



# Bankruptcy

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## Introduction

Bankruptcy is a process that results in the property and affairs of a person in financial difficulty being administered by a trustee for the benefit of creditors as set out in the *Bankruptcy Act 1966* (Cth) (Bankruptcy Act). Bankruptcy imposes immediate restrictions and responsibilities, and potentially limits a bankrupt's future financial and employment opportunities.

A decision to become bankrupt should not be taken lightly, and a person wanting to make the best choice to fit their circumstances should always seek information from an independent source such as a financial counsellor, the Australian Financial Security Authority, a registered trustee, a registered debt agreement administrator, a solicitor or an accountant.

## Bankruptcy – Key Points

Generally speaking bankruptcy lasts for three years.

The steps a trustee will take are to:

- confirm which creditors' debts should be paid
- sell the bankrupt's property
- ensure any creditors given priority in the Bankruptcy Act are paid first
- pay the remaining proceeds to creditors with each creditor paid in proportion to their share of the debtor's total debts.

If there is no registered bankruptcy trustee appointed, the Australian Financial Security Authority (AFSA) administers the estate as the Official Trustee in Bankruptcy.

It is important to seek advice and a list of registered trustees and registered debt agreement administrators is available from the AFSA website.

The AFSA website has a range of resources including a number of short videos to provide information to clients on key personal insolvency topics such as *Unmanageable Debt—Where to find help* and *Consequences of Bankruptcy*.

## The Australian Financial Security Authority

The Bankruptcy Act is administered by the AFSA, an executive agency in the Commonwealth Attorney-General's portfolio. The AFSA is responsible for:

- the administration of personal bankruptcy law and practice
- the Personal Property Securities Register—an online government noticeboard of security interests in personal property

The Official Trustee in Bankruptcy, the Official Receiver and the Inspector-General are each established under the Bankruptcy Act and supported by AFSA staff and resources.

The AFSA has a number of key bankruptcy-related roles, including to:

- act as trustee for personal insolvency administrations

- act as trustee pursuant to court orders particularly under the Proceeds of Crime legislation
- act as special trustee for government
- provide practical information about options to deal with unmanageable debt
- preserve the security and integrity of a large volume of personal insolvency records.

## Regulation of bankruptcy trustees and debt agreement administrators

The AFSA's key roles in regulation and enforcement include:

- regulating personal insolvency practitioners
- investigating alleged Bankruptcy Act and *Personal Property Securities Act 2009* (Cth) offences and where appropriate referring for prosecution.

People with complaints about trustees and administrators should contact the AFSA.

## To Bankrupt or not to Bankrupt

### Advantages of bankruptcy

Going bankrupt removes the immediate pressure of dealing with individual creditors as all creditors must communicate and lodge their claims with the trustee rather than directly with the debtor. Most unsecured creditors are not permitted to take any legal or other action to recover or enforce any claim against the debtor or their property for debts incurred prior to the debtor becoming bankrupt.

The rights of secured creditors (e.g. banks with mortgage) are not affected.

### Disadvantages of bankruptcy

#### Property

Except for a very restricted range of items, property of a bankrupt at the date of bankruptcy or acquired during the bankruptcy is collected and sold by the trustee.

#### Financial institutions

Banks, building societies, credit unions and other financial organisations must inform the bankrupt's trustee when they become aware that an undischarged bankrupt has an account with them, unless they are satisfied that the account is on behalf of some other person.

Payments must not be made out of that account without written instructions from the trustee.

#### A public record

The record of bankruptcy is added to a register, which can be accessed by the public. The AFSA maintains a computerised database (the National Personal Insolvency Index (NPII)) on which all insolvency proceedings under the Bankruptcy Act are recorded. If a debtor becomes bankrupt that will be a permanent record on the NPII. The public can access the NPII for a fee.

However, if a debtor or bankrupt believes that publishing their address and/or occupation on the NPII may put their safety at risk, they may apply to have the address and/or occupation suppressed. An application to have information suppressed must be made in writing to the Inspector-General.

The statement of affairs of the bankrupt, apart from the confidential Part A, can be searched by the public for a fee, and by a creditor without charge. Searches of the NPII database can be conducted through AFSA's Bankruptcy Register Search or via an index search agent. Credit reporting businesses also record details of bankruptcies.

A bankrupt must deliver to the trustee all documents and papers in their possession that might relate to any of their business dealings, property and financial affairs.

Transactions, gifts or transfers of property that took place particularly during the past five years will be examined, and the trustee may seek to have certain transfers set aside resulting in the trustee taking the property for the benefit of creditors.

The bankrupt may be made to appear at a public examination. Members of their family and their associates may be questioned concerning the bankrupt's financial affairs to help identify property that may be recovered by the trustee for the benefit of creditors.

The bankrupt's trustee will decide if the bankrupt must answer questions in front of either the Official Receiver or a court.

### **Income earned during bankruptcy**

If the bankrupt earns above a threshold, the Bankruptcy Act imposes a liability on the bankrupt based on their income after tax and a formula in the Bankruptcy Act (s 139S). They must make regular payments of the assessed amount to the trustee for the benefit of the creditors. The current threshold amount can be obtained from the AFSA website.

If the trustee informs the bankrupt of their contribution assessment and the bankrupt fails to make payments, the trustee is able to ask AFSA to use its powers to deduct those contributions directly from the bankrupt's wages or other sources of income. It is an offence for an employer to dismiss a bankrupt because the employer is required to deduct amounts from the employee's pay (s 139ZP Bankruptcy Act).

### **Approval needed to travel overseas**

A bankrupt may be required to deliver their passport to the trustee and may not be permitted to travel overseas without the trustee's permission.

### **Borrowing money—notification of potential creditors during bankruptcy**

A bankrupt must not incur credit above an amount fixed by law or draw a cheque for more than that amount without first disclosing that they are an undischarged bankrupt. The current amounts referred to can be obtained from the AFSA's website.

### **Prohibition on managing a company**

The bankrupt is prohibited from managing a company without the permission of a court (s 206B *Corporations Act 2001* (Cth)).

## Credit rating

A bankrupt's credit rating will be affected.

## Who would benefit most from bankruptcy

Although there are significant disadvantages in becoming bankrupt, bankruptcy may be the most suitable course of action for some people. These people include:

- low-wage earners, especially those with large families, pressing debts or special expenditure requirements, such as a sick or disabled family member
- single parents who do not own a house, whose household goods have been purchased on credit (but not subject to a bill of sale), who are receiving a supporting parent benefit or pension, who are being harassed by their creditors and who are unlikely to earn any other income in the near future
- estranged spouses/partners who have debts of their own and who are otherwise in the same position as the single parents just described, although many debts for household goods may also be the responsibility of the other spouse
- pensioners (unless they own a house or goods other than household goods).

## Criteria for Bankruptcy

### Who can become bankrupt?

Individuals resident in Australia or non-residents who have an Australian connection can choose to become or be made bankrupt. This includes people who do not operate a business, who are in business as sole proprietors or in partnership, and people with joint debts.

### Who cannot become bankrupt

#### Companies

Insolvent companies are administered or wound up under the *Corporations Act 2001* (Cth). Directors of companies who have given personal guarantees to creditors of the company, or who are found by a court to have allowed their company to trade while it was insolvent, may be made liable for some or all of the company's debts and be made bankrupt if they do not pay those debts personally. The Australian Securities and Investments Commission and the AFSA may cooperate to investigate the financial affairs of a director of an insolvent company who becomes bankrupt.

#### People who can pay their debts

People may have their bankruptcy petition rejected when it appears they have sufficient money or assets that they are able to convert reasonably easily into money to pay all of their debts, and have been bankrupt at least three times or bankrupt at least once in the last five years.

### People lacking capacity to manage their own financial affairs

Generally, a person who has power of attorney is not empowered to petition for bankruptcy on behalf of the person who does not have capacity to manage their own financial affairs. A person may apply

to the Queensland Civil and Administrative Tribunal to have the affairs of a person who lacks capacity administered. An application may then be made to petition for bankruptcy.

It is not possible for a creditor to bankrupt someone who is legally unable to sufficiently understand their own financial affairs to commit an act of bankruptcy.

## How to Become Bankrupt

There are two main ways a debtor may become bankrupt:

- voluntarily—a debtor becomes bankrupt when their debtor’s petition is filed with the Official Receiver of the AFSA and accepted
- through a court order—a debtor becomes bankrupt when a sequestration order is obtained by a creditor.

### Voluntary bankruptcy

To become bankrupt voluntarily, a debtor must fill out two forms:

- debtor’s petition
- statement of affairs.

These forms are available from the AFSA. On the statement of affairs, the debtor must show all debts owed to creditors. The debtor becomes bankrupt when the Official Receiver accepts the debtor’s petition. This will only occur if the statement of affairs is also adequately completed.

### Bankruptcy by a creditor

In order for a creditor to obtain a court order making a person bankrupt, that creditor must go through a number of steps. These steps include showing that the debtor:

- owes a debt of at least \$5000 and
- has committed an act of bankruptcy in the six months before the filing of a creditor’s petition.

Section 40 of the Bankruptcy Act sets out a long list of conduct by which a debtor may commit an ‘act of bankruptcy’. Failure to comply with a Bankruptcy Notice is the conduct that is most commonly relied upon as the act of bankruptcy.

If the creditor satisfies the court that at least one act of bankruptcy has occurred, the court may make a sequestration order (an order for bankruptcy) against the estate of the debtor. Once the sequestration order is made, the debtor becomes bankrupt and continues to be until they are discharged or the bankruptcy is annulled.

### How long does bankruptcy last

A bankruptcy usually lasts for three years and a day from the date on which the bankrupt files their statement of affairs with the AFSA.

At the end of this time the bankrupt is discharged, unless the trustee has objected and extended the bankruptcy to either five or eight years as a result of misconduct by the bankrupt.

The most common reason why bankruptcy is extended beyond the three-year period is failure to cooperate with the trustee by disclosing all of the bankrupt's debts and assets, or non-payment of income contribution assessments.

## Can bankruptcy be ended?

In some cases, a bankruptcy can be brought to an end by annulment (cancellation).

The bankrupt's trustee can issue a certificate of annulment if and when the bankrupt's:

- debts and the bankruptcy's administration fees and expenses have been paid in full
- offer of composition or arrangement to settle for a lesser sum has been accepted by the creditors
- application to the court to have the bankruptcy annulled was successful.

## Administration of a Bankrupt's Property

A debtor's bankruptcy is handled by a registered trustee who has agreed to administer the bankruptcy or, where no registered trustee agrees to do so, by the AFSA.

When a debtor becomes bankrupt, the trustee becomes the legal owner of all of the debtor's property with some exemptions. The trustee has wide powers to deal with or dispose of the property for the benefit of creditors.

Property includes anything of monetary value belonging to the bankrupt at the date of the bankruptcy or coming into the bankrupt's possession during the bankruptcy. The AFSA website has a quick guide *What happens to my belongings*, dealing with what assets a bankrupt is allowed to keep and what will be taken, including:

- property that once belonged to the bankrupt where it can be shown that the bankrupt sold, transferred or gave it to other persons such as family members or a trust, in certain circumstances if that took place within five years of the person becoming bankrupt
- property disposed of with an intent to defeat creditors and not for an adequate value at any time before the person becomes bankrupt
- property transferred within six months of the person presenting their own debtor's petition or a creditor filing a creditor's petition, without intent to defraud, to pay one creditor ahead of other creditors at a time when the debtor, although not yet bankrupt, was unable to pay all their debts
- contributions to superannuation funds made prior to bankruptcy, either by the bankrupt or a third party with the intent to defeat the interests of the bankrupt's creditors.

When assessing whether property is exempt property, the trustee must have regard to the number and ages of members of the bankrupt's household and any special health, medical or other needs of any of those members. The trustee must also have regard to whether the costs of seizure, storage and sale of the property would be likely to exceed the sale price of the property.

## Interest in a house

A bankrupt's interest in a house is not exempt. The trustee may take possession of it and sell it.



If the home is jointly owned by a married or de facto couple and the joint owner does not agree to a sale, the trustee is entitled to obtain an order from a court for the sale of the home.

The proceeds of sale are first paid to discharge any money owing to the financier and any other creditor holding a security registered over the home.

Any remaining proceeds are then divided between the trustee for the bankruptcy and the joint owner who is not bankrupt.

## **Companies and trusts**

Companies and trusts in which the bankrupt has an interest, even indirectly, may be ordered by the court to pay an amount of money to the trustee, which is equal to the value the court assesses to be the bankrupt's interest.

## **Property acquired by the bankrupt during bankruptcy**

During bankruptcy, the trustee has the power to take money or other items that the bankrupt receives such as gifts, lottery winnings or money received under a will. If the bankrupt manages to save money and purchases some property (e.g. shares), this also may be claimed by the trustee.

## **Jointly owned property**

When one joint owner becomes bankrupt, the trustee may seek to become registered as a joint owner on the property title in place of the bankrupt person.

If the difference between the debt to the financier and the likely sale price is small, it is sometimes possible for the other joint owner (if not also bankrupt) to purchase the bankrupt's interest.

Even though the trustee is registered as a joint proprietor, they will not be liable to make any payments under a mortgage, and registration of the trustee as a joint owner does not prevent the mortgage payments falling into arrears. If this happens, the mortgagee may exercise their legal rights against the property with the result that it may be sold by the mortgagee.

A trustee may not usually sell a home mortgaged to the Defence Service Homes because, under the *Defence Service Homes Act 1918* (Cth), permission will only be given for a sale where there is misconduct by the bankrupt.

## **What fees and charges apply**

Bankruptcy trustees generally charge by the hour and debt agreement administrators charge a percentage of payments made by debtors.

There are no filing fees for bankruptcy at the AFSA but there are filing fees for submitting a debt agreement proposal or Part X application (personal insolvency agreement).

There is a charge payable to the government calculated as a percentage of the total receipts in a bankruptcy, Part X agreements and Part IX debt agreements (known as a realisations charge).

The realisations charge is used to pay for regulation of the personal insolvency system and preliminary inquiries into bankruptcies by the Official Trustee in Bankruptcy (AFSA).



The costs of administering a bankruptcy are usually taken from money received in the debtor's bankruptcy.

In most cases this comes from selling the debtor's property and from contributions the debtor may be required to make from their income.

More information regarding fees and charges can be found on AFSA website.

## **Claiming a Bankrupt's Debts**

### **Unsecured creditors**

Generally, creditors who do not have their debt secured on the assets of the debtor by a mortgage or similar arrangement cannot take further action to recover debts. Instead they may lodge claims with the trustee to be able to share in any funds in the bankruptcy.

Important exceptions where bankruptcy does not protect the bankrupt from payment of debts include:

- fines for breaches of the law imposed by a court or tribunal
- fraud debts
- spousal or child maintenance payment
- certain debts to the Department of Human Services
- certain higher education debts and student supplement loans
- the Australian Taxation Office.

The Australian Taxation Office may use tax refund credits to reduce tax debts during the bankruptcy.

### **Service providers**

If the bankrupt has unpaid accounts for essential services, such as electricity, telephone or gas, the supplier might require a bond in order to keep the service connected.

### **Secured creditors, consumer credit contracts and leases**

Creditors, who hold security such as mortgages or bills of sale over the bankrupt's assets or with lease agreements, can recover the secured assets and sell them if payment is in default.

If the bankrupt wishes to retain those assets, the bankrupt must negotiate with the secured creditors and make regular payments.

However, if the assets' value exceeds the amount payable to finalise the agreement, the bankruptcy trustee can sell the assets at any time before the bankruptcy comes to an end.

If there is a shortfall after sale of the assets, the creditor cannot pursue the debtor but can claim in the bankruptcy.

### **Guarantors**

Bankruptcy of a person who owes money does not prevent a creditor from claiming from a guarantor (who is not a bankrupt) under a guarantee and recovering payment from the guarantor.

If a bankrupt has signed a loan agreement jointly with another person, the person who is not a bankrupt will still be liable for the full amount of any debts in joint names.

## **Court Proceedings of a Bankrupt**

If a party to legal proceedings becomes bankrupt, no further action can be taken in that proceeding unless first approved by a court. However, if the bankrupt person is the plaintiff in an action involving a personal injury or wrongdoing to the bankrupt, their spouse or family, the bankrupt may continue the action in their own name and keep any compensation or damages awarded. Otherwise, the trustee will become the proper person to pursue the action or may elect to discontinue it (s 60 Bankruptcy Act).

## **Federal Circuit and Family Court of Australia orders**

The Federal Circuit and Family Court of Australia (FCFCA) has exclusive jurisdiction over matters in which both family law and bankruptcy issues have arisen (s 35 Bankruptcy Act).

Transfers of property ordered or approved by the FCFCA before a person is bankrupt may not be overturned by a trustee, unless the trustee can show that the bankrupt person and the person to whom the property was transferred obtained the order from the FCFCA dishonestly, with a view to protecting the property from the bankrupt's creditors.

When there is a dispute about the relevant share of jointly owned property with a non-bankrupt spouse, the FCFCA has the jurisdiction to decide how the proceeds are shared. Maintenance payments to a spouse or children are specifically protected from the trustee and cannot be recovered by the trustee for the benefit of creditors as preferential payments. However, bankruptcy will not protect a person from making child support payments or paying arrears of child support, as these continue regardless of bankruptcy.

## **Goods subject to a hire purchase agreement or other security interest**

Generally, goods under hire purchase contracts will give rise to a security interest under the *Personal Property Securities Act 2009* (Cth). If that security interest is not 'perfected', which is usually achieved by registration of the interest on the Personal Property Securities Register, when the person becomes bankrupt that property vests in the bankrupt and can be taken by the trustee as part of the bankrupt's estate. However, if the hire purchase company has perfected its security interest, it may repossess the goods according to the terms of the hire purchase contract, which could include repossession rights when a person becomes bankrupt or if payments fall into arrears. If there is money still owing to the hire purchase company after it has sold those goods, the shortfall will be a debt provable in the bankruptcy.

Similar rules apply to security interests arising out of other financing transactions involving personal property such as bills of sale and certain types of leases.

# Responsibilities of a Bankrupt

## Operating a business

The bankrupt can still operate a business while bankrupt. If a bankrupt trades under an assumed name or business name, either as a sole trader or in partnership, the bankrupt must disclose their bankrupt status to everyone they deal with. Under s 206B of the *Corporations Act 2001* (Cth), the bankrupt cannot be a director of a company or be involved in its management without the permission of a court.

## Change of personal details and approval of overseas travel

A bankrupt must keep their trustee informed in writing of all changes of name and/or address (s 80 Bankruptcy Act). If the bankrupt wishes to travel overseas, a written approval of the bankruptcy trustee must be obtained. The trustee may impose certain conditions prior to permission to travel is being granted. A written request for approval of overseas travel should be made to the bankruptcy trustee well in advance of the proposed travel date with details of the reason, timetable and how the expense is being paid (s 272 Bankruptcy Act).

## Disclosure to bankrupt's creditors

The creditors are notified in writing of the bankruptcy as soon as possible by the bankrupt's trustee and will be informed of the assets and liabilities disclosed by the bankrupt in their statement of affairs. Creditors should provide to the trustee information about any assets the debtor has not disclosed.

## Opening a bank or cheque account

With the agreement of the financial institution, a bankrupt can open a bank account (including a cheque account).

# Alternatives to Bankruptcy

## Cooling-off period or moratorium

If a debtor is faced with the bailiff seizing goods or is thinking about becoming a voluntary bankrupt, they can lodge a signed statement with the AFSA stating that they intend to become bankrupt. This is called 'a declaration of intent to present a debtor's petition' (also referred to as temporary debt protection). This mechanism is useful to allow debtors some time to consider their options and seek financial advice.

Under the Bankruptcy Act, the debtor can apply for a 21-day period in which to decide whether or not to become bankrupt. A debtor may seek temporary relief from recovery action taken by a creditor, also referred to as temporary debt protection, by lodging a temporary debt protection form. Once such an application is accepted by the Official Receiver, it prevents unsecured creditors or the bailiff from enforcing their debts for a 21-day period.

A debtor may only make a declaration of intention once every 12 months (ss 54A–54L Bankruptcy Act). It is an act of bankruptcy to give an Official Receiver a declaration of intention to present a debtor's petition. An act of bankruptcy is an action by the debtor that allows any creditor to commence bankruptcy proceedings against the debtor.

## Informal arrangement with creditors

Debtors may discuss their financial difficulties with the creditors and apply for hardship assistance. The creditors might agree, especially if the debtor has a regular income, to allow the debtor to pay off the creditors over time or forego interest. However, informal arrangements will only be binding on those creditors who agree to them. Others may continue to take action to recover their debts.

For an informal arrangement to be effective, it is essential that it be entered into as a deed signed by the debtor and each creditor, and stating that the creditor releases the debtor from liability in consideration of fulfilling the terms of the deed. However, it only takes one dissenting creditor to force the debtor into bankruptcy.

## Part IX debt agreement

A debt agreement is a binding agreement between a debtor and their creditors, where the creditors generally agree to accept a lesser sum of money (pt 9 Bankruptcy Act).

A debt agreement may provide for:

- weekly or monthly payments from the debtor's income or a lump sum
- deferral of payments for an agreed period
- the sale of an asset to pay creditors.

Payment by the debtor is based on their capacity to pay having regard to all their income and household expenses.

### Effect of lodging a debt agreement proposal

When a debt agreement proposal is lodged with AFSA, the creditors can continue to receive payment but cannot enforce any remedy to collect any provable debt. Once the creditors accept the proposal, which becomes a debt agreement, they must cease action to recover payment. The debtor is released from their provable debts when they complete all the payments and obligations under the debt agreement, as if they had been discharged from bankruptcy.

The agreement will be publicly recorded on the National Personal Insolvency Index, for five years from the date of the debt agreement or the date the obligations under the agreement are satisfied, whichever is later.

A debt agreement has the advantage over an informal arrangement with creditors because it is registered and leaves no doubt regarding its enforceability.

A debtor can only make a debt agreement proposal if they are insolvent and have:

- not been bankrupt and used a debt agreement or a personal insolvency agreement under pt 10 of the Bankruptcy Act in the last 10 years
- unsecured debts of no more than the indexed amount
- after-tax income of no more than the indexed amount per year
- property not exempt under bankruptcy of no more than the indexed amount.

## Debt agreement procedure

### *Stage 1: Information*

A debtor must read the prescribed information sheet about the alternatives and consequences of bankruptcy and debt agreements.

### *Stage 2: Debt agreement proposal is lodged*

The debtor is assisted by an administrator to complete and lodge with AFSA the required forms.

There is also a fee payable to the AFSA for lodgement of a debt agreement proposal. There are certain exemptions to this fee including for individuals who have received certain emergency payments after 1 July 2011.

### *Stage 3: Debt agreement proposal is sent to creditors*

The AFSA sends the proposal and explanatory statement to creditors with a report asking them to:

- detail their debts
- vote on the debtor's proposal
- disclose whether they are related to the debtor.

### *Stage 4: Creditors assess debt agreement proposal and then vote*

Creditors assess the proposal and vote over a five-week period. For a proposal to be accepted, AFSA must receive 'yes' votes from a majority in value of the creditors who vote. During the voting period, creditors cannot take debt recovery action against the debtor or the debtor's property. AFSA then checks and counts the votes.

If the proposal is not accepted by creditors, it remains on the public record and creditors are able to commence recovery action including accrued interest.

If the proposal is accepted by the creditors, the debt agreement is recorded on the public record and the debtor, creditors and administrator are informed.

### *Stage 5: Debt agreement is carried out*

The debt agreement administrator is responsible for:

- collecting payments from the debtor
- keeping creditors and debtors informed
- paying dividends equally to creditors
- telling the AFSA when the agreement is completed.

The debtor is only released from their debts when all the payments and obligations are completed by the debtor.

The release does not:

- release anyone else from a debt that is owed jointly with the debtor
- release a guarantor from a guarantee that they gave for the debtor's debt

- prevent a secured creditor from dealing with a security to obtain payment of a secured debt.

When all payments and obligations are completed, the agreement ends. However, a debt agreement may be terminated by:

- a six-month default in payments
- the creditors voting to accept a proposal to terminate from the debtor or a creditor
- an order of the court.

It is an act of bankruptcy to lodge a proposal for a debt agreement. However, while a debt agreement is in force, a creditor cannot:

- present a creditor's petition against the debtor or proceed further with a creditor's petition that was presented against the debtor before the proposal
- enforce a remedy against the debtor's personal property
- start to take fresh steps in legal proceedings in respect of a debt owing at the time of lodging the proposal.

A debt agreement is terminated if the debtor becomes bankrupt.

#### The debt agreement administrator's fees

An administrator may charge a fee for giving the prescribed information and helping the debtor prepare the debt agreement proposal. The administrator charges a fee for administering the agreement as set out in the proposal as a percentage of payments made by the debtor. A realisation charge applies to all payments by the debtor to an administrator and must be paid to the Australian Government.

## Part X personal insolvency agreements

Another alternative to bankruptcy is for a debtor to make a personal insolvency agreement under Part X (pt 10 Bankruptcy Act). Unlike a Part IX debt agreement, there is no upper limit on the amount of the debt owed by the debtor.

The advantage of a formal agreement under Part X is that if a proposal is accepted at a meeting of the debtor's creditors, all creditors will be bound by the resolution of the meeting (even those who voted against it or did not attend), unless creditors are able to show to the court that the resolution was passed as a result of the meeting of creditors having been misled by the debtor, or that a better result for all creditors would be achieved by the debtor being declared bankrupt.

An agreement requires a formal resolution accepting a debtor's proposal to be passed at a meeting of creditors. Although it is not necessary for all of a debtor's creditors to attend the meeting, all creditors must be given formal written notice of the meeting, together with a report and certain disclosures.

A meeting of creditors is called by either an authorised solicitor or a registered trustee in bankruptcy after the debtor has executed an authority in writing for one of them to do so. Registered trustees and solicitors generally require funds in advance for payment of their fees before they agree to call a meeting.

For a resolution accepting a proposal to be passed, at least a simple majority of creditors at the meeting representing 75% in value of their debt must vote for it. Voting may be by person or by proxy.

A decision made in this way binds all creditors, whether or not they have attended and/or voted at the meeting. If a resolution has been procured by a dishonest way, a creditor may apply to the court, usually within 21 days after the meeting, to overturn the resolution passed and to have an order made declaring the debtor bankrupt.

To succeed on such an application, a creditor would need to show that there is a likely greater financial benefit to all creditors if the debtor is made bankrupt. It is not sufficient for a creditor to feel unhappy with the result of the meeting because they have been out-voted.

The main reason why creditors might agree to a Part X agreement is that it will probably cost them less than if the debtor is forced into bankruptcy.

## **Offences under the Bankruptcy Act**

A bankrupt who commits offences under the Bankruptcy Act may be fined or in some cases imprisoned if they:

- dispose of property before bankruptcy with the intention of defeating creditors' claims
- fail to disclose assets to the trustee
- deliberately obtain credit when the debtor knows that they will be unable to pay
- engage in gambling and speculation which results in bankruptcy
- incur debts during bankruptcy for over the indexed amount without disclosing that the debtor is bankrupt
- operate a business under an assumed name, without advising of the debtor's real name and the fact of the bankruptcy
- leave Australia without the bankruptcy trustee's permission
- fail to notify the trustee immediately of a change of name or address.

Further information regarding obligations and consequences of bankruptcy can be found on the AFSA website.



## Legal Notices

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