Elaborating UNCITRAL's Legislative Guide on Insolvency Law: Principles for Natural Persons

Jason J. Kilborn[*]

Abstract

This article advances detailed proposals for an expansion of UNCITRAL's landmark Legislative Guide on Insolvency Law *to encompass several key issues of particular concern to individual debtors. Small entrepreneurs makes up the vast majority of business actors in the world today, yet most of the discussion in the Guide is concentrated on corporate insolvency resolution. The Guide currently makes reference to natural person debtors, but it offers little or no discussion or consideration of several of the most salient issues unique to natural persons, as opposed to juridical entities. Many of these issues have crystallized only after the Guide's adoption in 2004, and a vast expansion of judicial and legislative activity on personal insolvency since that time has thrust these issues to the forefront of insolvency policy. This article thus advocates for a revisitation and expansion of the Guide by surveying in detail the most critical divergences in law and practice among existing personal insolvency regimes, including several of the newest laws adopted in 2015 and 2016. It proposes that the Guide's discussion of these issues, and of the very goals to be achieved by an insolvency law, be augmented by consideration of these crucial emerging topics, which are of increasing concern for legislators seeking the very guidance that UNCITRAL and its Legislative Guide project had aimed to provide.*

I. Introduction: New Developments Call for a New, Expanded Perspective

Time flies. Already more than a decade has passed since UNCITRAL and the UN General Assembly adopted the *Legislative Guide on Insolvency Law* in 2004.[1] The world of insolvency law and policy has changed considerably in that time. Perhaps the most dramatic change is the explosion of legislative activity relating to the insolvency of natural persons.

In 1999, when the proposal was first advanced for UNCITRAL's insolvency project, only a handful of states offered meaningful debt relief to natural persons, including small business entrepreneurs. One notable commentary aptly observes that "the classical reaction to insolvency ('bankruptcy') was punishment of the debtor and comprehensive liquidation and distribution of the debtor's property among the creditors."[2] This philosophy applied equally to juridical and natural persons, but it began to give way to a new vision of rescue and rehabilitation by the turn of the 21st century, as reflected in UNCITRAL's *Legislative Guide*. For small entrepreneurs and consumers, however, notions of rescue and rehabilitation remained generally out of reach in light of the paucity of assets in these small cases and the cost and complexity of modern rehabilitation procedures.

[*] Professor of Law, John Marshall Law School (Chicago) and Van der Grinten Professor of International & Comparative Insolvency Law, Business & Law Research Centre, Radboud University Nijmegen (The Netherlands), jkilborn@jmls.edu.

[1] *See* UNCITRAL, *Legislative Guide on Insolvency Law* iii (2014).

[2] *Principles of European Insolvency Law* 66 (W.W. McBryde, A. Flessner, & S.C.J.J. Kortmann, eds., 2003).

The plight of ordinary, individual debtors received growing attention in the 21st century, however. In the 1980s and 1990s, several bellwether European states had begun a long process of adopting, reviewing, and repeatedly revising new insolvency proceedings designed for the specific needs and characteristics of large numbers of overindebted individuals, especially those with limited assets and income.[3] As UNCITRAL's *Legislative Guide* was being formulated, these first-mover European states were busy revising and expanding their laws in response to the trials and errors of the first tumultuous years of this process.[4] After the mid-2000s, when the *Legislative Guide* was finalized, a movement rapidly expanded across Europe to consolidate the lessons of these early years and offer more effective debt relief to natural persons. By January 2016, this movement encompassed almost all of the EU Member States, and the remaining holdouts are facing increasing pressure to fall into line.[5] In both Africa and South America, several states have been actively exploring procedures for treating individual insolvency, and South Africa put in place such a process in 2005, followed by Colombia in 2012.[6]

UNCITRAL's *Legislative Guide* does not reflect this later legislative activity and the key lessons informing evolving insolvency policy for individual debtors. While the *Guide* expressly encompasses consideration of issues specific and sometimes unique to natural persons, it fails to identify key policies and procedures that a decade of experience has shown to be most salient in this particular context. While the *Guide* explicitly excludes consideration of issues specific to "consumer" insolvencies,[7] the small business persons that make up the majority of economic actors in the world today have much more in common with ordinary consumers than with large corporate debtors.[8] As the European Commission's recent study on individual insolvency pointedly observes, "procedures that are designed for corporate and/or larger business debtors may be inappropriate" for sole traders and family entrepreneurs.[9] And as the *Guide* itself admits, cases involving individual debtors will inevitably involve "the intersection of business indebtedness with consumer indebtedness," and "it may not always be possible to separate the debts into clear categories."[10] Consequently, the rules governing insolvency resolution for natural persons should apply to all such persons, as "it may not be feasible to have rules on business debts of natural persons that differ from the rules applicable to consumer debts."[11]

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[3] *See, e.g.,* Jason J. Kilborn, *Expert Recommendations and the Evolution of European Best Practices for the Treatment of Overindebtedness, 1984-2010,* at 18-20 (2011) [hereinafter, Kilborn, *Expert Recommendations*].
[4] *See, e.g.,* Jason J. Kilborn, "Two Decades, Three Key Questions, and Evolving Answers in European Consumer Insolvency Law: Responsibility, Discretion, and Sacrifice," in *Consumer Credit, Debt and Bankruptcy: Comparative and International Perspectives* 307-29 (Johanna Niemi, Iain Ramsay & William Whitford eds., Oxford: Hart Publishing 2009) [hereinafter, Kilborn, Two Decades].
[5] *See* Gerard McCormack et al., University of Leeds, *Study on a new approach to business failure and insolvency: Comparative legal analysis of the Member States' relevant provisions and practices* 285, 319, 333-39 (2016), online at http://ec.europa.eu/justice/civil/files/insolvency/insolvency_study_2016_final_en.pdf.
[6] *See, e.g.,* Melanie Roestoff et al., "The Debt Counselling Process—Closing the Loopholes in the National Credit Act 34 of 2005," 12 *P.E.R.* 247, 251-55 (2009); Jason J. Kilborn, "Reflections of the World Bank's *Report on the Treatment of the Insolvency of Natural Persons* in the Newest Consumer Bankruptcy Laws: Colombia, Italy, Ireland," 27 *Pace Int'l L. Rev.* 309, 322 (2015) [hereinafter Kilborn, Reflections].
[7] *Legislative Guide, supra* note 1, at 1.
[8] *See* World Bank, *Report on the Treatment of the Insolvency of Natural Persons* ¶¶ 18, 45 (2013).
[9] McCormack et al., *supra* note 5, at 288.
[10] *Legislative Guide, supra* note 1, at 284.
[11] *Id.*

It is high time for UNCITRAL to revisit its *Legislative Guide* project to include major recent developments with respect to the most prominent issues affecting individual debtors and their personal insolvency resolution. As the *Guide* acknowledges, "society is constantly evolving, [so] insolvency law cannot be static, but requires reappraisal at regular intervals to ensure that it meets current social needs."[12] The upheaval of the Great Recession and the consequent fundamental shifts in individual insolvency policy have revealed social needs to which the *Guide* does not respond. No wholesale revision is required; rather, the *Guide* could be significantly enhanced simply by including a more deliberate consideration of a few particular sticking points that have divided modern procedures, created notable inefficiencies, and undermined UNCITRAL's original goal to "foster and encourage the adoption of effective national … insolvency regimes."[13]

II. Emerging Topics of Particular Relevance to Individual Debtors

In our diverse world, one would expect a substantial degree of variation among national insolvency laws, and the *Legislative Guide* acknowledges and accepts this.[14] Nonetheless, some key issues are especially vital to efficient and effective insolvency systems, and they reflect important developments and trends and, sometimes, a high degree of consensus on better practices. Two such issues are introduced generally in the *Guide* but could benefit from greater elaboration specific to the context of natural person debtors: (1) standards for commencing an insolvency case, and (2) requirements for obtaining a discharge of unpaid debts.[15]

A. Commencement Standards for Insolvency Proceedings

The *Legislative Guide* recognizes that "[t]he standard to be met for commencement of insolvency proceedings is central to the design of an insolvency law," and it endorses standards that are "transparent and certain" to encourage and facilitate financially distressed debtors in seeking relief voluntarily, but also "balanced with appropriate and adequate safeguards to prevent improper use."[16] It proceeds to discuss the two commencement standards common to corporate cases: equitable insolvency (cessation of payments) and balance-sheet insolvency (debts exceeding present asset value).

This discussion masks the struggles witnessed in recent years to control access to debt relief for individuals. Natural persons cannot simply grind to a halt; they must carry on existing as best they can, providing for their own and their dependents' basic survival needs. Neither the general cessation nor the balance-sheet test is particularly appropriate to this context, and modern personal insolvency laws have struggled to find the right balance between encouraging debtors to obtain relief and discouraging debtors from abusing that opportunity. Modern laws differ dramatically in the degree to which they limit or condition, both formally and practically, individual access to personal insolvency relief. Often these standards are neither transparent nor certain, and some are more problematic than others.

[12] *Id.* at 16.
[13] *Id.* at iii.
[14] *See id.* at 2, 15; *see also* McCormack et al., *supra* note 5, § 8.7 at 358.
[15] The following discussion is adapted from an earlier, extended analysis of this material in Jason J. Kilborn, "The Personal Side of Harmonizing European Insolvency Law," 25 *Norton J. Bankr. L. & Pol'y* 581, 587-611 (2016).
[16] *See Legislative Guide, supra* note 1, at 45.

1. Insolvency, Overindebtedness, Hopelessness?

The *Legislative Guide* would benefit from a frank evaluation of the cacophony of differing definitions of financial distress that entitle individuals to commence an insolvency case. In the natural person debtor context, debt levels and income play a more prominent role than payment behavior or asset value. Existing approaches identify the necessary degree of financial distress in widely varying ways, whether by definition (*e.g.,* inability—not simple cessation—to service debts as they come due) or other objective indicators (*e.g.,* minimum debt levels or debt-to-income ratios).[17] European authorities have sought for many years to identify an optimal, uniform approach to defining "overindebtedness," but a final solution remains elusive.[18]

It would be useful for the *Guide* to identify and evaluate the opaque and restrictive approach taken by emerging individual overindebtedness regimes like those in Scandinavia and Eastern Europe. To commence a case under the Danish law, for example, debtors must clear two high hurdles: First, debtors must establish their "qualified insolvency," a restrictive notion that implies hopeless financial collapse. Even deeply insolvent debtors can be barred from relief if their standard of living is higher than what the court in its unfettered discretion considers "reasonable," or even if the debtor's future financial situation is "uncertain."[19] Before a reform in 2005, this second criterion all but excluded small business operators, as fluctuating business income rendered the debtor's financial future too uncertain.[20] Even after the reform, temporary unemployment (perhaps following the collapse of a small business) might still undermine the "certainty" of the debtor's distress. Second, the court must adjudge the debtor deserving of relief based on a vague and opaque reasonableness standard. Originally, the Danish law directed courts to presume that relief was *in*appropriate, though a 2005 reform reversed the presumption.[21] Other Scandinavian regimes apply similar access criteria, and all have extremely high rates of rejecting debtor applications.[22]

Another cautionary tale of an untransparent and overly demanding commencement standard comes from Poland. Effective since early 2009, the Polish law originally allowed access only to debtors whose financial distress was caused by exceptional circumstances entirely beyond their control.[23] In the first two-and-a-half years of the law's effectiveness, debtors submitted over 2000 applications for relief, but the courts admitted only 60 as meeting the stringent entry requirement. Polish policymakers characterized this 2.78% admission rate as "truly insignificant" and, effective December 31, 2014, the law was amended to permit access to debtors whose insolvency was not caused intentionally or through gross negligence.[24]

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[17] McCormack et al., *supra* note 5, at 314-18.
[18] *See* Civic Consulting, *The Over-Indebtedness of European Households: Updated Mapping of the Situation, Nature and Causes, Effects and Initiatives for Alleviating Its Impact* 19-31 (2013) (concluding that "the time may have come to abandon the attempt to precisely define a term that many people seem to find unhelpful").
[19] *See* Jason Kilborn, "Twenty-Five Years of Consumer Bankruptcy in Continental Europe: Internalizing Negative Externalities and Humanizing Justice in Denmark," 18 *Int'l. Insol. Rev.* 155, 167 (2009) [hereinafter Kilborn, Denmark].
[20] After the reform, the "uncertainty" factor can be set aside in cases of small entrepreneurs. *Id.* at 167 n. 76.
[21] *Id.* at 175-76.
[22] *See* Kilborn, *Expert Recommendations*, *supra* note 3, at 42-43.
[23] *See id.* at 43; Sejm Druk nr 2265, Draft law amending the law – Law on insolvency and restructuring and other acts (Feb. 7, 2014) (in Polish, on file with author) [hereinafter Sejm Druk 2265].
[24] *See id.*; Law on insolvency and restructuring § 491(4)(1) [Poland].

Legislators in other states would benefit if the *Legislative Guide* offered a discussion and perhaps critique of this experience, which created significant waste and inefficiency for both debtors and the insolvency system. Without such guidance, further legislative missteps have proliferated. The new Hungarian individual insolvency law contains a unique Goldilocks provision requiring a "not-too-solvent, not-too-insolvent" debt level for commencement, along with a panoply of restrictions. To be admitted into the "debt management for natural persons" procedure, effective September 1, 2015, Hungarian debtors must have at least 2 million forints in debt (about €6400) but no more than 60 million forints (about €193,000), and this debt must be at least 100% but less than 200% of the value of all of the debtor's assets and expected available income over the ensuing five years.[25] In addition, Hungarian debtors are excluded from the procedure altogether if they are subject to any foreign claims, enforcement proceedings by any creditor with a claim of 200,000 forints or more (about €640), or any outstanding debt for fines or most public law debts.[26] These unique commencement restrictions hamper the effectiveness of the Hungarian law and set it apart as exceptionally poorly conceived. A specific note of warning in the *Legislative Guide* as to this degree of exclusion would be especially constructive.

2. Minimum Payment Capacity

Even for debtors who successfully sail past the Scylla of demonstrating financial distress, some modern laws actually deny relief to debtors who are *too* distressed, as they crash on the Charybdis of a further requirement of minimum payment capacity. These regimes require debtors to either pay or provide assurance of future payment of the administrative fees of the process and sometimes even a minimum dividend on creditors' claims; otherwise, their cases are dismissed. This creates an ironic underclass of debtors who are too financially distressed to obtain relief from their financial distress.

In Slovakia, for example, barely 150 cases were opened in the first three-and-a-half years after implementation of the new personal discharge provisions in that country in 2006, very likely as a result of debtors' inability to finance administration fees.[27] Similar problems initially plagued the nascent procedures in Germany and Poland, but both of these countries settled on a similar solution: In Germany since 2001, and Poland since 2015, court costs and trustee fees are initially covered by the state treasury, and either practically in Germany, or formally in Poland, fees that remain unpaid at the conclusion of the debtor's payment plan are permanently borne by the public fisc.[28] Worse yet, the Austrian and Czech laws call for dismissal of cases in which the court is not satisfied that the debtor will manage to pay general creditors a minimum dividend of 10% or 30%, respectively, of their claims.[29] The South African law achieves the same result by requiring a demonstrated benefit to creditors before commencing an insolvency case.[30]

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[25] Gusztáv Báger, "Introduction of a Debt Management Procedure for Natural Persons in Hungary," 2015 *Public Fin. Q.* 492, 498 (2015); Kornelia Nagy-Koppany, *The Hungarian Personal Bankruptcy Act* (Sept. 1, 2015), http://www.lawyerissue.com/the-hungarian-personal-bankruptcy-act/.
[26] *See* Báger, *id.,* at 498-99 (excluding debts for housing, student loans, or overpayment of minor state subsidies).
[27] *See* Kilborn, *Expert Recommendations*, *supra* note 3, at 35.
[28] *See id.* at 35-36; Sejm Druk 2265, *supra* note 23; Law on insolvency and restructuring § 491(7)(1) [Poland].
[29] *See* Kilborn, *Expert Recommendations*, *supra* note 3, at 36 n. 107.
[30] Insolvency Act 1936 ss. 3(1), 6 [South Africa]; *see generally* Roestoff et al., *supra* note 6.

The *Legislative Guide* points out that public interest concerns in particular may militate in favor of enabling commencement of low-asset cases like these.[31] It also notes the particular importance of cost-effective procedures in low-asset cases commenced by small and medium-sized businesses.[32] It would be useful for the *Guide* to address more directly the counterproductive nature of excluding small entrepreneurs from modern relief systems based on their inability to pay. Even if these debtors have little or nothing to distribute to creditors, the purposes of personal insolvency legislation are quite distinct from those of traditional, creditor-oriented bankruptcy systems. Producing a benefit for creditors is only one of a large number of goals of modern personal insolvency law, which the *Guide* would do well to articulate (in addition to the largely creditor-oriented goals it currently lists).[33]

The *Guide* misses an opportunity when it discusses mechanisms for financing the administration of low-value cases[34] but draws no explicit connection between administrative costs and needless procedural formalities. Where applications for personal debt relief are adjudicated by courts, often with traditional formalities borrowed from corporate bankruptcy practice, the cost burden is generally substantial. Several states have reduced or eliminated formalistic procedures that are too expensive for small debtors and are not necessary to protect the practical interests of the parties. In the court-based Dutch procedure, for example, after practice revealed that little or no distribution was likely in most individual debtor cases, courts exercised their discretion to stop holding official hearing for verification of creditors' claims, and the legislature formally ratified this procedural simplification as of 2008.[35] In Sweden, a formerly three-step process involving preliminary agency determinations followed by court confirmation was found to be needlessly formalistic, so it was reduced to one, agency-controlled step, with the courts standing by only as appellate bodies.[36] Other examples of simplification, abandonment of formality, and efficiency enhancement through, *e.g.,* greater use of the internet, appear in several other Member States.[37] It would be quite useful for the *Guide* to point out that a simpler, more streamlined procedure might be recommended for cases involving natural person debtors and few assets. Again, without such guidance, developing systems continue to flounder. In the few year of its existence, the Greek personal insolvency procedure, for example, has been bogged down by bureaucratic court formalities, needlessly delayed hearings on debtor's petitions by as long as seven years.[38]

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[31] *Legislative Guide, supra* note 1, at 61-62.
[32] *Id.* at 63.
[33] *See id.* at 10-14, and for a detailed discussion of modern personal insolvency goals, see World Bank, *supra* note 8, ¶¶ 56-111.
[34] *See Legislative Guide, supra* note 1, at 62-63.
[35] *See* Raad voor Rechtsbijstand 's Hertogenbosch, Bureau Wsnp, *De Wsnp per 1 januari 2008: Wat wijzigt er?* (October 2007), www.mvz.nl/docs_mvz/watverandert_wsnp.pdf.
[36] *See* Jason J. Kilborn, "Out with the New, In with the Old: As Sweden Aggressively Streamlines Its Consumer Bankruptcy System, Have U.S. Reformers Fallen Off the Learning Curve?," 80 *Am. Bankr. L.J.* 435, 439-61 (2007) [hereinafter Kilborn, Sweden].
[37] *See, e.g.,* Kilborn, *Expert Recommendations*, *supra* note 3, at 37.
[38] Theodor G. Katsas, "Key Elements of the Greek Legal Framework on Insolvency of Natural Persons," in *Comparative Perspectives of Consumer Over-Indebtedness: A View from the UK, Germany, Greece, and Italy* 259, 264-65 (Federico Ferretti, ed., 2016).

3. Mandatory Pre-Filing Negotiation

One final commencement requirement not discussed in the *Guide* is a mandate for pre-filing negotiation with creditors. Debtors in several modern systems must have attempted to work out a voluntary debt adjustment with their creditors before seeking coercive relief (or have a qualified counseling agency certify that such an attempt would be futile).[39] Unfortunately, the results of this kabuki dance are all but predetermined, as the overwhelming majority of debtors have too little to offer creditors to secure a compromise arrangement, or trust and personal judgment issues interfere with rational business negotiation. In Greece, for example, of some 22,000 mandatory pre-insolvency conciliation attempts in the first years of the new personal debt relief system, only five produced voluntary workout plans.[40] Swedish debtors experienced similarly disappointing results in these mandated negotiations, which even creditor representatives characterized as "nearly meaningless."[41] As a result, both Sweden and Greece recently abandoned their mandatory conciliation requirement,[42] though it remains in a few other countries, including early-adopters Germany and the Netherlands, as well as some of the latest arrivals in Hungary[43] and, the newest system, Croatia.[44]

The *Legislative Guide* could offer useful perspective by juxtaposing historical preference for negotiated solutions against modern evidence of the futility of such negotiations in the personal insolvency context. A recent European Commission-sponsored study concluded "the benefit of [mandatory out-of-court negotiations] may be dubious, being, rather, a prolongation of the debtor's problems and an unhelpful delay."[45] Similarly, the World Bank observed pointedly "the merits of voluntary settlements are often illusory," citing long delays, debtors' being pressured to agree to "onerous payment plans that are not viable," and a very small rate of successful compromise.[46] The *Guide* could contribute quite constructively to this growing chorus of concern about the siren song of mandatory pre-commencement negotiation.

B. Requirements for Discharge of Debt

The second major issue identified briefly in the *Legislative Guide* that would benefit from significant elaboration is the requirements for debtors to obtain a discharge of unpaid debt. This is a vitally important concern for debtors, as debt relief is the primary if not sole purpose of their commencing insolvency proceedings, and lawmakers continue to experiment with demonstrably troubling differences in approach.

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[39] *See* Kilborn, *Expert Recommendations*, *supra* note 3, at 25.
[40] *See, e.g.,* Katsas, *supra* note 38, at 263 (noting a success rate of 0.02%).
[41] *See* Kilborn, Sweden, *supra* note 36, at 458-59.
[42] *See id.;* Katsas, *supra* note 38, at 263.
[43] *See* Báger, *supra* note 25, at 500, 502, 506-07; Nagy-Koppany, *supra* note 25.
[44] *See* Marko Kruc, *Croatia: Consumer Bankruptcy Act Introduces Consumer Bankruptcy into the Legal System* (Jan. 5, 2016), http://www.schoenherr.eu/publications/publications-detail/croatia-consumer-bankruptcy-act-introduces-consumer-bankruptcy-into-the-legal-system/.
[45] McCormack et al., *supra* note 5, at 348.
[46] *See* World Bank, *supra* note 8, ¶¶ 131, 133-34, 404.

1. Waiting or Paying for Discharge?

The *Legislative Guide* distinguishes three approaches to offering discharge relief to individuals: (1) Full discharge after a liquidation of the debtor's valuable, non-exempt assets, (2) no discharge until all debts are paid or the claims prescribe, or (3) discharge after a "period … during which … the debtor is expected to make a good faith effort to satisfy its outstanding obligations."[47] The first option represents the (in)famous US "fresh start" approach, allowing most debtors to seek an immediate discharge because they have no valuable, non-exempt property. The third option has become the principal choice of legislators in Europe and elsewhere, often characterized as an "earned start," because it requires debtors to submit to a multi-year payment plan (often in addition to relinquishing non-exempt assets, if any).[48]

Given the nascent state of practice in the early 2000s, the *Guide* offers no analysis of the crucial question of how an individual debtor's "good faith effort" is to be determined. Sufficient water has passed under the bridge now to provide critical guidance to legislators struggling with the very sensitive moral and economic choices involved in defining this vague "good faith effort." It would be useful for the *Guide* to include a few observations on the prevalence of this third approach, as well as on its hidden weaknesses.

First, the notion of requiring individual debtors to earn a discharge by enduring years on a subsistence budget is not uncontroversial. The European Commission's recent study on individual insolvency concludes "[t]here appears to be little evidence on whether Payment Plans merely serve an educative, retributive and symbolic function and are not in fact economically effective in terms of repaying debt."[49] The World Bank similarly questioned the utility of the administrative burdens of payment plans, noting "[i]n the majority of existing systems, in which fewer than one-fifth of cases initiated each year produce returns to creditors, it is highly questionable whether the administrative costs of the 'good behavior system' are justified."[50]

Second, as the World Bank observed, a great many European "payment" plans produce nothing of the sort; that is, the debtors have no non-exempt income to distribute to creditors over the plan period, yet they receive their discharge nonetheless. This is the overwhelmingly most common scenario for individual debtors in Germany, and a very common outcome of individual cases in Scandinavia.[51] After struggling with administering pro forma "payment" plans for years, a few European states, as well as the recent Colombian law, have essentially adopted the "fresh start" approach.[52] In Ireland, for example, the court has the power to decide whether or not to demand any future income payment from debtors via a "bankruptcy payment order."[53] In France and Luxembourg, recent amendments allow low-income debtors' cases to be routed to a "personal rehabilitation" procedure, in which an immediate discharge follows a brief evaluation

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[47] *Legislative Guide, supra* note 1, at 282.
[48] *See generally* World Bank, *supra* note 8, ¶¶ 262, 355-56; Johanna Niemi-Kiesiläinen, "Consumer Bankruptcy in Comparison: Do We Cure a Market Failure or a Social Problem?," 37 *Osgoode Hall L.J.* 473 (1999).
[49] McCormack et al., *supra* note 5, at 380.
[50] World Bank, *supra* note 8, ¶ 312.
[51] *See* Kilborn, *Expert Recommendations*, *supra* note 3, at 46-47; Kilborn, Two Decades, *supra* note 4, at 325.
[52] *See* Kilborn, Reflections, *supra* note 6, at 325-26
[53] Bankruptcy Act 1988 section 85D(1), as amended by PIA 2012 § 157 [Ireland].

and possible liquidation of the debtor's non-exempt assets.[54] Especially in France, this procedure has been invoked quite frequently, in more than 37% of cases in 2015 and more than 40% of cases in the first half of 2016.[55] The reformed Polish law goes one step further, allowing the court to confer a discharge immediately if the debtor's circumstances make it clear that no distribution to creditors can reasonably be expected.[56] Ironically, as these European systems were moving toward the US approach, the US system has tried to move in the opposite direction. US lawmakers have struggled with the challenge of separating "can pay" from "can't pay" debtors and demanding payment plans of the latter, but the infamous "means testing" resolution of that struggle has produced famously unsatisfying results.[57] A discussion of the futility of payment plans and the back-and-forth on this sensitive decision in the *Legislative Guide* would be very helpful to legislatures who are increasingly being called on to draw these lines.

2. Imposed Payment Plans—How Long?

If the European "good faith effort" approach is chosen, a range of other sticky questions require resolution, including two that virtually cry out for discussion in the *Legislative Guide*: How much time and how much payment is required for debtors to demonstrate a "good faith effort"? As to the timing part, the *Guide* notes fleetingly the "difficult issue" of "the length of time required to expire before the debtor can be discharged,"[58] but it offers no discussion of the torturous path of related legislative and judicial experience here.

Policymakers have wrestled for many years in setting the appropriate term for debtors to earn their discharge. The European Commission has recently begun pressing for a three-year maximum discharge period, but many European states remain resistant to reducing their longer required terms. In April 2015, an EU Commissioner contrasted the US and European approaches, noting "[a]s for natural persons, in the U.S. the average debt discharge period is less than one year, while in most EU countries it's between five and seven years," and praising the shorter period, as "[t]here is evidence which shows that shorter discharge periods allowed US households to recover more quickly from the crisis."[59] In late November 2016, the European Commission redoubled its emphasis on the three-year term by taking the extraordinary step of proposing a Directive which would compel Member States to establish three-year maximum discharge periods for individual debtors.[60]

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[54] *See* Jason J. Kilborn, "*La Responsabilisation de l'Economie:* What the United States Can Learn From the New French Law on Consumer Overindebtedness," 26 *Mich. J. Int'l L.* 619, 648-51, 65-60 (2005) [hereinafter Kilborn, France]; Kilborn, *Expert Recommendations*, *supra* note 3, at 49; Loi du 8 janvier 2013 concernant le surendettement et portant modification, arts. 16-22 [Luxembourg].
[55] Banque de France, *Indicateurs statistiques sur le surendettement à fin juin 2016*, https://www.banque-france.fr/uploads/tx_bdfgrandesdates/2016-06-statistiques-surendettement.pdf.
[56] Law on Insolvency and Restructuring art. 491[16] (as amended 2013) [Poland].
[57] *See* Jason J. Kilborn, "Still Chasing Chimeras But Finally Slaying Some Dragons in the Quest for Consumer Bankruptcy Reform," 25 *Loyola Consumer L. Rev.* 1, 3-13 (2012).
[58] *Legislative Guide, supra* note 1, at 39.
[59] Conference "Insolvency law in Europe: current trends and future perspectives" (Apr. 23, 2015), https://eu2015.lv/events/political-meetings/conference-insolvency-law-in-europe-current-trends-and-future-perspectives-2015-04-23.
[60] *Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU,* at 49, COM(2016) 723 final (22 Nov. 2016) (article 20).

Only a handful of European states now provide a discharge within three years, however. The Dutch law originally left the discharge period to judicial discretion, though judges chose a three-year term in so many cases[61] that this term was adopted as the statutory norm as of 2008.[62] The discharge term under the Latvian law began at seven years in 2008, reduced in 2010 to a unique sliding scale that provides a discharge after as little as one year, with a maximum of three-and-one-half years.[63] Ireland took a giant step in 2013 from a previous 12-year payment period, following which debtors *might* earn a discharge only if the court found such a result "reasonable and proper."[64] Now, Irish debtors earn an automatic, non-discretionary discharge three years after entry of the order opening their bankruptcy cases.[65] Also in 2013, Poland adopted a standard three-year discharge plan period, reduced from five in the original law.[66]

Other regimes remain above the three-year mark, despite years of chaotic reform on this issue. The enormously complex French system originally limited court-imposed payment plans to five years, *increased* to eight years from 1999-2003, then again to ten years until 2010, then back to eight years until 2016, when an ordinance reduced the maximum plan period to seven years.[67] In both Germany and Austria, a seven-year term was the original choice, which has been challenged as overly long from the very beginning.[68] The German discharge period was reduced to six years in 2001,[69] and in 2013, it was reduced further to five years for the relatively few debtors able to pay administrative costs, and to three years for debtors able to produce a 35% dividend for unsecured creditors.[70] The new Romanian system includes a sliding scale, as well: One year for a 50% dividend, three years for 40%, and five years if less than 40%.[71] Belgian legislators considered a seven-year period but reduced it to five at the last minute, without explanation.[72] Elsewhere in Europe, a five-year payment plan is standard, with the exception of Greece and Italy at four years.[73] In all of Scandinavia, five-year plans predominate,[74] though under a very recent Swedish reform, effective November 1, 2016, entrepreneurs will be subject to a standard three-year plan.[75] If the *Guide* could offer any perspective on which of these myriad approaches is most appropriate, much anguish by legislators and debtors could be avoided.

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[61] *See* Jason J. Kilborn, "The Hidden Life of Consumer Bankruptcy Reform: Danger Signs for the New U.S. Law From Unexpected Parallels in the Netherlands," 39 *Vand. J. Transnat'l L.* 77, 102 (2006) [hereinafter Kilborn, Netherlands].

[62] *See* Kilborn, Two Decades, *supra* note 4, at 320.

[63] *See* Goda Ambrasaite & Rimvydas Norkus, "Legal Aspects of Insolvency of Natural Persons in the Baltic States," 21 *Juridica Int'l* 176, 184 (2014); Kilborn, *Expert Recommendations*, *supra* note 3, at 51.

[64] *See* Oireachtas Lib. & Res. Svc., *Spotlight: Debt Part 2: Personal Debt and Consequences* 15 (issue no. 3, 2010).

[65] Bankruptcy Act 1988 § 85(1), as amended by PIA 2012 § 157 [Ireland].

[66] Law on Insolvency and Restructuring art. 491[15](1), 491[19](1) (as amended 2013) [Poland].

[67] *See* Kilborn, *Expert Recommendations*, *supra* note 3, at 51; Code de la consommation art. L. 732-3 [France].

[68] *See* Jason J. Kilborn, "The Innovative German Approach to Consumer Debt Relief: Revolutionary Changes in German Law, and Surprising Lessons for the United States," 24 *NW. J. Int'l L. & Bus.* 257, 282 (2004).

[69] *See id.* at 284.

[70] *See* Jan-Ocko Heuer, *Social Inclusion and Exclusion in European Consumer Bankruptcy Systems* 15-16 (2013).

[71] Law 151/2015 on Insolvency of Natural Persons arts. 72-73 (2015) [Romania].

[72] *See* Jason J. Kilborn, "Continuity, Change, and Innovation in Emerging Consumer Bankruptcy Systems: Belgium and Luxembourg," 14 *Am. Bankr. Inst. L. Rev.* 69, 87-88 (2006).

[73] *See* Katsas, *supra* note 38, at 266; Kilborn, Reflections, *supra* note 6, at 328.

[74] *See* Kilborn, *Expert Recommendations*, *supra* note 3, at 52.

[75] *See* Kronofogden, *Den 1 november ändras lagen om skuldsanering och det kommer en nu lag om skuldsanering för företagare* (May 19, 2016), https://www.kronofogden.se/51471.html.

3. Imposed Payment Plans—How Much?

Along with the duration of these payment plans, a particularly sensitive topic mentioned only obliquely in the *Legislative Guide* is how much payment to demand of debtors. Indeed, experience has shown that this is not even the appropriate question; rather, the issue is how much income will be reserved for the debtor's family support, with the remainder distributed to creditors. The *Guide* notes that insolvency laws generally exclude "assets necessary to satisfy the basic domestic needs of the debtor and his or her family,"[76] but it does not discuss the trouble modern systems have had in determining how much income to exclude. On this crucial issue, modern practices diverge widely, though convergence over time is again evident to a degree.

A particularly significant point of divergence is who makes this decision. Deferring to the discretionary judgment of courts or other case administrators has produced generally unsatisfying results. After commentators criticized the "scandalously low budgets" left to debtors in discretionary rulings by administrative commissions, French lawmakers adopted standard income exemptions as a minimum baseline.[77] In Sweden, statutory income exemptions were originally characterized as "guiding" in the determination of debtors' insolvency budgets, though they later became the *de jure* rule after having been the *de facto* choice of system administrators for years.[78] In Denmark, courts in different parts of the country construed the original "modest lifestyle" standard in troublingly divergent ways. Danish justice authorities ultimately intervened to impose a uniform statutory scheme for income exemption and "reasonable" household expenses, which greatly increased the budgets left most debtors.[79] A unique solution emerged in the path-breaking system in the Netherlands, which officially relegates debtors to 90% of the social assistance minimum income but allows judges to deviate upward from that standard. Dutch judges coordinated to develop a complex, written side-standard for determining these upward deviations, which has become the real, uniform law.[80]

Despite these lessons in the weaknesses of open discretion, several newer systems still leave it to the courts to define proper household budgets. The Greek law, even after numerous amendments over the past few years, still relies on unguided judicial discretion,[81] as do the amended laws in Poland,[82] Luxembourg,[83] Slovakia,[84] and Italy.[85] If the *Guide* offered some warning to these legislators about the known dangers of this approach, the unfortunate result for these systems and their struggling debtors might be avoided. While deferring to judicial or administrative "case-by-case" discretion might sound sensible, it has worked mischief time and again in the past several decades. The *Legislative Guide* could put legislators on the leading edge of this sharp learning curve by including some discussion and evaluation of this issue that has emerged as among the most important to individual debtors in modern insolvency policy.

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[76] *Legislative Guide, supra* note 1, at 80.
[77] *See* Kilborn, France, *supra* note 54, at 644.
[78] *See* Kilborn, Sweden, *supra* note 36, at 450-51.
[79] *See* Kilborn, Denmark, *supra* note 19, at 178.
[80] *See* Kilborn, Netherlands, *supra* note 61, at 98-101.
[81] *See* Katsas, *supra* note 38, at 266-67.
[82] Law on Insolvency and Restructuring art. 491[15](4) (as amended 2013) [Poland].
[83] *See* Kilborn, *Expert Recommendations*, *supra* note 3, at 57; Loi du 8 janvier 2013 concernant le surendettement et portant modification, art. 1 [Luxembourg].
[84] *See* Kilborn, *Expert Recommendations*, *supra* note 3, at 57.
[85] See Kilborn, Reflections, *supra* note 6, at 332.

The better practice here is for all debtors to be subject to the same, transparent, democratically established baseline of protected income. The more recent reform in Spain, for example, commits all debtors to the clear, uniform, statutory income exemption scheme.[86] As the European Economic and Social Committee urged, the standard should reflect a dignified human existence, rather than a bread-and-water punitive subsistence, reserving to debtors enough of their income "to live on decently day to day, the aim being to reintegrate [them] into economic and social life quickly."[87] In this vein, the recent Irish reform offers a useful model, urging courts to take heed of "any guidelines on reasonable living expenses issued by" the new Insolvency Service.[88] The Service developed sensitive, annually updated guidelines in consultation with a wide variety of sources, including focus groups asked to identify appropriate categories and amounts of expenditures for "neither a survival standard nor a standard for people in poverty; rather … a standard of living that should allow for people to engage in activities that are considered the norm for Irish society."[89]

III. Conclusion

If UNCITRAL is to modernize insolvency law and support sustainable development, it needs to address more fully the critical issues facing the other 99% of entrepreneurs suffering from financial distress. It is not sufficient to mention that these natural person debtors exist and face complex problems, but then proceed to concentrate on the appropriate structure of insolvency law for the 1% of corporate debtors. Sustainable success in international trade, including insolvency resolution, must be based on the success of the millions of small entrepreneurs who will be at the vanguard of advancing their national economies. These debtors and their families will be the engines driving future, sustainable economic growth, and they must be considered in determining the best structure for business law regimes. The *Legislative Guide* has for the past decade left lawmakers searching for solutions to the unique concerns of resolving these debtors' financial failure. Society has evolved, and so should the *Guide.* A deliberate discussion of these issues among the world's leading experts at UNCITRAL might produce durable solutions, but at the very least, it could signal the potential dangers of certain approaches and offer more holistic guidance on insolvency law for a new century.

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[86] Ley Concursal art. 178*bis* (2015), as amended by Law 25/2015 of July 25, 2015 [Spain].

[87] Opinion of the European Economic and Social Committee on 'Consumer protection and appropriate treatment of over-indebtedness to prevent social exclusion' (exploratory opinion), 2014 O.J. (C 311) 38, 39, 44-45.

[88] Bankruptcy Act 1988 section 85D(4), as amended by PIA 2012 § 157 [Ireland].

[89] Insolvency Service, *Guidelines on a reasonable standard of living and reasonable living expenses* 5-7, 16-30 (2013), http://www.isi.gov.ie/en/ISI/Guidelines_under_section%2023_June_13.pdf/Files/Guidelines_under_section%2023_June_13.pdf.