income and expenses. Plans can be modified to account for such variations, though this requires a request and a court hearing, likely obliging the debtor to incur another expense for lawyer assistance. In fact, few plans are modified; instead, two-thirds simply fail to fulfill the promised payments and are dismissed or converted to Chapter 7 liquidation cases. That is, only about one-third of Chapter 13 debtors manage successfully to complete their payments and receive a discharge.¹¹

Thus, before seeking relief, the debtor must decide which track toward relief to pursue, a liquidation under Chapter 7 or a payment plan under Chapter 13. Given the comparative burdens and benefits of each, not surprisingly, a relatively stable 70% of debtors have chosen the quicker and less demanding route of a Chapter 7 liquidation and discharge. The more interesting question here is why any debtor would opt for the more demanding and risky Chapter 13 track, especially in light of the significant failure rate. For continuing small business owners, the answer is more obvious, since only Chapter 13 allows the debtor to carry on the business. Chapter 13 for such people represents a simpler, more direct, and much less expensive option than Chapter 11 for a small business reorganization.

For *former* small business people and other individual debtors with no ongoing business operations, the choice of Chapter 13 is usually made to protect an asset that otherwise would be seized by a secured creditor; *i.e.*, a home or a vehicle. In a liquidation, debtors can negotiate with their secured creditors to retain collateral such as cars and homes, but the dire financial situation of such debtors and the elevated price of such collateral often complicates the negotiation as to the terms upon which the debtor will “redeem” the collateral or “reaffirm” the

⁷ Scott F. Norberg & Andrew J. Velkey, “Debtor Discharge and Creditor Repayment In Chapter 13,” *Creighton Law Review* 39 (2006): 473.

⁸ 11 U.S.C. § 1325(b)(2).

⁹ 11 U.S.C. § 1325(a)(3).

¹⁰ Jean Braucher, “Lawyers and Consumer Bankruptcy: One Code, Many Cultures,” *American Bankruptcy Law Journal* 67 (1993): 501, 532, 546-47, 550-51.

¹¹ Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, “Who Uses Chapter 13?,” in *Consumer Bankruptcy in Global Perspective* (Portland: Hart Publishing, Johanna Niemi-Kiesiläinen, Iain Ramsay & William Whitford eds., 2003): 269, 273, 274-75 & tbl. 1.

obligation secured by the collateral. Particularly in the context of home mortgage foreclosure, Chapter 13 offers debtors a mechanism for immediately and automatically staying the secured creditor's enforcement action, forcing the creditor to accept payments to cure a default over a "reasonable period" in the payment plan, and returning the secured loan to a normal servicing schedule. All of this can be accomplished in a Chapter 13 plan without the secured creditor's consent. Aside from a few instances of debtors whose feelings of honor or pride prompt them to choose Chapter 13, debtors have little economically sensible reason for choosing the payment plan track other than to preserve a business, home, or expensive vehicle.

8.2.6 Coercive sorting by way of the "means test"

Legislators tried to remedy the failure of the new Chapter 13 to attract significant interest in two ways. First, in the completely redrafted Bankruptcy Code effective in 1979, the attractiveness of Chapter 13 was enhanced by expanding the range of debts that could be discharged in Chapter 13 but not in Chapter 7 (see below on the large number of non-dischargeable debts in US law). This change had little noticeable impact on debtor choice, and the criticisms of creditors and conservative commentators grew in intensity during the 1980s and early 1990s. During a period of general economic prosperity, how could it be, these bankruptcy critics asked, that millions of US consumers were evading their obligations in a simple Chapter 7 liquidation? And why should the returns to these people's creditors be limited to their few assets when the credit extension decision had been made based on these debtors' anticipated future earning capacity? Should not that future earning capacity be brought to bear before depriving creditors of the essential benefit of their bargain? Indeed, the most aggressive and vocal critics suggested that immorality and irresponsibility, rather than lack of ability to pay, must be driving debtors to choose the easy way out in Chapter 7 rather than trying to fulfill their obligations in a multi-year payment plan.

Despite substantial empirical evidence of the very depressed economic situation of the vast majority of debtors, the rhetoric of condemnation continued for supposed masses of debtors who had the means to pay back some of their debts if only the system called on them to do so responsibly. From this rhetorical theme, a new and cumbersome mechanism emerged for sorting the "can't pay" debtors from the "won't pay" debtors and compelling the latter group to seek relief under Chapter 13. This sorting mechanism has been called informally the "means test," as it is designed to identify those debtors with the "means" to pay creditors and to prevent them from seeking relief under Chapter 7 and not bringing those "means" to bear on creditor payment. The "means test" was incorporated into an existing statutory provision that had always allowed the court to dismiss a Chapter 7 case for a debtor if "the granting of relief would be an abuse."¹² It also affects the requirements for payments in a Chapter 13 plan, whether or not the debtor elects or is forced into Chapter 13. The formerly open-ended provision on Chapter 7 abuse was elaborated with a complex series of tests and calculations to establish a presumption of abuse for debtors whom the test revealed to possess sufficient means to make substantial payments in a more tightly controlled five-year Chapter 13 plan.

For current and former entrepreneurs, the means test contains an important twist. US lawmakers generally favor business interests, especially small business, and the means test reflects this

¹² 11 U.S.C. § 707(b).

favoritism. The test allows for dismissal of a Chapter 7 case only if the case was filed by an individual “whose debts are primarily consumer debts.”¹³ While the term “consumer debt” is defined to include only debts for personal, family, or household purposes, the term “primarily” is not defined. The courts have struggled with the application of this provision in cases involving former small business owners in particular. Generally, “primarily” has been given a connotation of “majority,” so if more than 50% of the debtor’s debts are related to business, the means test does not apply. On the other hand, even for former entrepreneurs, a home mortgage is a consumer debt, and a large mortgage debt alone might well exceed the debtor’s clearly “business” debts. Moreover, since many small business owners finance their businesses using general-purpose credit cards (or home equity mortgages and lines of credit), the distinction between consumer and business debt may blur to such a degree as to subject many former entrepreneurs to the means test. In any event, some trustees have taken the position that ability to pay as indicated by the means test is a general basis which, in light of the totality of *any* debtor’s financial circumstances, could support a dismissal of a Chapter 7 case based on abuse, even if the debtor is technically not subject to the means test.¹⁴ This is a hotly contested issue, but many if not most current and former individual entrepreneurs are subjected to the means test in restraining their choice of Chapter 7 liquidation. Moreover, for all debtors (no matter the composition of their debts) who either elect or are forced into a Chapter 13 payment plan, the means test plays an important role in determining the required payments, as discussed below.

The means test analyzes individual debtor’s finances in two steps. If the debtor “passes” either step of the means test, abuse is *not* presumed based on ability to pay, and the case proceeds as described above (either with liquidation or with an elected payment plan not impacted by the means test). Debtors who “fail” both steps of the means test are essentially barred from Chapter 7 and may seek relief, if at all, only pursuant to a five-year Chapter 13 payment plan with maximum allowable expense deductions defined by the means test. All but a small fraction of debtors, however, have “passed” one or both steps of this test every year.

Debtors pass the first step if their “current monthly income” (CMI) falls below a defined threshold. The contrived legalese concept of “current monthly income” bears little relation to reality or common sense, however, as that term means the average of the debtor’s monthly income over the six-month period preceding the filing of the bankruptcy petition.¹⁵ Most debtors visiting a bankruptcy lawyer have experienced an income disruption (*e.g.*, unemployment, divorce, medical problem), so their backward-looking income is generally depressed, even if they indeed *do* possess the “means” to make future payments. This test is thus often *underinclusive* in that it fails to capture debtors whose anticipated future income might be sufficient to pay a substantial dividend to unsecured creditors. Of course, it is also *overinclusive*, as it captures some debtors who happen to have received a large gift, bonus, commission, tax refund, or other payment during the preceding six months and whose future monthly income will not include the extraordinary amount. This is particularly likely to be true for former small business people with irregular income streams.

¹³ *Id.*

¹⁴ 11 U.S.C. § 707(b)(3)(B).

¹⁵ 11 U.S.C. § 101(10).

This retrospective average monthly income figure is then multiplied by twelve, because unlike in Europe, income in the US is almost always discussed and analyzed in terms of *annual*, not monthly, amounts. The resulting annual figure is then compared with the inflation-adjusted median family income of a household of the same size as the debtor's in the debtor's state, as reported twice a year by the US Census Bureau.¹⁶ For example, as of May 2012, the median gross (pre-tax) income for a family of three in Illinois, a relatively average state, is just under \$70 000 per year (about €4000 per month). The median for a family of three in one of the poorest states, Mississippi, is just under \$47 000 (about €2600 per month), and in one of the richest states, Connecticut, just under \$83 000 (about €4600 per month). As one would expect of people seeking debt relief, consistently around 90% of all debtors filing under Chapter 7 in the years since the implementation of the means test have passed this median-or-below income test.¹⁷

The 10% of “above-median income” debtors forced to proceed to step two of the means test must then subtract a series of actual or presumed expenses from their contrived “current monthly income” figure to reveal whether significant “disposable income” remains for distribution to creditors. After deducting standard monthly allowances for food, clothing, housing and transportation, in addition to amounts contractually due to secured and priority creditors in the next five years, abuse is presumed if the remainder exceeds about \$180/€20 per month (that is, an amount that would allow the debtor to pay creditors at least \$11 725 over an imposed five-year plan).¹⁸

A comparison of the basic budget allowance for debtors under Dutch and US practice indicates the degree to which US law expects debtors to reduce their standard of living to quite a minimal level. Both the US means test and the Dutch guidelines for the *vrij te laten bedrag* developed by *Recofa* allow for a baseline standard budget for household expenses. While Dutch law incorporates a uniform national social assistance level enacted by the legislature, the US law incorporates a uniform national minimum budget designed and implemented by a federal administrative agency, the taxing authority (Internal Revenue Service). For example, as of May 2012, the baseline monthly budget allowance is \$565 (€375) for singles, \$1030 (€685) for two-person households, and \$1230 (€820) for three-person households. Similarly situated Dutch debtors would be budgeted about twice as much - a minimum of €300 per month for singles and about €200 for couples, with the possibility of substantial increases for working debtors, especially those earning overtime pay.¹⁹ Legislators in the Netherlands felt that asking debtors to live on the Dutch minimum income for more than three years was socially irresponsible; they

¹⁶ The applicable median figures are based on census data and consumer price indices and are available on the US Trustee's website at <http://www.justice.gov/ust/eo/bapcpa/meanstesting.htm>.

¹⁷ See, e.g., US Dept. of Justice, “United States Trustee Program: Annual Report of Significant Accomplishments, Fiscal Year 2010” (2011): 19, www.justice.gov/ust/eo/public_affairs/annualreport/docs/ar2010.pdf.

¹⁸ 11 U.S.C. § 707(b)(2)(A)(i). The actual dollar figure is indexed for inflation every three years, and the test is actually more complex than described. Debtors with more than \$28 000 but less than \$47 000 in unsecured debt can be denied access if their “disposable” income exceeds about \$120/€30 per month and over a 60-month plan would pay 25% of their unsecured debt (and at least \$7025).

¹⁹ Werkgroep Rekenmethode vtlb van Recofa, *Vtlb-rapport* (2011), http://www.wsnprvr.org/download/vtlb/Vtlb-rapport_jan_2011.pdf. I understand that the Dutch allowances combine a portion of the basic rental housing allowance with the basic budget allowance, currently to the extent of €194, while the US system makes entirely separate limited allowances for housing. See *id.* at 35. If I am right about this, this small difference hardly diminishes the shocking disparity between the US and Dutch basic budgets.

would likely be shocked to see the social irresponsibility of the US bankruptcy system that suggests that financially distressed citizens should be relegated to much lower budgets for five years.

Even considering the subsistence-level budget allowances, only a small fraction of the *above-median income* debtors have failed this second step of the means test by showing more than \$180 per month in “disposable” income. This is probably true in large part thanks to an unlimited deduction allowance for payments due on secured debts over the following five years. While Dutch practice under the *Recofa* guidelines would usually call for a homeowner to sell a privately owned residence,²⁰ the means test allows an unlimited deduction of home mortgage payments, no matter how extravagant or expensive the home. Spiraling US home price inflation not only led to the greatest world economic crisis since the 1930s, but it left many debtors with very large mortgage obligations, the payments on which likely reduce the disposable income of most debtors to close to zero. The secured debt deduction is available for car payments, secured business debts, and other secured debts, without limitation and without questioning the need or even utility of the secured collateral. This, of course, is in sharp contrast to Dutch practice, and it reflects US lawmakers’ favoritism toward secured lenders (and the favored position of secured debt in Chapter 13 payment plans).

While fewer than 1% of all Chapter 7 filers have been revealed as potential “abusers” of the quick relief of a Chapter 7 liquidation, even fewer debtors have faced dismissal of their petitions. One last safety-valve allows the system administrator (the US Trustee) the discretion to decline to seek a dismissal or conversion to Chapter 13 in light of “special circumstances.” The US Trustee has exercised this discretion in at least half (in recent years, 60-70%) of the presumptively abusive Chapter 7 cases in light of the “special circumstance” of debtors’ unemployment. Nonetheless, despite the fact that only a fraction of 1% of Chapter 7 filings are ultimately dismissed as “abusive,” debtors in *every* one of the *nearly one million* Chapter 7 cases filed each year in the US must shoulder a weighty paperwork burden to comply with this credit counseling and means testing nonsense. Moreover, the case trustee in *every* one of these *nearly one million* Chapter 7 cases must review the paperwork and file a statement explaining whether each debtor “passes” or “fails” the means test, and if dismissal is not sought, the US Trustee must explain in a written statement why the dismissal should not be imposed.²¹

8.2.7 Discharge and denial of relief

For all individual debtors, the post-reform US law imposes one final unique requirement for obtaining the discharge. Individual debtors must submit a certificate attesting that they have received “an instructional course concerning personal financial management” after filing their case but before receiving a discharge.²² The content of this generally two-hour course is regulated by the system administrator (the US Trustee) and imposes another charge of about \$50 on the emerging debtor. Most debtors have reported that the course was utterly unhelpful, but

²⁰ Recofa-richtlijnen voor schuldsaneringsregelingen, Article 3.7.

²¹ 11 U.S.C. §§ 704(b)(1), 707(b)(1), (2)(C).

²² 11 U.S.C.A. §§ 727(a)(11), 1328(g).

some expressed satisfaction that it taught them something of use in their new freshly started financial life.²³

Assuming compliance with the financial management course requirement, upon completion of the usually four-month Chapter 7 liquidation case, or upon completion of the usually five years of payments under a Chapter 13 plan, the debtor presumptively and automatically is granted a discharge. The court is not called on to “decide” whether the debtor has earned relief; rather, the statute directs that “the court shall grant the debtor a discharge.”²⁴ For Chapter 7 liquidation cases, however, this order is not without reservation. A Chapter 7 debtor can be denied a discharge based on several enumerated statutory bases, mostly involving fraud, refusal to comply with trustee or court orders, or concealing assets or documents. For former entrepreneurs, a particularly salient basis for denial of discharge is that the debtor has “failed to keep or preserve any recorded information, including books, documents, records, and papers, from which the debtor’s financial condition or business transactions might be ascertained, unless such act or failure to act was justified under all of the circumstances of the case.”²⁵ This provision gives the court rather broad discretion to decide that the debtor’s bookkeeping has been inadequate, and unjustifiably so. No clear trend can be discerned as to how this provision is applied, other than to note that denials of discharge are extremely uncommon.

For debtors who make it past the Scylla of the means test and the Charybdis of the denial of discharge provisions, the famed “fresh start” of US bankruptcy law awaits, though the start is not nearly as fresh as one might expect. US law excepts more debts from discharge than any other individual bankruptcy law in existence. The range of such excepted claims differs slightly in the two types of cases. In Chapter 7, debts based on the following are not subject to the discharge at all: (1) income taxes less than three years old and property taxes less than one year old (as well as loans from third parties made to finance the payment of such taxes); (2) value obtained by fraud, including as a matter of law debts for more than \$600 for “luxury goods” incurred within 90 days before the petition date or cash advances of more than \$875 incurred within 70 days of the petition date; (3) embezzlement or theft (larceny); (4) domestic support obligations (child support or alimony owed to a former spouse), as well as property division obligations arising from a divorce or separation action; (5) “willful and malicious injury” to the person or property of a third party; (6) fines and penalties owed to governmental units not related to compensation for financial loss to such units; (7) student loans (unless the debtor makes an exceptional showing of “undue hardship”); (8) death or personal injury caused by the debtor’s operating a motor vehicle under the influence of drugs or alcohol; (9) orders of restitution following criminal conviction under federal law; (10) fees or assessments owed to a condominium or homeowners’ association that come due after the petition date; and (11) deferred filing fees for any civil suit brought *in forma pauperis* by a prisoner, as well as costs imposed on the prisoner following an adverse judgment.²⁶

²³ Deborah Thorne & Katherine M. Porter, “Debtors’ Assessments of Bankruptcy Financial Education,” in *Consumer Knowledge and Financial Decisions: Lifespan Perspectives* 197 (Douglas J. Lamdin, ed., New York: Springer, 2011), <http://ssrn.com/abstract=1654417>.

²⁴ 11 U.S.C. §§ 727, 1328(a).

²⁵ 11 U.S.C. § 727(a)(3).

²⁶ 11 U.S.C. § 523.

The list of debts not subject to discharge following successful completion of a Chapter 13 payment plan is slightly smaller: “Willful and malicious” injury debts are dischargeable in Chapter 13, as are debts for fines owed to government units, restitution orders, and prisoner litigation fees and costs.²⁷ For Chapter 13 debtors, the path to a fresh start is longer and more perilous, and two-thirds of them never arrive at this final destination. Some of these debtors may receive relief even if they do not complete their payment plans, however, though the requirements for such “hardship discharges” are quite strict and are rarely satisfied.²⁸

8.3 United Kingdom (England & Wales)

8.3.1 Introduction

Moving from the United States to the United Kingdom brings one closer to the *Wsnp*, both geographically and in terms of the operation of individual insolvency law. This brief comparative discussion will set aside the somewhat different law in Scotland, focusing on the law of England and Wales in the Insolvency Act 1986, as amended by the Enterprise Act 2002 (effective April 2004 and, according to the DTI white paper that led to its enactment, containing “a major package of reforms . . . to encourage entrepreneurship and responsible risk taking, which will contribute to the creation of wealth and employment”²⁹). Like the US Bankruptcy Code, the Insolvency Act offers two paths to relief: liquidation bankruptcy and payment plans in the form of “individual voluntary arrangements,” or IVAs. The resemblance to US law ends at this superficial level, however, as the British personal insolvency systems tracks much more closely to the Dutch.

8.3.2 The more effective *minnelijk traject* in England and Wales: IVAs

Designed with small entrepreneurs in mind, the IVA track allows individuals to avoid the stigma of bankruptcy by negotiating repayment arrangements with creditors outside the formal relief system but supported by several of its key legal provisions. While the Insolvency Act does not require debtors to seek informal compromises with their creditors as a condition to requesting formal bankruptcy relief, many debtors nonetheless do so. The majority today are likely *not* present or former entrepreneurs, but wage-earning employees, and they pursue both an informal counseling route, as in the US, and the more structured IVA approach. Like the some 30% of debtors who choose Chapter 13 payment plans in the US, British debtors opt for IVAs to avoid the social and financial stigma of bankruptcy, the professional restrictions of a bankruptcy adjudication (though these are far less significant today, as discussed below), and to save businesses and other property interests from liquidation.

To initiate the IVA process, a debtor must approach a licensed insolvency practitioner (IP) to act as a “nominee” in formulating and negotiating the payment plan, as well as to act as “supervisor”

²⁷ 11 U.S.C. § 1328(a).

²⁸ See 11 U.S.C. § 1328(b).

²⁹ Department of Trade and Industry, White Paper Cm 5234, *Productivity and Enterprise: Insolvency – A Second Chance* (2001), online at <http://www.insolvency.gov.uk/cwp/cm5234.pdf>.

in administering the payments.³⁰ Though the IP must present a report to the court on the viability of a proposed IVA,³¹ the terms of the IVA are unregulated; the only driving consideration is to propose an arrangement more attractive to creditors than bankruptcy would be, since an IVA can be implemented only with a vote of acceptance by 75% in value of unsecured creditors.³² Because debtors with excess income are likely to be required to offer three years of payments to creditors even in bankruptcy (as discussed below), debtors generally promise five years of payments to sweeten the attractiveness of an IVA. Again, the level of austerity that the debtor is willing to endure for this period, and that the creditors demand of the debtor, are left totally to the IP-intermediated negotiations with the body of creditors.

In recent years, the US trend of waning creditor enthusiasm for negotiated compromises has been observed in England and Wales, also. A trade association representing the interests of large commercial lenders, the Insolvency Exchange (TiX), often controls at least 25% of the debt in any individual insolvency case, and the members of this association have ratcheted up their demands in accepting IVA proposals. First, they have increased their demands as to the percentage payments expected from acceptable IVAs, called the “hurdle rate,” to as high as 45%. Second, they have objected to the amount and method by which IPs “front load” the extraction of their own payments from IVAs (often as much as £2000 for setting up the IVA and as much as £10 000 for administering the payments). Nonetheless, the percentage of individual insolvency cases concluding with an IVA has remained in the region of about 40% from 2006 through 2011, a significant increase over pre-2006 levels, which had hovered around the low 20% region.³³ The heightened demands on the debtor, as well as the vicissitudes of modern economic life, often lead to failure of IVAs, however, leaving the debtor without relief and likely in a worse position than before.

8.3.3 Bankruptcy liquidation and income payment orders

The traditional, more aggressive, and most popular form of relief in both the US and UK is personal bankruptcy. British bankruptcy hews closer to the Dutch model, however, in that it combines a liquidation of non-exempt assets with a requirement that some debtors make payments to their creditors from future income. Also, the property exemptions regime in Britain is much less generous than most US jurisdictions, so debtor equity in homes, in particular, is generally sacrificed to creditors in UK bankruptcy (though the extraction of equity might not take place for several years after a bankruptcy filing, as the trustee’s rights in residences might be preserved by charging orders until the debtor sells the property later).

While the Insolvency Act does require debtors to qualify for bankruptcy relief by demonstrating an inability to pay his or her debts, this entry requirement is little more than a technicality for all practical purposes. The real barrier to entry for many debtors, like in the US, has been cost, though not for lawyers. The official filing fees include not only a £175 fee for court costs, quite

³⁰ A new “fast track IVA” process allows debtors to move out of bankruptcy and into the IVA track, with the Official Receiver acting as nominee and supervisor of the arrangement. This option, however, has proven all but superfluous, since it offers little or no benefit over the traditional IP-managed IVA process.

³¹ IA 1986 s 256A.

³² Insolvency Rule 5.23(2).

³³ For information on the insolvency system and statistics, hardly a better resource can be found than the official Insolvency Service website, at <http://www.bis.gov.uk/insolvency>.

similar to the US filing fee, but also a £525 deposit toward the Official Receiver's administration of the case, bringing the total required filing fee to £700, nearly as much as US debtors pay for both court costs and attorney fees for Chapter 7 liquidation cases. A lower-cost option ("debt relief order" or DRO, costing only £90) is available only to debtors with few debts and even fewer assets, so this option is likely unavailable to former entrepreneurs, who may be "priced out" of bankruptcy.

Bankruptcy in the UK diverges from the US model and moves toward the Dutch approach in its treatment of the debtor's future income. The Insolvency Act joins the *Wsnp* in attempting to extract some future payment for creditors. Debtors in bankruptcy in England and Wales can be subject to Income Payment Orders, requiring payment of all future income beyond "reasonable domestic needs," generally for a term of three years.³⁴ Whether or not to require such payments, and how to interpret the debtor's "reasonable domestic needs," is entirely within the discretion of the Official Receiver, subject to court approval. Since the Enterprise Act 2002 introduced the possibility in 2004 of debtor acquiescence to such payments in an Income Payments Agreement (to avoid lengthy and expensive court battles with the Official Receiver), the percentage of debtors subject to such future payments has risen from about 10% to about 20%. Nonetheless, the remaining 80%, like the vast majority of debtors in US Chapter 7 and the Dutch *Wsnp*, have barely enough income to support their families, leaving nothing to pass on to creditors.

8.3.4 Automatic discharge, fewer restrictions

Like US law, the Insolvency Act sets forth the automatic benefit of the debtor's bankruptcy: "A debtor is discharged from bankruptcy at the end of the period of one year" after the case commencement date.³⁵ The Official Receiver *can* file a notice before this time to challenge the debtor's discharge, but such challenges are presented in only about 2% of cases.

Somewhat more common are requested restrictions on the debtor's ability to engage in financial and professional life following bankruptcy. Until 2004, debtors often languished in an "undischarged" state for years on end, and undischarged bankrupts were and still are subject to a variety of restrictions. For example, they cannot act as a company director, manage a company, hold a wide variety of public offices, or obtain more than £500 of credit without explicitly disclosing their bankruptcy.³⁶ The Enterprise Act 2002 did not do away with all of the negative effects of bankruptcy, but it alleviated the former restrictions regime significantly. Debtors are freed from the state of being "undischarged" now automatically after one year, and the discharge can occur even earlier than this if the Official Receiver concludes that further investigation is unnecessary. As a result, debtors receive a "fresh start" and can return to professional and financial activity as a legal matter much faster now, though some professional licensing organs and commercial credit granting institutions might continue to impose negative consequences on discharged bankrupts.

The Official Receiver can request, however, that the court subject some debtors to the former regime of longer-term restrictions on their post-discharge activity through the entry of a

³⁴ IA 1986 s 310.

³⁵ IA 1986 s 279(1).

³⁶ The full schedule of restrictions is available online at

<http://www.bis.gov.uk/assets/insolvency/docs/personalinsolvency/schedulebankruptcyrestrictionsjuly2009.pdf>.

“bankruptcy restrictions order” (BRO). Such an order maintains some or all of the restrictions imposed on an undischarged bankrupt for a specified period of time *after* discharge, ranging from 2 to 15 years.³⁷ BROs most often extend for a term of only 5 years, and they are entered in a small number of cases (less than 5% in the aggregate). Such an order might be entered, for example in relation to a former entrepreneur, if the Official Receiver believes that the debtor has failed to keep proper business records, though such instances are extremely rare (less than 1% of cases).

8.4 Germany

The provisions on individual insolvency and discharge (*Restschuldbefreiung*) in the German Insolvency Act (*Insolvenzordnung*, or *InsO*) are very similar to those in the *Wsnp* after the amendments to the latter in 2008. Unlike the *Wsnp*, however, the German law never required the debtor to show “good faith.” This omission removes a significant hurdle for small business people seeking relief. The *InsO* also never assigned discretion to the court to develop flexible relief plans with “reasonable and fair” provisions; instead, like the post-2008 *Wsnp* approach, the German law laid down an objective and universal standard for relief: if debtors would give up their non-exempt assets and resign themselves to life on the standard minimum income level from general welfare law for six years (originally seven, but reduced to six shortly after the law became effective), they would receive an all but automatic discharge of their unpaid debts.³⁸

For individual entrepreneurs, both the *Wsnp* and the *InsO* make continuation of the debtor’s business difficult if not impossible in most cases by requiring a liquidation of the debtor’s valuable assets. As a result, very few German debtors continue their businesses while in insolvency. In 2011, for example, of the some 130,000 insolvency cases not involving artificial business entities, only about 1600 involved continuing small businesses. Public information on these cases is scarce and hard to find, but presumably these are service businesses involving few or no tangible assets. Former small business people are somewhat more common in *InsO* proceedings, making up about 17% of the natural person insolvencies in 2011.³⁹

The most notable distinction between Dutch and German law was and is the *much* longer payment plan term, tellingly called in the German law the “good-behavior period” (*Wohlverhaltensperiode*). German legislators included an ingenious system of incentives, or “motivation rebates,” in the law to encourage debtors to hold out for this long period of deprivation. If the debtor makes it through four years of the six-year period, the trustee refunds to the debtor an incentive bonus of 10% of the debtor’s nonexempt income assigned to the trustee during that year. At the end of year five, the rebate grows to 15%, and the end of the sixth year brings the long-awaited discharge of all but a few debts (the German *InsO* excludes from discharge only intentional tort liability, fines and penalties, and the obligation to pay deferred insolvency court costs and fees).⁴⁰ These provisions draw no distinctions between consumers and debtors engaged in business, whether presently or in the past.

³⁷ IA 1986 ss 31, 360(5), 390.

³⁸ InsO § 287.

³⁹ Destatis, Press Release, “5,9 % weniger Unternehmensinsolvenzen im Jahr 2011” (8 March 2012).

⁴⁰ InsO §§ 291-292(1).

The latest reform discussions in Germany have the potential to bring this distinctive aspect of German law into closer conformity with the *Wsnp*.⁴¹ The Justice Ministry has suggested that the six-year good-behavior period might be halved to three, though the most recent statements from the minister reflect strong ambivalence about this. In all likelihood, a discharge after only three years might be made available only to debtors who manage to pay court costs and a minimum dividend to creditors of as much as 25%. Given that an estimated 80% of debtors today are unable to pay even the filing fees, it is extremely unlikely that any significant portion of debtors would benefit from this proposed reduction of one of the longest payment plan periods in all of Europe.

8.5 Denmark

Denmark deserves special note here for three reasons. First, it deserves special credit for starting the wave of personal insolvency laws in Europe with its groundbreaking *Gældssaneringslov*, adopted 9 May 1984 and effective 1 July 1984 (adding a new Part IV to the Danish Bankruptcy Act (*Konkurslov*)). The rest of Scandinavia (except Iceland) adopted laws based explicitly on the Danish model in the early 1990s. Unlike virtually every other law that would follow, however, the Danish law requires no pre-bankruptcy negotiation with creditors. The commission that developed this law specifically rejected the idea behind a *minnelijk traject*, concluding that, as a fundamental policy matter, the debt adjustment system was designed to rehabilitate individuals struggling with hopeless debt by *imposing* reasonable and realistic write-downs on creditors. Debtors would not need to resort to the formal relief system if creditors were reasonable about negotiating relief informally.

Second, in part because of its position at the very vanguard of the new individual insolvency relief movement, the Danish law has struggled with the key issue of whom to offer this (at the time) revolutionary relief. Especially for present and former entrepreneurs, the Danish model has placed serious and often insurmountable roadblocks in the path to relief. A reform effort in 2005 struggled to liberalize the system somewhat, especially for small business people, but it continues to jealously guard the access point to the insolvency procedure. Fear of abuse of this extraordinary relief persists in Denmark, where a complex, two-part admissions test still prevents access by most applicants.

The first entry criterion requires debtors to exhibit “qualified insolvency,” which implies a complete impossibility, free from virtually any doubt, that debtors might return to financial health in the foreseeable future by reducing their living standards and applying their best efforts to paying off debt.⁴² Relief can be rejected at this stage for debtors who dedicate more than what the court in its unguided discretion considers to be a “reasonable” amount of income to living expenses (especially housing and cars). This first test originally all but prevented debtors continuing to operate small businesses from qualifying for relief, as business income makes the debtor’s financial future too unclear to determine “qualified insolvency.” The first and only major reform of this law, in October 2005, was motivated in significant part by a desire to support small business people. Accordingly, one aspect of the reform was to authorize the court

⁴¹ For the latest statements and documents on insolvency law from the Justice Ministry, see http://www.bmj.de/DE/Recht/Rechtspflege/Insolvenzrecht/_node.html, especially the speech entitled “Fortschritte der Insolvenzrechtsreform.”

⁴² *Konkurslov* § 197.

to set aside this “uncertainty” factor for small business debtors, but old habits die hard, as indicated below.

The second entry criterion requires the court to be convinced that offering relief is appropriate in light of a series of factors, such as the debtor’s efforts to manage debt problems and the make-up of the debt load (preferably relatively few fines, penalties, and “irresponsible” debts, such as debts for luxury consumption). Originally, the law required the debtor to overcome a negative presumption, that relief would *not* generally be appropriate. The 2005 reform reversed this presumption; that is, now insolvent debtors should be allowed into the system unless specific circumstances “suggests decisively against” relief for the debtor.⁴³

Despite these two reforms loosening the court’s tight grip on the doorway to relief, the stringent entry requirements have led to an astoundingly high application rejection rate in Denmark. From 2002 through 2004, for example, of an average of about 4700 debt adjustment applications per year, the courts immediately rejected more than half every year. After a spike in admissions following the 2005 reform, acceptance rates fell back to their former low levels and for many years have remained fairly steady at only about 40-45% (2000-2250 of about 5000 applications annually).⁴⁴

A third and final point worthy of note is a parallel development with respect to budgets and payment plans in the Danish law and the *Wsnp*. Despite the lack of guidance in the law, a standard payment term was quickly adopted as the norm in Denmark as in the Netherlands, though the Danish term was a bit longer, at five years. With respect to the amount of debtor income to be reserved for the debtor’s expenses, however, Danish courts exercised their discretion in widely varying ways to define a “modest lifestyle.” Rather than informal standardization through the *Recofa* working group, official standardization was imposed on debtor budgets in Denmark when the Justice Ministry adopted the 2005 reform commission’s proposal to set down clear amounts for the core “reasonable” basic budget. The Justice Ministry’s guidelines are quite similar to those in the *Recofa Vtlb-rapport*, and they offer more uniform, and generally more generous and humane budgets to debtors, especially families with children, than had been imposed by Danish courts earlier.

8.6 France, Belgium, and Luxembourg

Given the *Wsnp*-oriented comparison undertaken here, very little can be said about the very complex and well developed system of *surendettement des particuliers* (consumer overindebtedness) in France as it relates to ex-entrepreneurs.⁴⁵ The provisions in the Consumer Code (*Code de la consommation*) that set out *Wsnp*-type relief in France are not available to debtors who are subject to the collective provisions on business insolvency in book VI of the

⁴³ *Id.* (“*taler afgørende imod*”).

⁴⁴ These figures are based on data from the court administration’s statistics for newly undertaken debt adjustment cases (*insolvensskifter mv.*), online at <http://www.domstol.dk/om/talogfakta/statistik/Pages/skiftesager.aspx>.

⁴⁵ For a discussion of recent developments in the French personal insolvency system and others, see Jason J. Kilborn, *Expert Recommendations and the Evolution of European Best Practices for the Treatment of Overindebtedness, 1984-2010* (Deventer: Kluwer, 2011) [“Law of Business and Finance” series, vol. 11, Sebastian Kortmann & Dennis Faber, eds.] <http://ssrn.com/abstract=1663108>.

Commercial Code.⁴⁶ Former small business debtors and their business-related debts are subject to those provisions, so ex-entrepreneurs are all but completely excluded from the French system for treatment of strictly personal debt (that is, debts not related to present or former business dealings).⁴⁷ Similar restrictions apply in the *Wsnp*-type law in Luxembourg.⁴⁸ The similar Belgian law does not draw a distinction between business and non-business debts, though it does limit entry only to non-merchants and former merchants who have ceased commercial activity at least six months before seeking a “collective debt adjustment” proceeding.⁴⁹

The French restriction has been alleviated somewhat with the implementation in June 2011 of the Ordinance of 9 December 2010, allowing individual owners of limited liability individual enterprises (*EIRL*) to segregate their patrimony into business and personal portions. Their “personal” patrimony, consisting exclusively of debts unrelated to business, now qualifies for treatment in the *surendettement* system under a new chapter III-*bis* in the Consumer Code.⁵⁰

8.7 Conclusions

Surveying all of these systems and their evolution over time, one can observe a gradual migration toward a more efficient and effective central position on several points. First, most make some attempt to favor or facilitate negotiated arrangements with creditors. Most laws require such an attempt in one form or another as a requirement for formal relief, and the Dutch and English systems have seen relatively impressive rates of negotiated or partially negotiated workouts in recent years. Nonetheless, the desire for consensual compromise has been consistently frustrated to greater or lesser degrees everywhere by creditor resistance and the realities of debtors’ limited payment capacity. For former entrepreneurs in particular, the large numbers of creditors in these cases tend to make informal agreements all the more elusive.

Second, flexible and discretionary approaches to payment plans have given way to non-discretionary, standardized adjustment plan requirements. Especially in terms of plan duration, flexibility has been abandoned quite quickly everywhere in favor of one agreed period, though national laws remain divided as to the proper length of that period. Required income turnover has even made its way to the United States, which continues to resist imposing such a demand on all, but even there, one can observe a movement away from discretionary judgments as to “reasonable” expenses and toward a national, uniform standard (though the US and English laws lag behind on this key issue). Though significant time, money, and other resources are dedicated to screening for “can-pay” debtors and forcing as much income distribution to creditors as possible, *most* debtors (the overwhelming majority) actually have nothing extra to offer their creditors. One must continue to ask whether these systems’ efforts to extract a few extra pennies from impecunious debtors is worth the variety of burdens that this Quixotic pursuit imposes on debtors, system administrators, and increasingly strained state judiciary budgets.

⁴⁶ Code de la consommation art. L333-3.

⁴⁷ Code de la consommation art. L330-1 (applying the relief provisions only to “dettes non professionnelles”).

⁴⁸ Loi du 8 déc. 2000, art. 2, Memorial A no. 136 (also limiting relief to “dettes non professionnelles,” but allowing former merchants to engage the system for qualified debts six months after having ceased commercial activity).

⁴⁹ Gerechtelijk Wetboek/Code judiciaire art. 1675/2.

⁵⁰ See JORF no. 0286 du 10 décembre 2010, textes nos. 17 et 18 (NOR: JUSC1027130P et JUSC1027130R).

Third, only the “business-friendly” systems in the United States and England and Wales tend to support a continuation of (or at least quick return to) the debtor’s business activity. The short time frame of a Chapter 7 liquidation or a bankruptcy case under the IA 1986 means that, even if business assets must be liquidated, the entrepreneur is back at the business of entrepreneurship quickly following a resolution of an earlier business failure. Indeed, the Chapter 13 process in the United States even allows for a continuation of an ongoing business, assets and all, during the five-year repayment process, provided this approach produces as good or better returns for creditors as would a liquidation. The newer Continental systems continue to struggle with the notion of small business turnaround, remaining hostage to an earlier conception of the purpose of bankruptcy as purely intended to support creditor collection. The US and British models demonstrate that a better balance can be struck between protecting creditors and invigorating the entrepreneurial spirits of former – and future – small business people.

Finally, though it would have been scandalous to suggest such a thing 20 years ago, consensus has solidified as to the proper form of relief in exchange for whatever sacrifice is demanded of the debtor: automatic discharge of unpaid debts with few restrictions on re-entry into economic life, even for negligent debtors with careless bookkeeping skills. *Pacta sunt servanda* has been displaced as the motto for debt enforcement, giving way to “forgive and forget.” Realism has displaced formality and “principle” when the bottom line is laid bare and there really is nothing to be gained for creditors in trying to squeeze one more drop of blood from stones. Moreover, in an increasingly competitive global economy, lawmakers have realized that repressing entrepreneurship for overly extended periods results in losses not only for debtors and their localities, but also for the nation in the international race for new ideas and products. Rather than vilifying the “bankrupt,” legislators by and large now acknowledge and embrace the idea that entrepreneurship is about making mistakes and getting back up after failure. The agreed point of these systems, especially for former small business people, is to get debtors back on their feet, back in the game, and back to applying their energies to being creative, productive, and . . . entrepreneurial!

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