

# Debt relief for South African NINA debtors and what can be learned from the European approach

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## **Abstract**

The focus of this article is on the international trend of providing debt relief to all hopelessly insolvent individuals, so allowing them a fresh start. Such debtors include those with 'no income and no assets' (NINA), whose access to insolvency proceedings would yield no benefit for their creditors. The initial ultra-liberal American 'straight discharge', or 'fresh start', is contrasted with the 'earned fresh start' approach in Europe. The European approach is investigated in some detail and key elements in the German and French consumer-insolvency systems are specifically considered, as these systems respectively illustrate the traditional and the new European approaches to providing debt relief to NINA debtors. Internationally regarded principles and guidelines are considered as a subtext. The purpose of the investigation is to ascertain whether there are any lessons to be learnt by South Africa from the European approach, and to indicate a way forward for future law reform as regards debt-relief measures for NINA debtors. The research concludes with an evaluation of the different approaches within the South African context and offers some remarks on the way forward.

## **INTRODUCTION**

Internationally, the traditional creditor-orientated objective of consumer insolvency,<sup>1</sup> namely to maximise returns for creditors, has increasingly had to make way for the modern fresh-start objective. The latter can be summarised as to offer debt relief and a consequential discharge of debt

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<sup>1</sup> The term 'consumer' insolvency, is a misnomer, as it makes no difference from the consumer debtor's perspective whether debts are private or commercial in nature; see INSOL International, 'Consumer Debt Report: Report of Findings and Recommendations' (2001 hereinafter INSOL) 3. In this respect the term 'natural person' insolvency is technically more correct. However, some reports and comparative systems refer to the term 'consumer', and therefore the terms 'natural person' and 'consumer' will be used interchangeably and as synonyms in this article.

to consumers who cannot reasonably repay their creditors.<sup>2</sup> The modern international trend is furthermore specifically to accommodate the so-called No-Income-No-Asset (NINA) group of debtors, which is formed by those who have neither income, nor assets available for distribution amongst creditors.<sup>3</sup>

The broader South African natural-person insolvency system is still heavily based on a creditor-orientated approach.<sup>4</sup> It further does not provide for a procedure that specifically aims to assist and accommodate the NINA debtor.<sup>5</sup> However, the South African Law Reform Commission has proposed that provision be made for a pre-liquidation composition, a procedure intended to cater for these debtors.<sup>6</sup> Unfortunately, as indicated below, this proposed measure is not really appropriate to NINA debtors' circumstances. In addition to the Law Reform Commission's proposal, the Trade and Industry Portfolio Committee has apparently set up a subcommittee to consider the possibility of introducing debt-relief measures aimed at South African households into either the National Credit Act<sup>7</sup> (hereinafter 'NCA') or a separate piece of legislation.<sup>8</sup> It remains to be seen what reform initiatives will result from the Committee's deliberations. At this juncture, however, South African NINA debtors are left destitute.

Accordingly, the aim of this article is to investigate the European approach regarding debt-relief procedures for NINA debtors, and to make proposals for a specific procedure for NINA debtors in South Africa.<sup>9</sup> The German and French consumer-insolvency systems are selected for this purpose as they respectively illustrate the traditional and the new European approaches to the provision of debt relief for NINA debtors. Although the objective of

<sup>2</sup> *ibid* 15, 22. cf Joseph Spooner, 'Fresh Start or Stalemate? European Consumer Insolvency Law Reform and the Politics of Household Debt' (2013) *European Review of Private Law* 747 at 762–763.

<sup>3</sup> The World Bank Insolvency and Creditor/Debtor Regimes Task Force Working Group, 'Report on the Treatment of the Insolvency of Natural Persons' (2011) (hereinafter 'World Bank') 97–98.

<sup>4</sup> cf Hermie Coetzee, 'Is the Unequal Treatment of Debtors in Natural Person Insolvency Law Justifiable?: A South African Exposition' (2016) *International Insolvency Review* 36 at 37.

<sup>5</sup> See in general Hermie Coetzee, 'Does the Proposed Pre-liquidation Composition Proffer a Solution to the No Income No Asset (NINA) Debtor's Quandary and If Not, What Would?' (2017) *THRHR* 1.

<sup>6</sup> See in general cl 118 of the 2015 Insolvency Bill, read together with the '2014 Explanatory Memorandum' 201 and 208 [on file with authors].

<sup>7</sup> 34 of 2005.

<sup>8</sup> Linda Ensor, 'MPs to Look at Tools for Debt Relief' *Business Day*, (9 November 2016) <<http://bit.ly/2fEz3yN>> accessed 14 November 2016.

<sup>9</sup> See with regard to the debt-relief procedures provided for NINA debtors in England and New Zealand, Melanie Roestoff and Hermie Coetzee, 'Consumer Debt Relief in South Africa: Lessons from America and England, and Suggestions for the Way Forward' (2012) *SA Merc LJ* 53; Coetzee and Roestoff, 'Consumer Debt Relief in South Africa – Should the Insolvency System Provide for NINA Debtors? Lessons from New Zealand' (2013) *International Insolvency Review* 188.

this article is to draw from the European approach, internationally regarded principles and guidelines are considered as a subtext.<sup>10</sup>

An important new trend in Europe, which forms one of the main focus areas of this article, is a break with the traditional European earned-discharge approach. In accordance with this development, an immediate discharge is granted to NINA debtors instead of subjecting them to a waiting period that is no more than symbolic.<sup>11</sup> The question arises as to whether South African lawmakers should adopt this approach. Secondly, we focus on certain key elements of the selected systems' NINA procedures, namely, access requirements,<sup>12</sup> and the question of whether a separate and specific procedure for NINA debtors should be created.<sup>13</sup> In this regard, the further question arises as to whether the debtor or an independent regulator or intermediary should decide on the type of proceedings to be implemented.<sup>14</sup> We also consider whether the courts' involvement should be restricted<sup>15</sup> and whether the process should rather be administrative in nature.<sup>16</sup> A final important aspect involves the granting of a moratorium on debt enforcement, and the question of the most appropriate stage in the debt-relief proceedings when it should become operative.<sup>17</sup>

In order to achieve our stated objectives of this research, the discussion commences with a description of the current legal position of NINA debtors

<sup>10</sup> These principles and guidelines are derived from the INSOL (n 1) and World Bank (n 3) reports respectively.

<sup>11</sup> See Jason Kilborn, 'Continuity, Change, and Innovation in Emerging Consumer Bankruptcy Systems: Belgium and Luxembourg' (2006) American Bankruptcy Institute LR 69 at 88, 93 and 106, where the author discusses some systems that subscribe to symbolic waiting periods.

<sup>12</sup> There seems to be international consensus that all honest, but unfortunate debtors should have access to debt relief; World Bank (n 3) 63–67; and Spooner (n 2) 11, 14 and 16. It is specifically preferred that the same relief should be provided to all debtors notwithstanding their financial means; World Bank (n 3) 97.

<sup>13</sup> See World Bank (n 3) 98 and 136. The World Bank refers to various manners in which NINA debtors are accommodated in diverging jurisdictions. However, it becomes apparent from the discussion that this group of debtors is *sui generis* and that their needs necessitate a tailor-made option.

<sup>14</sup> INSOL International is in favour of the debtor choosing between different procedures ((n 1) 16 and 19. However, it seems that the World Bank supports public-agency decision-making provided that measures are in place to ensure consistent treatment and to enable challenges to decisions (n 3) 67–68 and 132.

<sup>15</sup> International principles and guidelines suggest that courts will, due to various reasons, always have a role to play in insolvency procedures. However, international reports appear to favour reduced court involvement; see World Bank (n 3) 49–56 and INSOL (n 1) 25–27.

<sup>16</sup> Pressure on public funding of the court system; the limited capability of lower-ranked courts to address socio-economic issues relating to debt; and varying decision-making by presiding officers create pressure for administrative processing for especially the large number of NINA debtors; see World Bank (n 3) 55 et seq.

<sup>17</sup> International principles and guidelines call for a moratorium on debt-enforcement measures whilst insolvency procedures are in force; INSOL (n 1) 14 and 17; World Bank (n 3) 14 and 52.

in South Africa. Thereafter, we discuss the general European approach to debt relief by comparing it to the American approach. This is followed by a discussion of the German system, which serves as an example of the so-called traditional European approach, after which we present the French system as an example of the so-called 'new' European approach to consumer-debt relief. International principles and guidelines are considered throughout our discussion. Next, the different approaches are evaluated and proposals for possible law reform in South Africa are offered. Finally, we offer some concluding remarks.

### THE CURRENT POSITION OF NINA DEBTORS IN SOUTH AFRICA

South African insolvents have (theoretically) three statutory debt-relief measures at their disposal:<sup>18</sup> sequestration;<sup>19</sup> debt review;<sup>20</sup> and administration-order<sup>21</sup> procedures. However, none of these procedures is suited to NINA debtors' needs.<sup>22</sup> Furthermore, their direct and indirect access requirements are of such a nature that NINA debtors are all but expressly excluded from using any one of them, in that all existing measures, in one way or another, demand assets or disposable income (available for distribution) as direct or indirect requirements for access.<sup>23</sup>

The sequestration procedure, which is in essence an asset-liquidation procedure, is regarded as South Africa's principal debt-relief measure, as it is the only procedure which leads to a discharge of debt.<sup>24</sup> However, as debt relief is not the aim of the procedure, the discharge is largely coincidental.<sup>25</sup> In fact, the procedure unapologetically and, in contrast to international trends,<sup>26</sup> explicitly favours benefit to creditors over benefit to debtors. This is clear that sufficient assets are set as access requirements, not only to cover sequestration costs, but also to ensure an advantage for creditors.<sup>27</sup> Regarding the latter, courts have accepted that a pecuniary advantage is

<sup>18</sup> See Lienne Steyn, 'Statutory Regulation of Forced Sale of the Home in South Africa' (LLD thesis, University of Pretoria 2012) 349 et seq, for a comprehensive explanation and consideration of the statutory measures

<sup>19</sup> Stemming from the Insolvency Act 24 of 1936.

<sup>20</sup> See s 86 of the (NCA).

<sup>21</sup> See s 74 of the Magistrates' Courts Act 32 of 1944 (MCA).

<sup>22</sup> See Coetzee (n 4) 37–38; Coetzee and Roestoff (n 9) 200.

<sup>23</sup> See Coetzee (n 4) 38.

<sup>24</sup> S 129 of the Insolvency Act, read together with Coetzee and Roestoff (n 9) 193.

<sup>25</sup> See in general *Ex parte Ford* [2009] 3 World Bank SA 376 (WCC) 383; *Ex parte Shmukler-Tshiko* [2013] JOL 29999 (GSJ).

<sup>26</sup> See World Bank (n 3) 126–127.

<sup>27</sup> See ss 6, 10 and 12.

required.<sup>28</sup> This entry condition obviously excludes NINA debtors from using the procedure, as they, by definition, do not own valuable or, at the very least, realisable assets.<sup>29</sup> Another feature that curtails access and renders the procedure especially unsuited to NINA debtors' needs, is that of cost.<sup>30</sup> Two factors can generally be attributed to the high costs involved: as a sequestration order affects a person's status, the high courts are involved;<sup>31</sup> and as the procedure was designed to deal with substantial estates, it is cumbersome and involved. Further, relating to the sequestration procedure's most attractive feature – the discharge that it provides as a tailpiece – this automatically occurs after a substantial period of ten years,<sup>32</sup> although the debtor may apply to court for his or her rehabilitation at an earlier stage.<sup>33</sup> In the latter respect, insolvents generally apply for their rehabilitation and consequent discharge after a period of four years.<sup>34</sup>

As we have indicated, the two secondary (as neither leads to a discharge of debt)<sup>35</sup> statutory debt-relief measures are debt-review and administration-order procedures. These are both repayment-plan procedures and, as is the case with sequestration, are heavily reliant on the courts<sup>36</sup> – although the magistrates' courts as opposed to the high courts are involved. The procedures both prescribe a myriad of access requirements (although these are not identical), which exclude many debtors from their ambits. However, most relevant to the present discussion is that the very nature of these procedures – that is repayment plans – exclude NINA debtors from

<sup>28</sup> See *Trust Wholesalers and Woolens (Pty) Ltd v Macan* [1954] 2 SA 109 (N) 111; *BP Southern African (Pty) Ltd v Furstenburg* [1966] 1 SA 717 (O) 720; and *Fesi v ABSA Bank Ltd* [2000] 1 SA 499 (C) 504. In *Nieuwenhuizen v Nedcor Bank Ltd* [2002] 2 All SA (O) 367, ten cents in the rand were accepted as a point of departure in the determination of whether the advantage for creditors' requirement was met. See in turn, *Ex parte Ogunlaja* [2011] JOL 27029 (GNP) para 9, where the court found, with reference to the practice rule in the North-Gauteng High Court, Pretoria that at least twenty cents in the rand were required to show advantage for creditors. However, more recently and most importantly the Constitutional Court, in *Stratford v Investec Bank* [2015] 3 SA 1 (CC) 19–20, with reference to *Meskin and Co v Friedman* [1948] (2) SA 555 (W) 559, decided that 'advantage to creditors' should be interpreted as a 'reasonable prospect' that some pecuniary benefit will result. However, the Court decided that the concept is 'broad and should not be rigidified'. The Court specifically determined that specifying cents in the rand or 'non-negligible' is unhelpful and that the courts should rather exercise their independent discretion.

<sup>29</sup> See in general (n 12).

<sup>30</sup> *ibid.*

<sup>31</sup> The involvement of the courts as a matter of course is inconsistent with the international trend of reducing court involvement and of a move towards an administrative approach; see (n 14) and (n 16).

<sup>32</sup> See s 127A of the Insolvency Act.

<sup>33</sup> See s 124 in general.

<sup>34</sup> See s 124(2).

<sup>35</sup> The lack of a discharge is in contravention of international principles and guidelines; see (n 2).

<sup>36</sup> See (n 15) and (n 16) regarding the preferred trends of reduced court involvement and administrative processing.

their range in that they have no disposable income available for distribution under a repayment plan.<sup>37</sup>

It follows that NINA debtors are systemically excluded from the system as a whole,<sup>38</sup> as the broader system, perhaps unintentionally, distinguishes between debtors 'with' and debtors 'without' assets and income.<sup>39</sup> In this regard it has been argued elsewhere<sup>40</sup> that such differentiation amounts to unjustifiable, unfair discrimination on the basis of NINA debtors' socio-economic status. This, in turn, means that such discrimination conflicts with the Constitution of the Republic of South Africa 1996<sup>41</sup> and, more specifically, with the right to equality.<sup>42</sup> Nonetheless, as we have shown, neither of the existing procedures is in any event suited to NINA debtors' unique circumstances.<sup>43</sup>

The untenable situation of NINA debtors may perhaps, in part, be attributed to the fact that the broader natural-person insolvency system is largely incoherent as a result of its haphazard development.<sup>44</sup> Consequently, government has never considered the debt-relief system holistically, and has, therefore, not reflected on the systemic marginalisation of NINA debtors. The absence of clear policy directives as regards the *broader* system can also be attributed to the lack of a holistic review, and is further exacerbated by the multiplicity of government departments, pieces of legislation and intermediaries involved. This, too, is a direct result of disorganised development.<sup>45</sup> However, it appears that government is aware of the difficulty facing NINA debtors as relevant reform initiatives in the form of the proposed pre-liquidation composition<sup>46</sup> are under consideration.

The proposed pre-liquidation composition procedure is contained in clause 118 of the 2015 Insolvency Bill. The objectives of the proposed procedure can be deduced from the 2014 Explanatory Memorandum, where the following is stated:

Because of the requirement that liquidation<sup>47</sup> of the estate of a natural person debtor must be to the advantage of creditors ... liquidation is not available if the unencumbered assets are insufficient to warrant liquidation. Provision

<sup>37</sup> Coetzee (n 5) 4.

<sup>38</sup> In contrast, international principles and guidelines push toward access to all honest, but unfortunate debtors; see (n 12).

<sup>39</sup> *ibid.*

<sup>40</sup> Coetzee (n 4) 54.

<sup>41</sup> Hereinafter the 'Constitution'.

<sup>42</sup> See s 9 of the Constitution, read together with Coetzee (n 4).

<sup>43</sup> Such circumstances require unique considerations. See (n 13).

<sup>44</sup> Roestoff and Coetzee (n 9) 75.

<sup>45</sup> *ibid.*

<sup>46</sup> See in general cl 118 of the 2015 Insolvency Bill.

<sup>47</sup> The Insolvency Bill uses the term 'liquidation' when referring to both the liquidation of juristic persons and the sequestration of natural persons.

must be made for debtors with little or *no assets*<sup>48</sup> who through no fault of their own are unable to pay their debts.<sup>49</sup>

and

Consideration must be given to afford debtors other than companies or close corporations who do not qualify for liquidation an opportunity for a fresh start which entails a discharge of debts. This is in line with international developments in insolvency law.<sup>50</sup>

It is thus clear that the Commission is aware of NINA debtors' plight and has focused on, amongst others, addressing the problem by means of the clause 118 procedure.<sup>51</sup> Nevertheless, it has been argued that the measure will not, for reasons we set out below, achieve its objectives.<sup>52</sup>

In brief, the proposed measure entails a two-pronged procedure. The first part is a negotiation phase, and the second is a forced discharge by the Master should negotiations fail.

As regards the first part of the procedure, it is envisaged that a debtor with total outstanding debts of under R200 000, and who cannot pay his or her debts, initiates the procedure by lodging a signed copy of the composition together with a sworn statement, with an administrator.<sup>53</sup> It follows that administrators will oversee the proposed procedure<sup>54</sup> and their initial task will be to determine a date for questioning the debtor and for considering the composition.<sup>55</sup> This takes place at a hearing at a location accessible and convenient to creditors.<sup>56</sup> Between the determination of a date for the hearing and its conclusion, creditors are prohibited – save with the permission of a court – from instituting legal action against, or applying

<sup>48</sup> Emphasis added.

<sup>49</sup> See '2014 Explanatory Memorandum' (n 6) 201.

<sup>50</sup> *ibid* 208. See (n 12) in relation to access and (n 2) as regards the discharge.

<sup>51</sup> The fact that the Commission proposes a specific procedure for no-asset estates, tally with international trends; see (n 3) and (n 13).

<sup>52</sup> See in general Coetzee (n 5).

<sup>53</sup> CI 118(1). There was no monetary threshold in the 2000 Insolvency Bill. It is not clear why the threshold was included, especially since the credit industry is now accustomed to unlimited amounts of debt being restructured by means of the debt-review procedure. Further, as the courts are not involved, jurisdictional issues could not be the reason. Clearly, the proposed monetary threshold will result in the exclusion of some NINA debtors, which would, once again, leave them destitute due to the lack of suited alternatives; regarding the latter, see (n 12).

<sup>54</sup> This proposal is in line with the internationally preferred approach of reduced court involvement through the migration towards dispensations that are administrative in nature; see (n 15) and (n 16).

<sup>55</sup> CI 118(6).

<sup>56</sup> CI 118(7)(a).

for the liquidation of, the debtor's estate.<sup>57</sup> The administrator presides over the hearing,<sup>58</sup> where claims will be proven and where the debtor may be interrogated by the administrator, creditors and other interested parties on matters relating, in the main, to his or her financial position.<sup>59</sup> Where the majority in number and two-thirds in value of concurrent creditors who vote on the composition, accept the proposal, the administrator must certify the composition and send it to the Master and the creditors. It will then be binding on all creditors who have received notice of, or who appeared at, the hearing.<sup>60</sup> Secured and preferential creditors' claims or rights will only be subject to the composition if the creditors have consented thereto in writing.<sup>61</sup> A debtor who, on reasonable grounds, is not able to comply with the composition may, with the administrator's authorisation, lodge an amended composition.<sup>62</sup>

The second part of the procedure is of special importance to NINA debtors. This part comes into play where the required majority creditors' vote cannot be obtained, and where the debtor cannot pay substantially more than that which was offered. Under these circumstances the (latest) proposal, which is contained in subclause 22, sets out that

- (a) the administrator must declare that the proceedings in terms of this clause have ceased and that the debtor is once again in the position he or she was prior to the commencement thereof and lodge a copy of the declaration with the Master and known creditors by standard notice; and
- (b) the Master<sup>63</sup> may upon application by the debtor grant a discharge<sup>64</sup> of debts of the debtor other than secured or preferred debts if –
  - (i) the debtor satisfies the Master that the administrator and all known creditors were given standard notice of the application for the discharge with a copy of the debtor's application at least 28 days before the application to the Master; and

<sup>57</sup> Cl 118(23). A moratorium on debt enforcement is in line with international guidelines, although it should become operative once a debtor applies for the procedure. See INSOL (n 1) 16–17; (n 17).

<sup>58</sup> This feature is in line with international principles and guidelines; see (n 16).

<sup>59</sup> Cl 118(10)(e).

<sup>60</sup> Cl 118(1), read together with cl 118(17).

<sup>61</sup> Cl 118(17) This feature is in line with international principles and guidelines. See World Bank (n 3) 105–107 and 137–138.

<sup>62</sup> Cl 118(19)(b)(ii). Provision for plan modification is in line with international principles and guidelines. See World Bank (n 3) 83–84 and 134–135.

<sup>63</sup> The Master was decided upon as a court application would be too costly. A decision by the Master is subject to review. See '2014 Explanatory Memorandum' (n 6) 209. This proposed feature is in line with international principles and guidelines, as regard reduced court involvement and administrative processing (see (n 15) and (n 16)).

<sup>64</sup> The proposed discharge feature accords with international principles and guidelines. See (n 2).



- (ii) the Master is satisfied after consideration of the comments, if any, by creditors and the administrator and the application by the debtor –
  - (aa) that the proposed composition was the best offer which the debtor could make to creditors;
  - (bb) that the inability of the debtor to pay debts in full was not caused by criminal or inappropriate behaviour by the debtor;
  - (cc) that the debtor does not qualify to apply for an administration order in terms of section 74 of the Magistrates' Courts Act 32 of 1944.<sup>65</sup>

Although the proposed pre-liquidation composition procedure mostly strikes the right notes when measured against international principles and guidelines, the primary question is whether, if implemented, it could provide a solution to the plight of NINA debtors'. Unfortunately, as has been argued elsewhere, although the initiative is commendable in many respects and signifies a paradigm shift from the South African natural-person insolvency system's 'obsession with the advantage for creditors', it will not achieve its commendable objective of providing relief in no-asset circumstances.<sup>66</sup> This is because the implementation of the procedure would only assist those who already have some form of statutory recourse available. The basic reason for this inference is that only those with negotiating power – that is, income and or assets – will be able to succeed in the compulsory negotiation phase of the procedure. Furthermore, the post-negotiation phase, in which the Master is empowered to discharge debt where negotiations have failed, will only be available to NINA debtors once they have advanced through the pointless negotiation phase of the procedure.<sup>67</sup> The procedure also involves costs, which are clearly wasteful in NINA cases where the first part of the procedure is doomed from the outset. Notwithstanding waste, it has been pointed out that NINA debtors can, in any event, not pay for such (unnecessary) expenses.<sup>68</sup> In this light, it is in the interests of the South African legislature to investigate jurisdictions, that have successfully addressed the plight of NINA debtors in one way or the other, in order to gain some insight into the mechanisms they have employed with a measure of success.

## **EUROPEAN APPROACH TO DEBT RELIEF**

### **The American versus the European Approach**

The traditional European approach to consumer debt relief entails a so-called earned-new-start or earned-discharge approach, in terms of which a

<sup>65</sup> It is odd that the debt-review procedure in terms of the NCA is not mentioned.

<sup>66</sup> Coetzee (n 5) 9.

<sup>67</sup> *ibid* 9–10.

<sup>68</sup> *ibid* 10.

debtor's best efforts<sup>69</sup> to pay off at least a part of his or her debt in terms of a repayment plan, will, on conclusion of the plan, reward him or her with a discharge of the remaining debts.<sup>70</sup> In contrast, the American so-called straight-discharge approach provides a debtor with an opportunity to make a fresh-start.<sup>71</sup> This approach has its origins in Chapter 7 of the Bankruptcy Code,<sup>72</sup> which, in exchange for a surrender of all non-exempt assets, immediately and automatically discharges the consumer debtor from all pre-insolvency debt.<sup>73</sup> In addition to the Chapter 7 relief, Chapter 13 of the American Code provides for an alternative relief measure that grants the debtor a discharge of all pre-insolvency debt after completion of a repayment plan extending over a period of three to five years. Previously, consumer debtors automatically qualified for a Chapter 7 straight-discharge, as they had a free choice between the different measures. However, after the introduction of the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCA) in 2005,<sup>74</sup> certain debtors are now also required to earn their discharge by making payments in terms of a Chapter 13 repayment plan. This is because the BAPCA introduced a means test, in terms of which debtors are channelled to the Chapter 13 procedure when their income exceeds a prescribed median.<sup>75</sup> Although the American system does not provide a specific procedure for NINA debtors, they will obviously qualify for Chapter 7 bankruptcy, and thus an immediate discharge, as they have no available income. Chapter 13 further provides for a so-called hardship-

<sup>69</sup> The so-called best-effort principle; Nick Huls, 'Towards a European Approach to Overindebtedness of Consumers' (1993) *J of Consumer Policy* 215 at 221.

<sup>70</sup> See in general Udo Reifner, et al *Consumer Overindebtedness and Consumer Law in the European Union* (Institute for Financial Services e.V., Erasmus University Rotterdam, School of Law, University of Helsinki, Helsinki Collegium for Advanced Studies 2003) 166; Jason Kilborn, 'The Innovative German Approach to Consumer Debt Relief: Revolutionary Changes in German Law, and Surprising Lessons for the United States' (2004) *Northwestern J of International Law and Business* 257 at 281; Johanna Niemi-Kiesiläinen, 'Changing Directions in Consumer Bankruptcy Law and Practice in Europe and the USA' (1997) *J of Consumer Policy* 133 at 135; Huls (n 69) 215.

<sup>71</sup> *Local Loan Co v Hunt* 292 US 234 (1934) at 244. The fresh-start principle is fundamental to the American insolvency system. The American approach to debt relief is, from a debtor's perspective, regarded to be the most generous in the world; Katherine Porter and Deborah Thorne, 'The Failure of Bankruptcy's Fresh Start' (2006) *Cornell LR* 67 at 79; Jason Kilborn, 'La Responsabilisation de l'économie: What the United States can Learn From the New French Law on Consumer Overindebtedness' (2005) *Michigan J of International Law* 619 at 632.

<sup>72</sup> In the USA, insolvency is regulated by federal legislation, namely the Bankruptcy Reform Act of 1978, generally known as the Bankruptcy Code or Code. This Act appears as Title 11 of the United States Code. See in general in respect of the American consumer-insolvency system, Jeffrey Ferriell and Edward Janger, *Understanding Bankruptcy* (LexisNexis 2013).

<sup>73</sup> Jason Kilborn, 'Inaugural Lecture' (2010) <<http://bit.ly/1BoDJAP>> accessed 2 December 2016 at 32.

<sup>74</sup> Pub L 109-8, 119 Stat 23.

<sup>75</sup> S 707(b)(2) of the Code.

discharge for those debtors who are unable to complete the payments in terms of their repayment plan.<sup>76</sup>

As mentioned above, a new trend regarding the treatment of NINA debtors, namely to move away from the traditional earned-discharge approach and to provide an immediate discharge – similar to the American straight-discharge approach – has recently emerged in Europe. In what follows, the German system – a good example of the traditional approach – is compared to the French so-called new approach to debt relief.

### **The Traditional European Approach – Germany**

In 1999, new insolvency legislation – the *Insolvenzordnung* (hereinafter InsO) – was introduced in Germany.<sup>77</sup> With this legislation, lawmakers for the first time acknowledged the fresh-start principle by providing insolvent<sup>78</sup> consumers relief in the form of a discharge of residual debt, the so-called *Rechtschuldbefreiung*.<sup>79</sup>

As mentioned, the German consumer insolvency system provides a good example of the traditional European earned-discharge approach and its so-called best-effort principle. In addition, the German system requires that the debtor must show ‘good conduct’ during the period of repayment.<sup>80</sup> Under German legislation, a debtor must first attempt to reach an out-of-court agreement with his or her creditors.<sup>81</sup> In this negotiation phase of the proceedings, the debtor is normally assisted by one of the many state-subsidised debt-counselling centres (*Schuldnerberatungsstelle*) spread throughout Germany.<sup>82</sup> However, due to poor financial support from the

<sup>76</sup> See s 1328(a) and (b) of the Code.

<sup>77</sup> 1994 BGBl I S. 2866. See in general in respect of the German insolvency legislation, Christoph Paulus, ‘The New German Insolvency Code’ (1998) *Texas International LJ* 141.

<sup>78</sup> The opening of insolvency proceedings requires the existence of a reason for doing so. Insolvency is the general reason for opening such proceedings. The debtor is insolvent if he or she is unable to meet his or her mature obligations to pay. Insolvency will be presumed as a rule if the debtor has stopped payment. Imminent insolvency will also qualify as a reason to open insolvency proceedings. The debtor will be deemed to be faced with imminent insolvency if he or she is likely to be unable to meet his or her existing debt obligations on the date of their maturity; see ss 16–19 InsO. However, no minimum or maximum amount is prescribed in respect of the amount of the outstanding debt; Hortense Trendelenburg, ‘Discharge in Germany from an International Point of View’ (2000) *International Insolvency Review* 111 at 115.

<sup>79</sup> Ss 286–303 InsO; see Trendelenburg (n 78) 113 et seq. Before 1999, German insolvency legislation (the *Konkursordnung* of 1877) did not provide for any discharge and the principle of a lifelong liability for debt was applicable to German debtors. For a discussion of the legal position before the introduction of the InsO, see Kilborn (n 70) 260 et seq; Paulus (n 77) 141 et seq.

<sup>80</sup> Jan van Appeldoorn, ‘The “Fresh Start” for Individual Debtors: Social, Moral and Practical Issues’ (2008) *International Insolvency Review* 57 at 65; Susanne Braun, ‘German Insolvency Act: Special Provisions of Consumer Insolvency Proceedings and the Discharge of Residual Debts’ (2005) *German LJ* 59 at 68.

<sup>81</sup> S 305(1) InsO.

<sup>82</sup> Kilborn (n 70) 273; Huls (n 69) 216.

*Länder*,<sup>83</sup> these centres have, in the past generally been unable to provide sufficient personnel to assist debtors in accessing the insolvency-relief process. Consequently, long waiting periods for assistance contributed to the lack of cases.<sup>84</sup>

If an out-of-court agreement cannot be reached, the court may attempt to secure an agreement between the parties.<sup>85</sup> However, in practice, courts apparently prefer not to implement an in-court negotiation process.<sup>86</sup> If the in-court negotiation phase is not implemented, a simplified liquidation procedure will be followed, in terms of which the court appoints a trustee who realises the non-exempt assets of the insolvent estate and divides the proceeds between the creditors.<sup>87</sup>

Previously an application could be refused, and a discharge thus prevented, if the debtor's assets were insufficient to cover court costs. However, amendments introduced in 2001 now provide for a reduction in costs and allow debtors to defer payment of court costs, meaning that the debtor can settle these on completion of the insolvency proceedings.<sup>88</sup>

After the liquidation process has been completed, the so-called period of good conduct (*Wohlverhaltensperiode*) follows, in terms of which the debtor formally surrenders all non-exempt income to a trustee,<sup>89</sup> who must make annual payments to creditors.<sup>90</sup> During this period, there is a moratorium on debt enforcement.<sup>91</sup> The court cannot order a stay of enforcement to protect the negotiations in the out-of-court negotiation phase. The moratorium can, therefore, only be effected once the formal court proceedings have started.<sup>92</sup> The stay also affects wage garnishment, which becomes invalid.<sup>93</sup>

<sup>83</sup> The individual German states.

<sup>84</sup> Kilborn (n 70) 274; Trendelenburg (n 78) 114.

<sup>85</sup> Ss 307(1), 308 and 309.

<sup>86</sup> Kilborn (n 70) 277. Recent amendments to the Act allows the court a discretion as to whether the in-court negotiation process should be followed (s 306(1)). For NINA debtors, this in-court negotiation phase of the process will probably not be sensible as the NINA debtor does not have any income or assets that would place him or her in a position to effectively negotiate with his or her creditors. See also the discussion of the proposed pre-liquidation composition of the South African Law Reform Commission and our critique above, namely that it would not be a sensible process for NINA debtors.

<sup>87</sup> Ss 311–314. It seems that German courts form an integral part of the consumer-insolvency system. This is in contravention with international principles and guidelines, which prefer reduced court involvement (see (n 15)).

<sup>88</sup> See s 4a and 4b; Kilborn (n 70) 278–279; Dejan Bodul and Ivana Žiković, 'Advantages and Disadvantages of German Consumer Bankruptcy Model: Guidelines for Croatian Lawmaker' (2014) *Ekonomski Vjesnik / Econviews* 393 at 395.

<sup>89</sup> S 287(2).

<sup>90</sup> S 292(1). Kilborn (n 70) 279.

<sup>91</sup> S 294(1); and see Van Appeldoorn (n 80) 62.

<sup>92</sup> S 89(1). Although a moratorium on debt enforcement is in line with international guidelines, it should become operative once a debtor applies for the procedure. The delay in the moratorium becoming effective, as was mentioned within the context of the proposed South African pre-liquidation composition, is not optimal. See *INSOL* (n 1) 16–17; (n 17).

<sup>93</sup> See s 89(2); Reifner (n 70) 180.

After expiry of a six-year period,<sup>94</sup> the court will discharge most of the remaining debt, provided the debtor has shown 'good conduct' and complied with the conditions and requirements of the repayment plan.<sup>95</sup> A discharge may be refused if the debtor made him- or herself guilty of an insolvency offence, misconduct, or fraudulent conduct in terms of the Act, or if he or she has obtained a discharge within the ten years preceding the application.<sup>96</sup> In order to encourage debtors to maintain good conduct, the German legislator has established several periodic incentives.<sup>97</sup> At the end of the fourth year, an amount representing 10 per cent of any non-exempt income that was collected, is paid back to the debtor. In the fifth year, this repayment increases to 15 per cent.<sup>98</sup> The final incentive is the discharge, which will be provided by the end of the sixth year.<sup>99</sup>

A further innovation in the German legislation is the requirement that debtors should do their best to find and keep any 'reasonable'<sup>100</sup> employment.<sup>101</sup> Should the debtor not comply with this requirement, a creditors will be entitled to apply for a denial of discharge.<sup>102</sup> However, as regards NINA debtors, it is important to note that a discharge is not excluded in cases where the debtor, in spite of his best efforts, cannot find or keep employment.<sup>103</sup> The courts are furthermore willing to accept zero plans, as long as they represent the debtor's so-called best-efforts. NINA debtors are, therefore, not denied the opportunity of obtaining a fresh

<sup>94</sup> S 287(2). A period of six years seems exorbitant, as a period of between three and four years are generally preferred. In this respect, see Hermie Coetzee, 'A Comparative Reappraisal of Debt Relief Measures for Natural Person Debtors in South Africa' (LLD thesis, University of Pretoria 2015) 96 and the authorities cited there. See also Melanie Roestoff, 'Rehabilitasie in die Suid-Afrikaanse Verbruikersinsolvensiereg: Internasionale Tendense en Riglyne' (2016) LitNet 594 at 621.

<sup>95</sup> S 300. See Kilborn (n 70) 279–280.

<sup>96</sup> S 290; cf Braun (n 80) 67 et seq.

<sup>97</sup> Assaf Lichtash, 'Realigning the American Consumer Bankruptcy System with the Goals of the Fresh-start Doctrine: A Global Comparative Analysis' (2011) *Loyola of Los Angeles International and Comparative LR* 169 at 184.

<sup>98</sup> S 292(1).

<sup>99</sup> S 300. Certain debts are excluded from the discharge (see s 302). However, German law excepts fewer debts from a discharge than US law. Thus, although German law demands more from the debtor, it provides for a broader discharge; see Kilborn (n 70) 280 n 135; Trendelenburg (n 78) 119.

<sup>100</sup> The debtor must, for example, be willing to accept work outside the scope of his or her profession and even temporary work. Kilborn (n 70) 280; Trendelenburg (n 78) 117.

<sup>101</sup> S 295(1)1.

<sup>102</sup> S 296.

<sup>103</sup> Kilborn (n 70) 280.

start.<sup>104</sup> In fact, most of the insolvency cases in Germany are NINA cases<sup>105</sup> and distributions to creditors, either from the debtors' assets or non-exempt income, are therefore rarely seen.<sup>106</sup>

### The New European Approach – France

In December 1989 legislation dealing with the problems of over-indebted consumers was introduced in France. This legislation, commonly referred to as the *Loi Neieritz*,<sup>107</sup> added several provisions to the French Consumer Code (*Code de la Consommation*), which provided for a debt-relief measure in terms of which the debtor's debt obligations could be rescheduled into a repayment agreement with creditors.<sup>108</sup>

The French procedure is not court-orientated, but is overseen by administrative bodies, called *commissions de surendettement des particuliers* (commissions on individual over-indebtedness).<sup>109</sup> These commissions are not part of the judiciary, and their activities are not supervised by any judicial agency.<sup>110</sup> In order to obtain access to the French debt-relief procedure, a consumer debtor must apply to one of these commissions.<sup>111</sup> The commissions' first task is to ascertain whether the access requirements,

<sup>104</sup> *ibid* 292; Braun (n 80) 63. The fact that the system accommodates NINA debtors by allowing them access to the system and by making provision for a discharge in such circumstances, are in line with international principles and guidelines; see (n 2) and (n 12) respectively.

<sup>105</sup> It is interesting that the system does not provide for a separate and specific procedure (see (n 13)), although one can argue that the system is designed for such cases, as the majority of debtors can be characterised as NINA debtors.

<sup>106</sup> Kilborn (n 70) 286; See Götz Lechner in Hans Micklitz (ed), *Consumer Bankruptcy in Europe: Different Paths for Debtors and Creditors* (European University Institute 2011) 59–80 regarding the different categories of German consumer insolvents. Wage exemptions also protect most of the debtors' income; see Kilborn (n 70) 291.

<sup>107</sup> Act no 89-1010 of 31 December 1989. See in general Kilborn (n 71) for a detailed discussion of the legal developments regarding consumer over-indebtedness in France.

<sup>108</sup> The French Consumer Code has recently been amended in October 2016. The current provisions pertaining to the treatment of consumer over-indebtedness are contained in Book VII, Title I–IV of the *Code de la Consommation*, (hereinafter *C Consumm*).

<sup>109</sup> Art L712-1–L712-9 *C Consumm*. A commission is established for each department in France – art L712-4. France is divided into thirteen administrative regions. Each region is divided into 'departments' (counties). There is a total of ninety-six departments – see 'General Information and Facts About France' <<[www.france-pub.com/efrance.htm](http://www.france-pub.com/efrance.htm)> accessed 16 November 2016.

<sup>110</sup> Kilborn (n 71) 637. Reduced court involvement and specialised administrative processing are in line with international principles and guidelines. See (n 15) and (n 16) respectively.

<sup>111</sup> Art L712-2.

namely ‘good faith’<sup>112</sup> and ‘over-indebtedness’,<sup>113</sup> have been complied with.<sup>114</sup> At present each commission consists of seven members, including a representative of the French Central Bank, the Banque de France,<sup>115</sup> who acts as secretary and whose main function is to negotiate the repayment plan between the debtor and his or her creditors.<sup>116</sup>

French legislation does not provide for an immediate automatic stay of enforcement actions once an application has been brought by the debtor. However, once the debtor’s application has been filed, he or she may apply to the commission to refer his or her request to the District Court for a suspension of debt-enforcement procedures.<sup>117</sup> Furthermore, as soon as the commission has accepted the application by the debtor, all enforcement proceedings in respect of the debtor’s assets, as well as transfers of remuneration agreed to by him or her, are suspended and prohibited until the commission has made a decision on the appropriate debt-relief measures to be implemented. However, the duration of the moratorium may not exceed two years.<sup>118</sup> The debtor may also apply to the commission to refer his or her request to the District Court to suspend any eviction procedure to which he or she is subject.<sup>119</sup> This moratorium is effective until the commission makes a decision on the appropriate debt-relief measures to be implemented, but may not exceed the maximum period of two years.<sup>120</sup>

After the commission has decided that the debtor’s application is eligible, it will take control of the case and direct it along one of three possible

<sup>112</sup> Art L711-1. Good faith is assumed, but may be called into question if it appears that the debtor has deliberately become over-indebted or that he is concealing assets or information from the commission – see Banque de France, ‘Dealing with Household Overindebtedness’ (September 2012 <<http://bit.ly/2gSEld8>> accessed 19 November 2016 at 5.

<sup>113</sup> ‘Over-indebtedness’ is defined as the manifest impossibility for the debtor to pay the totality of his or her non-professional debt that are claimable now or in future – see art L711-1. The mere fact that the debtor’s primary residence has an estimated value, which is equal or greater than the amount of all non-professional debts, does not exclude the debtor from the debt-relief measures provided for by the Act – see art L711-1.

<sup>114</sup> See art L711-1 and L712-1; Kilborn (n 71) 636 n 115.

<sup>115</sup> The other members are the commission’s chairman, the departmental head of the Directorate-General of Public Finances, a representative of the credit industry, a representative of consumer organisations, a person with three years’ experience in social work and a person with a qualification and three years’ experience in the legal field; see Departmental Over-indebtedness Commission, ‘Composition’, *Droit-finances.net* <<http://bit.ly/2gjGvBT>> accessed 12 November 2016.

<sup>116</sup> Kilborn (n 71) 639.

<sup>117</sup> Art L721-4. In the case of immovable property where a forced sale has already been ordered, the auction date can only be postponed in terms of an order by the court responsible for the attachment of the property – art L721-7 and L722-4. The lack of an automatic moratorium on debt enforcement once a debtor applies for a debt-relief measure, contravenes international principles and guidelines; see (n 17).

<sup>118</sup> Art L722-2 and L722-3.

<sup>119</sup> Art L722-6.

<sup>120</sup> Art L722-9.

tracks.<sup>121</sup> The first track, or level of debt relief,<sup>122</sup> which involves an out-of-court negotiated payment plan<sup>123</sup> with so-called ordinary measures,<sup>124</sup> was initially the only option available for debt relief and a court could not grant a discharge of debt.<sup>125</sup> Moreover, some courts initially dismissed cases involving debtors who did not have adequate resources to form the basis of a feasible payment plan. However, in 1993 the French High Court rejected this approach and required courts to deal with these ‘terminal’ cases ‘as best they could’.<sup>126</sup> Therefore, a lack of resources is no longer a proper basis for the dismissal of a plan in France.<sup>127</sup>

In 1998, the French legislator introduced the second level of debt relief, which, amongst other things, provides for a discharge of unpaid debt. If negotiations fail, the commissions may impose or recommend to the court so-called extraordinary measures, which are more effective than the so-called ordinary measures of debt rescheduling and interest-rate reductions.<sup>128</sup> At present, the commissions may impose some or all of the measures provided for in article L733-1 of the French Code. These measures include: debt rescheduling or postponement of repayment; the reduction of interest rates; the application of payments primarily to capital; and the granting of a two-year moratorium<sup>129</sup> on debt enforcement.<sup>130</sup> Where a moratorium has been granted, the commission is obliged to re-evaluate the debtor’s financial situation on conclusion of the two-year period. Depending on the outcome of this re-evaluation, the commission may impose or recommend to the court any or all of the measures provided for in articles L733-1, L733-7

<sup>121</sup> Arts L712-2 and L724-1; Spooner (n 2) 752. The World Bank is in favour of public-agency decision-making as regards the most suited measure; see (n 14).

<sup>122</sup> Kilborn (n 71) 632.

<sup>123</sup> Art L732-1. Payment plans’ total length, including the period for which it may have been subject to revision or renewal, may currently not exceed seven years. However, loans relating to the purchase of the debtor’s principal residence may be rescheduled over a longer period (art L732-3 and L733-3).

<sup>124</sup> ‘Ordinary measures’ involve limited concessions and modifications to the debtor’s debt, such as debt rescheduling and interest-rate deductions; Spooner (n 2) 753. See art L732-2 regarding the measures that may be included in a repayment plan.

<sup>125</sup> Kilborn (n 71) 635–636; Spooner (n 2) 752. At present, this is still the position in South African law; see the discussion of the debt review and administration procedures above.

<sup>126</sup> Kilborn (n 71) 649 n 228.

<sup>127</sup> *ibid* 649. Contrary to the present position in South African law, in terms of which courts will not confirm payment plans that are not economically viable, see *Seffert v Firstrand Bank Ltd* [2012] 6 SA 581 SCA para 13.

<sup>128</sup> Kilborn (n 71) 650.

<sup>129</sup> This period was designed to allow the debtor’s financial situation to stabilise; Kilborn (n 71) 650.

<sup>130</sup> The total duration of the measures provided for in art L733-1 may not exceed seven years. However, loans relating to the purchase of the debtor’s principal residence may be rescheduled over a longer period (art L733-3).



and L733-8, with the exception of the two-year moratorium.<sup>131</sup> In terms of article L733-7 the commission may, first of all, recommend,<sup>132</sup> in the case of the forced sale of the debtor's principal residence, a reduction in the outstanding amount of the debtor's home loan after the sale, and thus after application of the proceeds of the sale to the principal amount outstanding. The reduction must enable the debtor to afford payment of both the reduced amount and any rescheduled debt under article L733-1.<sup>133</sup> In conjunction with the measures provided for in article L733-1, the commission may also recommend a partial discharge of debt.<sup>134</sup> In terms of article L733-8, the commission may recommend<sup>135</sup> that the measures provided for in articles L733-1 and L733-7 be made conditional upon steps taken by the debtor to facilitate or guarantee payment of the debt.<sup>136</sup>

A survey conducted by the Banque de France provided the stimulus for the introduction of the third level of debt relief, namely the *rétablissement personnel* (personal-recovery) procedure in 2003.<sup>137</sup> The data from this survey indicated that the French system did not provide effective relief to most over-indebted consumers. Most consumers' insolvency was clearly not a temporary situation, and the two-year moratorium was a mere formality, which placed an unnecessary administrative burden on the commissions.<sup>138</sup> Consequently, lawmakers introduced *rétablissement personnel*, eliminating the payment-plan requirement and providing an immediate discharge<sup>139</sup> of the debtor's obligations in return for a liquidation of his or her available assets.<sup>140</sup> However, since 2010, the commissions may also recommend *rétablissement personnel* without a liquidation of assets where the debtor's

<sup>131</sup> Art L733-2. A party may bring an appeal to the District Court in respect of any of the measures imposed or recommended by the commission; see art L733-12. In such a case the court may also order the implementation of the *rétablissement personnel* (personal-recovery) procedure without liquidation (art L733-15); see in respect of personal recovery, the discussion below. As soon as the measures in terms of art L733-1 have been imposed or the measures in terms of art L733-7 and L733-8 have been approved by the court, creditors are, during the implementation period of these measures, entitled to exercise enforcement proceedings against the debtor's assets; see art L733-17.

<sup>132</sup> The measures in terms of art L733-7 will thus only be effective after approval by the court; see art L733-6 and L733-10.

<sup>133</sup> The same provisions apply where the house has been sold by private treaty in order to avoid foreclosure; see art L733-7.

<sup>134</sup> Art L733-7.

<sup>135</sup> The measures in terms of art L733-8 will thus only be effective after approval by the court – see art L733-6 and L733-10.

<sup>136</sup> For example, steps to sell some of the debtor's assets; see Banque de France, 'Dealing with Household Overindebtedness' (September 2012) < <http://bit.ly/2gSEld8> > accessed 19 November 2016 at 5.

<sup>137</sup> Kilborn (n 71) 655.

<sup>138</sup> *ibid.*

<sup>139</sup> Art L742-22.

<sup>140</sup> Arts L724-1 and L742-1.

only assets are personal household items without any market value, or where the value would be disproportionate to the cost of the sale.<sup>141</sup>

In terms of the latest version of the French Code, the commission may, after consideration of the debtor's application for debt relief, recommend implementation of the personal-recovery procedure. If the commission is of the opinion that the debtor's financial circumstances have been 'irremediably compromised'<sup>142</sup> – are so overburdened by debt that neither an out-of-court repayment plan,<sup>143</sup> nor any of the measures provided for in articles L733-1, L733-7 or L733-8 will provide a solution to the debtor's debt problems – the commission may recommend personal recovery with a liquidation of assets,<sup>144</sup> or, where the debtor's only assets are personal household items without any market value, or where the value would be disproportionate to the cost of the sale, a personal recovery without a liquidation of assets.<sup>145</sup> In such a case the court merely confirms the commission's recommendation,<sup>146</sup> after which the debtor receives an automatic and immediate discharge of all non-professional debts.<sup>147</sup> In contrast to the US and German systems, the French Code does not provide any grounds for refusal of a discharge, and a lack of good faith on the part of the debtor only plays a role when the commission has to decide whether the debtor should be allowed access to the system.<sup>148</sup>

If the debtor's financial circumstances become irremediably compromised<sup>149</sup> during the course of the process relating to an out-of-court repayment plan,<sup>150</sup> or during the process relating to the measures imposed and/or recommended by the commission,<sup>151</sup> the debtor may apply to the commission for a personal recovery with or without a liquidation of assets.<sup>152</sup> Implementation of the personal-recovery procedure may also be recommended if the commission, after the conclusion of the two-year

<sup>141</sup> Arts L724-1 and L741-1. The fact that the French system acknowledges and provides specific debt-relief measures for NINA estates, tally with international principles and guidelines. See (n 13).

<sup>142</sup> Art L724-1.

<sup>143</sup> In accordance with art L732-1.

<sup>144</sup> Art L742-1. See arts L742-14–L742-19 regarding the liquidation proceedings. The liquidator must realise the debtor's assets within twelve months (see art L742-16).

<sup>145</sup> Arts L724-1 and L741-1. The fact that the system does not discriminate on financial grounds as regards access or the discharge of debt, corresponds with international principles and guidelines. See (n 12) and (n 2).

<sup>146</sup> Art L741-2. In terms of art L741-5 a party may appeal to the District Court against the commission's recommendation for a personal recovery without liquidation.

<sup>147</sup> Art L741-3. Certain debts, such as fines and compensation awarded to victims in a criminal conviction, are excluded (see arts L711-4 and L711-5).

<sup>148</sup> Art L711-1.

<sup>149</sup> Art L724-1.

<sup>150</sup> Art L732-1.

<sup>151</sup> Art L733-1, L733-7 and L733-8.

<sup>152</sup> Art L724-2.

moratorium and the subsequent re-evaluation of the debtor's financial situation, is of the opinion that it is necessary in the circumstances.<sup>153</sup>

From the above discussion it should be clear that, with its introduction of the *rétablissement personnel* procedure, the French legislator deviated from the traditional earned-discharge approach by introducing a fresh-start procedure, similar to the US Chapter 7 procedure.<sup>154</sup> Moreover, the French legislator in effect also acknowledged the right of NINA debtors not to be excluded from a discharge procedure. It is also interesting to note that there is no limitation on the number of times a debtor may apply for *rétablissement personnel* and a debtor can thus undergo personal recovery as many times as necessary.<sup>155</sup>

### **Evaluation of the Different Approaches**

Practice has shown that repayment plans often do not provide satisfactory returns for creditors and the traditional European earned-discharge approach has, therefore, often been criticised.<sup>156</sup> However, it is important to note that the philosophy behind the traditional European approach lies in its pedagogical purpose.<sup>157</sup> Kilborn<sup>158</sup> explains as follows:

European policy seems rather consistently to recognize at least a pedagogical purpose to be served, that is, multi-year plans remind debtors and those around them that everyone must do their best to fulfil their obligations, whatever the “best” is and budgetary guidance and supervision might be provided to debtors during the plan period to reinforce this goal. To one degree or another, this pedagogical purpose is moralistic, inculcating good payment morality by reminding debtors that they must sacrifice their own comfort and desires to offer something to their creditors, even if debtors “have nothing but blood, toil, tears and sweat”.

The German system clearly emphasises the importance of impressing financial responsibility upon consumer debtors and thus the educational purpose of the traditional earned-discharge approach. In contrast with the French system, which requires some debtors to earn their discharge, but grants an immediate discharge to NINA debtors, the German system treats all debtors equally. This is because all debtors who comply with the best-effort principle and eventually make it through the six-year so-called good behaviour period – even those who cannot provide any distribution to

<sup>153</sup> Art. L733-2.

<sup>154</sup> Kilborn (n 71) 655–656.

<sup>155</sup> *ibid* at 660. However, repeated filings may be an indication of the debtor's lack of good faith; see *ibid* at (n 306).

<sup>156</sup> *ibid* at 667.

<sup>157</sup> Reifner (n 70) 168.

<sup>158</sup> Kilborn (n 73) 34.

creditors – will be granted the privilege of a discharge of unpaid debts.<sup>159</sup> The German system thus accomplishes a balance by requiring a waiting period for a discharge in all cases, including NINA cases.

When taking the administrative burden into consideration, together with the unnecessary costs involved, the six-year repayment period of the German system is clearly too long. However, it is submitted that South African lawmakers should not adopt the new approach of providing an immediate discharge to NINA debtors. It is submitted that lawmakers should, in light of the vital educational purpose it fulfils, rather adopt the traditional earned-discharge approach for all debtors, but for a shorter waiting period of three years which period correspond to internationally preferred principles.<sup>160</sup> In this way, all consumer debtors – that is debtors who qualify for debt-restructuring,<sup>161</sup> normal insolvency proceedings,<sup>162</sup> or for a NINA procedure – will be treated equally and will be subject to the same waiting period during which they are supposed to learn the necessary lessons of insolvency. We suggest that the traditional approach may also be more acceptable for the pro-creditors South African community that still supports a system which emphasises the objective of maximising returns for the *concursum creditorum* by requiring advantage for creditors as a prerequisite for rehabilitation and discharge of debt.<sup>163</sup>

As regards access requirements, it is to be noted that the French system,<sup>164</sup> in contrast to the German system (where good faith is tied to the right of discharge),<sup>165</sup> requires debtors to demonstrate good faith in order to obtain access to insolvency proceedings. An important point of criticism against good faith as a requirement for access, is the fact that it may expose debtors to divergent interpretations of the concept if it is not properly defined. Also, society only needs protection against a minority of unscrupulous debtors and, therefore, a default inquiry into debtors' good faith at the application

<sup>159</sup> Kilborn (n 71) 664. Kilborn (n 70) 296 suggests that the German system's 'good behavior period' is much more concerned with the debtors' 'resocialization and re-entry into the open credit economy than with ensuring any dividend to creditors'.

<sup>160</sup> See (n 94).

<sup>161</sup> I.e. debt review or administration in terms of the NCA and MCA respectively.

<sup>162</sup> I.e. sequestration in terms of the Insolvency Act.

<sup>163</sup> See in respect of the South African pro-creditors approach in general André Boraine et al, 'The Pro-creditors Approach in South African Insolvency Law and the Possible Impact of the Constitution' (2015) Nottingham Insolvency and Business Law e-Journal 59.

<sup>164</sup> Several European countries require good faith as a requirement for access to insolvency proceedings. However, it is only France and the Netherlands that expressly require good faith for access; see Roestoff (n 94) 616.

<sup>165</sup> Van Appeldoorn (n 80) 64. See regarding Germany, s 1 of the InsO in respect of the objectives of insolvency proceedings. In terms of s 1 of the InsO, the first objective of insolvency proceedings is the collective satisfaction of creditors' claims by way of liquidation of assets or a repayment plan. The second objective is to provide honest (and thus bona fide) debtors with an opportunity to obtain a discharge of residual debt.

stage would be excessive and wasteful.<sup>166</sup> Consequently, it is submitted that South African lawmakers should not follow the French approach in this regard and that bona fides should generally, and at most, be required as a pre-condition for the eventual granting of a discharge. However, we do recommend that relief should be denied in cases of fraud or serious misconduct. Nevertheless, this does not mean that cases must be screened at the application stage of the procedure and we consequently recommend that interested parties should rather be able to challenge the granting of a discharge at a later stage.

Further, regarding access and within the ambit of the NINA procedure, we are not in favour of thresholds (as for instance, proposed by the South African Law Reform Commission) relating to total debt, as such restrictions would have the effect of excluding worthy cases from any form of relief. However, administrators should be empowered to refer cases for an inquiry where substantial amounts of debt are involved. Nonetheless, we do suggest that debtors should meet financial requirements to gain access to the NINA procedure in that they should neither have any valuable, realisable or non-excluded assets, nor surplus income available for distribution amongst creditors. In this respect, the French requirement of only allowing a debtor 'where the debtor's only assets are personal household items without any market value or where the value would be disproportionate to the cost of the sale' is a good point of departure as regards assets. In relation to income, to determine whether there is surplus income available for distribution and consequently whether a debtor qualifies for the NINA procedure on a case-by-case basis, would be costly and time consuming. However, a measure of discretion is still needed and a standard baseline should be supplemented by non-standard allowances, such as for housing, transport and child care. Although many jurisdictions view the insolvency system as an extension of the ordinary collection system where the same limitations on the garnishment of wages and other income are adopted, in South Africa no limitations as regards the percentage of income that may be attached in individual enforcement procedures are prescribed. We therefore suggest that bands of uniformity, where people are categorised into groups with different excluded amounts in accordance with, for example, the number of dependent children and their ages, be developed and that these be uniformly applied.<sup>167</sup>

Contrary to the French system, which allows the commissions to implement an out-of-court settlement procedure as one of the three possible options for debt relief, the German system obliges all debtors, including NINA debtors, to make an attempt at negotiating a repayment plan before access to insolvency proceedings will be allowed. However,

<sup>166</sup> See also Coetzee (n 94) 419.

<sup>167</sup> cf *ibid* 442 et seq.

this obligatory out-of-court settlement procedure has not proved effective in providing a solution to the consumers' financial problems<sup>168</sup> and is clearly an inappropriate and wasteful measure for NINA debtors, as they do not have any assets or income on the basis of which to make any acceptable or realistic offer to their creditors.<sup>169</sup> The viewpoint of the South African Law Reform Commission that its proposed pre-liquidation composition procedure would adequately address the plight of South African NINA debtors, is thus clearly misconceived. It is submitted that the French system, which assigns, a so-called gatekeeping responsibility<sup>170</sup> to the commissions to direct the consumer along one of three appropriate routes to eventual debt relief, is preferable to the German system, which requires all debtors to follow the same single route to eventual debt relief. German law does not provide a separate procedure designed specifically for NINA debtors and all over-indebted consumer debtors are obliged to go through the same long, expensive and complex procedure, including a liquidation procedure which, amongst others, requires the appointment of a trustee.<sup>171</sup> This, despite the fact that the liquidation phase of German proceedings – as is the position in the USA – is virtually meaningless, as most debtors have no assets that could be realised and thus, proceeds that could be divided between creditors.<sup>172</sup>

Apart from the French system's unique approach in assigning the responsibility of selecting and implementing the appropriate debt-relief proceedings to the commissions, the involvement of the Banque de France in the French system to provide the necessary legitimacy and trust in the system, has, according to Kilborn, been one of the most effective elements of the French system.<sup>173</sup> In this regard, it is submitted that South African lawmakers should learn from the French approach and should consider extending the current debt-counselling system, which is, at present, supervised by the National Credit Regulator, to include directing over-indebted consumers to the appropriate proceedings. Such proceedings should include an asset-liquidation, income-restructuring and non-expensive tailor-made NINA procedure for those who have nothing of value with which to pay the costs of the proceedings or to make payments to their creditors.

As indicated earlier, the modern international trend and guidelines are that the courts' involvement in insolvency proceedings should, as

<sup>168</sup> cf Kilborn (n 71) 667.

<sup>169</sup> See Bodul and Žiković (n 88) 395.

<sup>170</sup> Kilborn (n 71) 636.

<sup>171</sup> S 313(1). See Bodul and Žiković (n 88) 396.

<sup>172</sup> Kilborn (n 70) 278. See also Bodul and Žiković (n 88) 395. See further Dörte Busch, 'Current Reform Efforts of German Consumer Insolvency Law and the Discharge of Residual Debts' (2006) German LJ 591 at 593 et seq for a discussion and evaluation of current reform efforts and models of German consumer insolvency and the discharge of residual debts.

<sup>173</sup> Kilborn (n 71) 639. See also World Bank (n 3) para 136, which notes the involvement of a government regulator as one of the factors that contribute to the higher success rate of voluntary settlements.

far as possible, be restricted.<sup>174</sup> It clearly does not make sense to burden the already overloaded courts with NINA cases.<sup>175</sup> The French system's establishment of administrative bodies to deal with cases and to direct debtors to the appropriate proceedings, is thus preferable to the German court-orientated system. It is suggested that South African lawmakers should consider limiting our courts' involvement to highly complex insolvency proceedings,<sup>176</sup> or, as is the position under French law, limiting it to a mere supporting role, for example, in revising or approving recommendations made by debt counsellors.<sup>177</sup>

A central issue in consumer-insolvency law is that provision should be made for a moratorium on collection efforts by creditors in order to protect debtors from harassment by creditors and thus provide them with a much-needed breathing space. Under German and French law, the commencement of an insolvency or debt-relief application does not have the automatic effect of halting debt collection. In Germany, a moratorium only follows from a decision to open insolvency proceedings by the court, while under French law, the onus is on the debtor to apply to the commission to request the court's protection while the case is handled by the commission, and a final moratorium only becomes effective once the commission has accepted the debtor's debt-relief application. It is submitted that South African lawmakers should provide for an automatic moratorium for all debtors the moment a case is filed. This not only reflects the internationally preferred position,<sup>178</sup> but also promotes legal certainty and safeguards the estate – if there is a significant estate to secure – on behalf of the *concursum creditorum*.

## CONCLUSION

Over-indebtedness is an ongoing problem that must be addressed on a continuous basis and, most importantly, in a suitable manner. South African consumer debtors are heavily over-indebted, as is evidenced by the National Credit Regulator's Creditor Bureaux Monitor Report,<sup>179</sup> which records that, for the second quarter of 2016, more than 40 per cent of credit-active consumers had impaired credit records.<sup>180</sup> Furthermore, the majority of South

<sup>174</sup> See (n 15).

<sup>175</sup> Bodul and Žiković (n 88) 396.

<sup>176</sup> Such as sequestration where advantage to creditors is required.

<sup>177</sup> Such a reform will also address the problem of overburdened courts experienced with regard to applications for debt rearrangement in terms of the NCA; see *Standard Bank of South Africa Ltd v Kruger*; *Standard Bank of South Africa v Pretorius* [2010] 4 SA 635 (GSJ) para 17; Melanie Roestoff, 'Ferris v Firstrand Bank Ltd 2014 3 SA 39 (CC) – Enforcement of a Credit Agreement After Breach of a Debt Rearrangement Order and the Ineffectiveness of Debt Review in Terms of the National Credit Act' (2016) De Jure 134 at 152.

<sup>178</sup> See (n 17).

<sup>179</sup> National Credit Regulator, 'Credit Bureaux Monitor Report' (National Credit Regulator) <<http://bit.ly/2hgcPaH>> accessed 7 December 2016.

<sup>180</sup> *ibid.*

African consumer debtors can most probably be labelled as NINA debtors in that an exceptionally large portion – some 27.1 per cent – of South Africans are unemployed.<sup>181</sup> Also, the most recent World Bank statistics estimate the country's poverty headcount at 16.6 per cent in 2011.<sup>182</sup> Consequently, appropriate debt-relief measures for individuals from especially the NINA category of debtors are of paramount importance. Although it is encouraging that the South African government is recognising the need for appropriate debt-relief measures, amendments to current proposals (as set out in the 2015 Insolvency Bill) are necessary for it to achieve its objective of providing debt relief to currently marginalised consumer debtors. In this regard, much can be learned from the European approach to debt relief and internationally sanctioned principles and guidelines.

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<sup>181</sup> StatsSA, 'Statistics South Africa Quarterly Labour Force Survey Q3:2016' <<http://bit.ly/2gBL3Bt>> accessed 7 December 2016.

<sup>182</sup> World Bank, 'Poverty & Equity' <<http://bit.ly/2h2iEoQ>> accessed 7 December 2016.