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NEW ZEALAND'S NO ASSET PROCEDURE: A FRESH START AT NO COST?

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A new procedure for insolvent individuals, known as the No Asset Procedure ('NAP'), was introduced into New Zealand law in 2007. This article outlines that the government's intention was to provide an alternative to bankruptcy for individuals whose circumstances were identified as not being adequately dealt under existing law. However, a 2011 Evaluation indicated many creditors and budget advisers were critical of NAP as failing to facilitate changes in spending and budgeting habits. Introducing mandatory financial literacy or budgeting courses would reinforce that NAP is an earned fresh start for debtors and may also increase the legitimacy of NAP in the eyes of society.

I NEW ZEALAND'S 'NO ASSET PROCEDURE'

A Introduction

A new procedure for insolvent individuals known as the 'No Asset Procedure' ('*NAP*') was introduced into New Zealand law in 2007 when the *Insolvency Act 2006* (NZ) came into force.[1] As this paper will discuss, the government's intention was to provide an alternative to bankruptcy for individuals whose circumstances had been identified as not being adequately dealt with by the existing bankruptcy regime. In 2001, the Ministry of Economic Development ('*MED*')[2] identified that changes had occurred in the composition of persons adjudicated as being bankrupt; with consumer credit-related issues, as opposed to sole trader or business-related debts as the primary cause of insolvency compared to when the law was last reviewed in the 1960s.[3] The MED's concern was that the bankruptcy regime was no longer an effective solution for individuals whose debt was due to consumer credit-related issues.[4] As, often, such individuals can do little to avoid more debt, the punitive restrictions of bankruptcy were 'considered less appropriate for individuals in these

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1 *Insolvency Act 2006* (NZ) brought into force on 3 December 2007 by the *Insolvency Act 2006 Commencement Order 2007* (NZ).

2 The MED was one of four government departments that ceased to exist from 1 July 2012 when it was incorporated into the Ministry of Business, Innovation and Employment.

3 New Zealand, Ministry of Economic Development, *Insolvency Law Review: Tier One Discussion Documents* (Wellington, 2001) 30.

4 Ibid 21.

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circumstances, which discourage them from becoming productive members of the society or improve their financial position.'[5] Accordingly, the NAP was introduced to provide such debtors with a better opportunity for a fresh start[6] as all debts, apart from certain excluded amounts, are wiped at the end of a 12-month period. The term 'consumer debtor' in this article will be used to refer to such debtors.

The first part of this paper considers the objectives behind the introduction of the NAP procedure into New Zealand law by identifying the gap between the insolvency procedures available before 2007 and the characteristics of this new class of debtors. The paper then reviews the legislative framework for NAP contained in the *Insolvency Act 2006* (NZ) and the impact of NAP since its inception. Finally, it evaluates the operation of the procedure and provides some suggestions for amendment.

B Existing Procedures

Prior to the enactment of the *Insolvency Act 2006* (NZ), the *Insolvency Act 1967* (NZ) governed the insolvency of individual debtors, although private compromises with creditors did occur under the *1967 Act* and continue to be an option under the current regime. The *1967 Act* contained two pre-bankruptcy alternatives for an insolvent individual.[7] First, a debtor could enter into a proposal for financial restructuring under Part XV of the *Insolvency Act 1967* (NZ), subject to the agreement of creditors. A proposal can include an offer to assign all or any of their property to a trustee, an offer to pay debts by instalments, an offer to compromise debts or an offer to pay debts at some time in the future. The proposal is required to be accompanied by a statement of affairs in a prescribed format and is filed at court, together with a security or a guarantee, if any. Once the proposal is filed and accepted by the court, a creditors meeting is called to decide whether to accept it. If accepted and approved by the court, a creditor is prohibited in respect of any debt covered by the proposal from enforcing payment or commencing legal proceedings or commencing a creditor's petition against the debtor. This procedure is retained in the *Insolvency Act 2006 (NZ)* in subpart 5 of Part 2 of the Act.

The second option available to a debtor is to apply for a summary instalment order ('SIO'). This order was filed in court and once approved, binds creditors for three years. Under the *Insolvency Act 1967* (NZ),[8] the total debts of the debtor were required to be less than $12,000. The order allows a debtor to pay debts in regular

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5 Office of the Minister of Commerce, Cabinet Paper to the Chair of the Cabinet Business Committee, *Insolvency Law Reform Bill: Approval for Introduction* (2005) [13].

6 Hon Lianne Dalziel, Minister of Commerce 'Insolvency Law Changes Announced' (Press release, 18 February 2003).

7 See Paul Heath, 'Consumer Bankruptcies: A New Zealand Perspective' (1999) 37 *Osgoode Hall Law Journal* 428, 434-438 for a discussion of the reforms contained in the *Insolvency Act 1967* (NZ).

8 *Insolvency Act 1967* (NZ) Part XVI.

instalments without the threat of further legal action in relation to those debts while the order is in force. This alternative also continues to be available to debtors under the *Insolvency Act 2006* (NZ), although the debtor's total unsecured debts (excluding any student loan balance) have been increased to not more than $40,000.[9] The Official Assignee has taken over the role of administering SIO's under the *Insolvency Act 2006* (NZ). A SIO usually lasts for 3 years, but may be extended in exceptional circumstances.

However, the main option for an insolvent debtor under the *Insolvency Act 1967* (NZ), like its predecessors, was bankruptcy. There has been a considerable history of bankruptcy laws in New Zealand,[10] with the first bankruptcy related ordinance enacted in 1844.[11] This was replaced by the more far-reaching *Bankruptcy Act 1867* (NZ), the *Bankruptcy Act 1883* (NZ) and the *Bankruptcy Act 1892* (NZ), which was 'substantially modelled on the prevailing legislation in the United Kingdom.'[12] After the enactment of a number of consolidating Acts, the *Insolvency Act 1967* (NZ) was passed. The term 'bankrupt' in the New Zealand context continues to describe the status of a natural person (not a corporate person) who, on the filing of a petition, either by the debtor or by one of the debtor's creditors, is adjudged bankrupt by the High Court. A 'natural person' is an individual, whether involved in trade such as a sole trader or in a partnership, or a consumer. On adjudication, all of the debtor's property is vested in the Official Assignee ('the *Assignee*'), and the bankrupt under New Zealand law is subject to conventional limitations on certain activities, such as obtaining credit, carrying on business and leaving the country, without the consent of the Assignee. A bankrupt in New Zealand is normally discharged three years after adjudication, unless the bankrupt receives approval for an earlier discharge by the court. The *Insolvency Act 2006* (NZ) retained bankruptcy as the primary remedy for an insolvent individual with some modifications. The *2006 Act* also retained the monopoly role of the State, through the New Zealand Insolvency and Trustee Service ('*NZITS*'), and more specifically, the Assignee, in the administration of the estates of bankrupt individuals.[13]

Accordingly, while the *Insolvency Act 1967* (NZ) provided alternatives to bankruptcy, underlying the availability of both the summary instalment order and debt repayment scheme options is an assumption that the debtor has some funds. However, for consumer debtors "whose liabilities are incurred primarily for private,

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9 *Insolvency Act 2006* (NZ) s 343(1)(a).

10 See Ivan A Hansen, *Bankruptcy: In the beginning—An historical survey of the laws of bankruptcy* (New Zealand Institute of Credit and Financial Management, 1980); Paul Heath and Michael Whale (eds), LexisNexis, *Heath and Whale on Insolvency* [2.1].

11 *Imprisonment for Debt Limitation Ordinance 1844* (NZ).

12 Heath and Whale, above n 10, [2.1].

13 For a discussion of the advantages of a contrary position whereby private insolvency experts administer estates, see New Zealand Law Commission, *Insolvency Law Reform: Promoting Trust and Confidence*, Study Paper No 11 (2001) 9.

family or householder purpose"[14] and who often have little or no assets or income, these alternatives to bankruptcy are unavailable. Consumer debtors often 'have a very limited ability to repay any debts, there is often very little action they can take to avoid bankruptcy (i.e. attain an SIO or negotiate a voluntary arrangement to repay the debt over time).'[15]

C Consumer Debtors

1 International Phenomena

The increasing number of consumer debtors is not a phenomenon unique to New Zealand. Internationally, the changing demographic of individual debtors has been identified in most western economies. This development has also generated a very substantial amount of research on the causes, characteristics and impacts of this change in the composition of debtors.[16] Burton observed that one consequence of the changing societal attitudes to credit is that access to credit has become a central feature of economic status, it legitimates citizens and thereby consumers, and those who are denied credit, are classified as inferior.[17]

More recently, there is an emerging body of research on the link between credit and consumption that argues that the underlying demand for credit is linked to societal changes to consumption.[18] Burton, for example, argues that 'credit underpins many aspects of consumption and has been instrumental in the development of what has become known as consumer society'.[19] Others who also research into the deregulation of financial institutions also argue that government action, or inaction, especially relating to the fringe market for financial services, has contributed to rising levels of consumer debt. Internationally, a number of studies have identified a relationship between the increasing number of consumer debtors and the lack of controls on the providers of consumer credit cards. Squires, after charting the rise of consumer debt in the United States in the second half of the twentieth century, observed that 'accompanying expansion of credit, sometimes by consumer choice,

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[14] INSOL International, 'Consumer Debt Report: Report of findings and recommendations' (INSOL International, London, 2001) 1.

[15] Office of the Minister of Commerce, Appendix One to the Regulatory Impact Statement of the Cabinet Paper to the Chair of the Cabinet Economic Development Committee, *Bankruptcy Administration: No Asset Procedure and Insolvency Act changes, Insolvency Law Reform Bill: Approval for Introduction* (December 2003) 12.

[16] See eg, Jason J Kilborn, *Comparative Consumer Bankruptcy* (Carolina Academic Press, 2007); Johanna Niemi-Kiesilainen, Iain Ramsay and William Whitford (eds), *Consumer Bankruptcy in Global Perspective* (Hart Publishing, 2003); Stephanie Ben-Ishai and Saul Schwartz, 'Bankruptcy for the Poor?' (2007) 45(3) *Osgoode Hall Law Journal* 471; Mary Wyburn, 'Debt Agreements for Consumers under Bankruptcy Law in Australia and Developing International Principles and Standards for Personal Insolvency' (2014) 23 *International Insolvency Review* 101, 112-116.

[17] Dawn Burton, *Credit and Consumer Society* (Routledge, 2008) 30.

[18] See eg, Kilborn, above n 16; Katherine Porter 'The Damage of Debt' (2012) *69 Washington & Lee Law Review* 979; Burton, above n 17.

[19] Burton, above n 17, 38.

sometimes in response to aggressive marketing by financial institutions, reflects restructuring of financial services in many ways.'[20] Ramsay commented that the lack of regulation over consumer lending practices, such as 'securitisation and computerised risk-based lending' and the accompanying dominance on neo-liberal ideology, may be included in an account for changes towards a credit culture in the United Kingdom.[21]

The World Bank's Insolvency and Creditor/Debtor Regimes Task Force ('*Task Force*') met for the first time in January 2011 to consider the topic of the insolvency of natural persons in the wake of the global financial crisis. The Task Force commented that individual countries have a 'diversity of policy perspectives, values, cultural preferences and legal traditions that shape the way that jurisdictions may choose to deal with the problems of individual over indebtedness.' The Task Force concluded however that 'recent events suggest that the expansion of access to finance, the extension modern modes of financial intermediation, and the mobility and globalization of financial flows may have changed the character and scale of the risk of consumer insolvency in similar ways in many different economies.'[22]

2 Changes in objectives of Insolvency law

The rise in consumer insolvency has forced changes to the focus of insolvency law. Historically, while benefits for creditors have constituted the primary objective of insolvency regimes, the rise in the number of non-business debtors has forced countries to focus on benefits for debtors and their families. Furthermore, more recently, there has been a move away from looking at the 'creditor-debtor relationship' in 'simple binary terms', with a third category of benefits identified. These are 'benefits redounding broadly to significant segments of wider society and to society as a whole.'[23] The 2013 Report on the Treatment of the Insolvency of Natural Persons that was produced by the Task Force ('*World Bank Report*') groups these benefits into two categories:[24]

> One category encompasses a variety of benefits associated with disciplining creditors to acknowledge the reality of their low-value claims against distressed debtors, internalize the costs of their own lax credit evaluation, and more effectively and fairly redistribute those costs among the society that benefits from the availability of credit. The other category focuses on the *intra*-national and *inter*-national benefits or maximizing

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[20] Gregory D Squires, 'Inequality and Access to Financial Services' in Johanna Niemi-Kiesilainen, Iain Ramsay and William Whitford (eds), *Consumer Credit, Debt and Bankruptcy: Comparative and International Perspectives* (Hart Publishing, 2009) 12.

[21] Iain Ramsay, 'Wannabe WAGS and Credit Binges: The construction of overindebtedness in the UK' in Niemi-Kiesilainen, Ramsay and Whitford (eds), above n 20, 75, 77.

[22] Working Group on the Treatment of the Insolvency of Natural Persons, 'Report on the Treatment of the Insolvency of Natural Persons' (Report, World Bank, 2013) [7]-[8].

[23] Ibid [57].

[24] Ibid [78].

engagement and productivity in debtors, especially in light of the increasingly competitive global marketplace.

The World Bank Report affirmed the value for a country to develop its insolvency regime to provide solutions for the increasing number of insolvent individuals. In this sense, the World Bank Report argues that since most western societies accept, if not encourage' the benefits of lending, the insolvency regime should be viewed as representing 'a sort of trade-off for deregulation of consumer lending. If natural persons are to be exposed to inevitable risk that they do not—and likely cannot—understand or avoid, insolvency restores fair equilibrium by offering insurances against those risks, with the "premiums" financed through small and appropriately distributed increases in the costs of credit.'[25]

A number of countries have enacted measures targeted at individual 'unfortunate debtors,'[26] being debtors who have been exposed to inevitable or unavoidable risk, in an attempt to rehabilitate such debtors to become again productive members of the economy and consumers.[27]

3 New Zealand

In the New Zealand context, as a consequence of the Labour-Alliance government's decision in 1999 to review New Zealand's insolvency law, the MED published in 2001 a Discussion Document ('*Discussion Document*').[28] The Discussion Document outlined the changing characteristics of a typical New Zealand bankrupt.[29] It identified that consumer debtors were increasing segment of the make-up of total bankrupts and contributed to '63 percent of all bankrupt estates for the year ending 31 December 1999.'[30] This change was also partly driven by the wave of privatisation and deregulation that had transmuted New Zealand, by the end of the 1990's, to be

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[25] Ibid.

[26] The term 'unfortunate debtor' was first used by Paul Rock, *Making People Pay* (Routledge, 1973) where he classified debtors as 'professional', 'feckless' or 'unfortunate'. His research concerned the optimum method of enforcement of debts, and observed that debt collectors adopt different sanctions for what he called was a "tripartite classification of debtors". A professional debtor, he classified, as someone who incurs debt, with no intention to repay, accordingly the default will be made at the beginning of the agreement. A feckless debtor is characterised as an individual is disorganised and irresponsible, whereas as an unfortunate debtor is one who will pay what the debtor can afford.

[27] See INSOL International, 'Consumer Debt Report: Report of Finding and Recommendations' (Report, INSOL International, 2001) <http://www.insol.org/pdf/consdebt.pdf>; and Niemi-Kiesilainen, Ramsay and Whitford (eds), above n 16. For an overview of the different legislative responses, see also the Working Group on the Treatment of the Insolvency of Natural Persons, above n 22.

[28] New Zealand, Ministry of Economic Development, *Insolvency Law Review: Tier One Discussion Documents* (2001).

[29] For a discussion of the characteristics of consumer bankruptcy in New Zealand in 1999, see also Heath, above n 7, 438-440.

[30] New Zealand, Ministry of Economic Development, *Insolvency Law Review: Tier One Discussion Documents* (2001) [5.3].

one the least regulated economies in the western world.[31] The Discussion Document also recorded that consumer debt generally consisted of unpaid utilities, tax, credit card debt and loans from finance companies or banks. Many consumer bankrupts were identified as long-term insolvent debtors, who had been able to avoid 'bankruptcy by managing their outgoings until some 'life event' occurs that interferes with their ability to meet their obligations.'[32] The Discussion Document referred to a recent survey of 1,208 bankrupts, where 472 (39%) identified loss of income or unemployment as the major cause of their bankruptcy. The causes of personal insolvency were also identified. These ranged from unavoidable cost of sensible risk-taking to dishonest and criminal conduct. With respect to consumer bankruptcy, access to credit and over-indebtedness were the most common factors.[33] Domestic discord or relationship breakdown was also a significant factor. Finally, NZITS statistics reported by the MED showed that almost 80% of bankrupt estates did not return a dividend to creditors, the majority began as debtor-filed petitions, that approximately 30% owned a credit card and approximately 50% were on some form of income support.

D Government Rationale for NAP

The 2001 Discussion Document did not contain a draft of the NAP or outline other possible options. Instead, it was limited to identifying the gap between the current bankruptcy procedures and the typical financial circumstances of consumer debtors. However, after consultation, in 2003 the Minister of Commerce announced that a decision had been made to adopt some form of alternative to bankruptcy which will 'provide consumer debtors with a better opportunity for a fresh start.'[34] In contrast, debtors who are adjudicated bankrupt are also afforded a 'fresh start', but generally this will not occur until three years after the start of the bankruptcy. The 'No Asset Procedure' as originally designed was a 12-month process, after which the debtor was discharged and the debtor's name was removed from the public register.

The Regulatory Impact Statement ('*RIS*'), which accompanied the Cabinet Paper that recorded the government's approval of the MED's draft NAP regime, set out the details of this consultation. It stated that 'targeted consultation was undertaken on the policy objectives and design of the procedure. Further, those groups consulted included consumer, low-income, and government agencies.'[35] Government agencies included the Ministry of Consumer Affairs, the Ministry of Social Development and

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31 New Zealand Law Commission, above n 13, 20-21. For an overview of the changing economic context, see also Heath, above n 7, 431-434; and Thomas GW Telfer, 'New Zealand Bankruptcy Law Reform: The new role of the Official Assignee and the Prospects for a No-Asset regime' in Niemi-Kiesilainen, Ramsay and Whitford (eds), above n 20, 249-251.

32 New Zealand Law Commission, above n 13.

33 The evidence for this assertion was provided by the Ministry of Consumer Affairs. See New Zealand, Ministry of Economic Development, *Insolvency Law Review: Tier One Discussion Documents* (2001) [5.3].

34 Hon Lianne Dalziel, above n 6.

35 Office of the Minister of Commerce, above n 15.

the Insolvency and Trustee Service.[36] Targeted private sector consultation with representatives of consumer and creditor groups on the policy objectives and the design of the procedure was also stated to have occurred.[37] The RIS stated that 'most support streamlining the current insolvency procedures by introducing an alternative to bankruptcy for consumer debtors.'[38] However, two financial lenders (namely, the Financial Services Federation and Fisher and Paykel Finance Ltd) were identified as unsupportive of a NAP. They viewed a NAP as a 'soft option' and were concerned that it will greatly lessen the threat of bankruptcy as a deterrent for debt repayment and also as a means to obtain payment.[39] However, the MED considered the threat of bankruptcy does not in fact act as a deterrent. The RIS stated that consumer debtors often can do little to avoid bankruptcy. This characterisation of the target debtor for the NAP as 'unfortunate', rather than reckless or fraudulent, also is reflected in the MED's conclusion that the target debtors were unlikely to abuse the procedure. The ability of the OA to decline a debtor's entry to the procedure, that creditors are able to lodge objections and that a debtor only has one opportunity to enter in a NAP were identified as sufficient measures to manage any risk of abuse.[40]

The Cabinet Paper, which recorded the Cabinet's approval of the NAP, identified the objectives of the procedure as follows:[41]

- to acknowledge that the debtor usually cannot avoid bankruptcy and therefore the punitive and deterrent aspects of the current regime are inappropriate and have limited relevance;
- to give the debtor the opportunity of a fresh start;
- to provide appropriate safeguards against the risk of abuse; and
- to provide a simple procedure that minimise administration costs to the state.

In terms of this last objective, the RIS stated that NAP would minimise the costs of administration for the State, with most of the cost savings arising through the shorter-duration of a NAP compared to bankruptcy, and that student loan debts are not

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[36] Ibid. In this document, it was recorded that the following government departments were consulted on the proposals in the paper: Treasury, Department for Courts, Ministry of Consumer Affairs, Ministry of Justice, Inland Revenue Department, Te Puni Kokiri, Ministry of Social Development, Ministry for Pacific Island Affairs, Ministry of Education, Study Link.

[37] Ibid. The following organisations were identified as The Joint Insolvency Committee: New Zealand Law Society and the Institute of Chartered Accountants; Carter Holt Harvey; Scott Panel and Hardware; CreditWorks Outsourcing Credit Management Solutions; Benchmark Building Supplies; Dun and Bradstreet New Zealand; Phillips Fox; New Zealand Universities Students Association; Financial Services Federation; Fisher & Paykel Finance Limited; New Zealand Federation of Family Budgeting Services (inc); Citizens Advice Bureaux; Youth Law; Law Commission.

[38] Ibid.

[39] Ibid.

[40] Ibid.

[41] Ibid.

discharged by a NAP. In terms of costs imposed on creditors, the RIS only identified the cost of compliance for creditors who chose to file an objection with the OA.

Subsequently, the *Insolvency Law Reform Bill 2005* (NZ)[42] was introduced into Parliament. The Explanatory Note also records additional benefits of the proposed introduction of the NAP. These include that for an insolvent individual, entering into a NAP will have a reduced social stigma and financial cost compared to bankruptcy. For society, the benefits of NAP were to encourage insolvent individuals (either subject to bankruptcy or NAP) to become (again) productive members of society.[43]

II THE NO ASSET PROCEDURE IN NEW ZEALAND LAW

A Eligibility

Eligibility for admission to the NAP is governed by s 363 of the *Insolvency Act 2006* (NZ). A debtor who satisfies the five eligibility criteria may apply to the Assignee for entry to NAP.[44] The application must be filed together with a statement of a debtor's affairs.[45] The Assignee, on receipt of the application and statement, may reject the application if, in the Assignee's opinion, either document is incomplete or incorrect. The New Zealand Insolvency Trustee Service ('*NZITS*') annually publishes insolvency statistics for each financial year for all insolvency procedures that NZITS administers. These statistics indicate that the leading reason NAP applications are rejected is an incomplete statement of affairs. In each of the six financial years from 1 July 2008 to 30 June 2014, between 30% and 64% of the total number of applications rejected were rejected, as shown in the following table:

Reasons why NAP rejected	**2008-09**	**2009-10**	**2010-11**	**2011-12**	**2012-13**	**2013-14**
Incomplete SOA	39%	30%	34%	43%	64%	53%

However, applications rejected for this reason may be resubmitted. It is unclear how

[42] The Insolvency Law Reform Bill 2005 (NZ) was divided by the *Supplementary Order Paper 2006* No 61 (NZ) into three Bills: the Insolvency Bill 2006 (NZ); the Companies Amendment Bill 2006 (NZ) and the Cross-Border Insolvency Bill 2006 (NZ).

[43] Explanatory Notes, Insolvency Law Reform Bill 2005 (NZ) 14.

[44] *Insolvency (Personal Insolvency) Regulations 2007* (NZ) reg 65 provides that an application for entry to the no asset procedure under section 362(1) must— (a) be addressed to the Assignee; and (b) state that the debtor applies for entry to the no asset procedure; and (c) be signed by the debtor; and (d) be dated. Further the application must contain the following information: (a) the debtor's full name: (b) the debtor's current address, telephone number, and any other contact details (such as a mobile telephone number or an email address): (c) the debtor's occupation: (d) the debtor's date of birth and be accompanied by a statement of affairs that complies with regulation 6.

[45] Ibid reg 6 sets out the contents of the statement of affairs applicable to bankruptcy, which also applies to an application for the no asset procedure.

many initially rejected applications are ultimately accepted by NZITS, as this information is not published.

After a completed application and statement of affairs is received, the Assignee then is required to check whether all of the five criteria in s 363 are satisfied. This section provides:

> **363 Criteria for entry to no asset procedure**
> (1) The Assignee may admit a debtor to the no asset procedure if the Assignee is satisfied on reasonable grounds that—
> (a) the debtor has no realisable assets; and
> (b) the debtor has not previously been admitted to the no asset procedure; and
> (c) the debtor has not previously been adjudicated bankrupt; and
> (d) the debtor has total debts (excluding any student loan balance) that are not less than $1,000 and not more than $40,000;[46] and
> (e) under a prescribed means test, the debtor does not have the means of repaying any amount towards those debts.

Although the policy documents surrounding the introduction of the NAP referred to the procedure being aimed at consumer debtors, the criteria in s 363(1) do not expressly refer to such debtors.[47] Brown and Telfer observe that instead of distinguishing between consumer and non-consumer debtors, the 'no asset procedure seeks to take a subset of debtors out of the bankruptcy procedure by screening for no asset debtors based on a number of listed criteria.'[48] Accordingly, entry into the procedure is limited to those who do not have the financial means to repay the debt immediately or in the short or medium term. NZITS Statistics show that failure to satisfy any one of these five criteria is another significant cause of the rejection of NAP applications as follows:[49]

Reason why rejected	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Realisable assets	16.7%	17.1%	19%	15%	5%	16%

[46] The total debt figure excludes any student loan, as student loans remain enforceable notwithstanding that a debtor has entered into a no asset procedure pursuant to the *Insolvency Act 2006* (NZ) s 369(2)(c).

[47] Some suggest that this may be due to the fact that the definition of consumer bankrupt is elusive in its own right: see David Brown and Thomas Telfer, *Personal and Corporate Insolvency Legislation: Guide and Commentary to the 2006 Amendments* (LexisNexis, 2nd ed, 2013) 39.

[48] Ibid.

[49] This table is based on public data released by the New Zealand Insolvency and Trustee Service in annual ITS Statistical Data Reports. Data in this table is based on the ITS Statistical Data Report 2008-2009; the ITS Statistical Data Report 2009-2010; the ITS Statistical Data Report 2010-2011; the ITS Statistical Data Report 2011-2012; ITS Statistical Data Report 2012-2013, and ITS Insolvency Statistics and Debtor Profile Report of 1 July 2013-30 June 2014. All statistics are accessible from the following website: <http://www.insolvency.govt.nz/cms/site-tools/about-us/statistics>.

Previous NAP	.06%	.29%	0	0	0	0
Previous bankruptcy	1.87%	2.8%	2.5%	3%	2%	3%
Debts over 40K	27.7%	28.9%	29%	18%	13%	14%
Means to repay	6.8%	6.4%	3.5%	5%	7%	7%
Total% of NAP rejected[50]	**53.13%**	**55.49%**	**54%**	**41%**	**27%**	**40%**

Section 363(2) provides additional clarification of the term 'realisable assets'. Realisable assets for the purposes of NAP, does not include the assets that a bankrupt is allowed to retain under section 158. A 2009 amendment to the regime excluded from the definition of 'realisable assets' any assets (for example, gifted assets) that might be recoverable by the assignee if the debtor was adjudicated bankrupt on the date of application for entry to the NAP and if the irregular transaction provisions in subpart 7 of Part 3 of the *Insolvency Act 2006* (NZ) apply.[51] Section 158 applies to bankrupts and provides that a bankrupt may choose to retain as the bankrupt's own property certain assets up to a maximum value. These assets include the bankrupt's necessary tools of trade and necessary household furniture and effects; with the maximum value of such items being fixed at the discretion of the assignee. In addition, the bankrupt may retain a motor vehicle with a maximum value of $5000.[52] Bankrupts are also entitled to retain any necessary tools of trade and furniture and effects which are worth more than the maximum value, if creditors consent by an ordinary resolution.[53]

The total debt parameters of an amount owing between $1000 and $40,000 may be varied by Order in Council to take account of increases in the Consumer Price Index.[54] To date, no variation has occurred. Interestingly, although a finding that an applicant's debts exceeds $40,000 is one of the leading reasons for rejection of a NAP application, the percentage has decreased from around 28% in the first three years of the procedure to only 13% of applications in the reporting year 2012-2013 and 14% in 2013-2014. This would seem to indicate that there is no significant pressure to increase the $40,000 debt maximum. Finally, with respect to the fifth criteria, namely that under a prescribed means test, the debtor is unable to repay his or her debts, the *Insolvency (Personal Insolvency) Regulations 2007* (NZ) provides

[50] NAP applications were also rejected for unspecified 'other' grounds and that the application was withdrawn.
[51] *Insolvency Amendment Act 2009* (NZ) s 7.
[52] *Insolvency Act 2006* (NZ) s 158(3).
[53] Ibid s 159.
[54] Ibid s 363(3).

that for the purposes of this means test, the income of the debtor personally and that of any relatives with whom the debtor lives must be taken into account in determining if a debtor has a surplus of money, after paying the household's usual and reasonable living expenses.[55] Not surprisingly, the NZITS website does not provide the actual guidelines used by the Service to determine whether an individual has the ability to repay debts, but a budget form to be used available on the NZITS website requires disclosure of full details of all net household income and all costs from household, travel, family and general sources. The underlying question appears to be whether the debtor has 'any net disposal income.'[56] The impact of the means test is that persons who are employed are often ineligible for NAP, because they are in a position to make on-going contributions towards their debts. For this reason, NAP debtors predominately are less likely to be employed than debtors under either of the alternative insolvency procedures.[57]

In addition, even if a debtor does satisfy all of the s 363(1) criteria, a debtor may still be disqualified from the NAP under one of the grounds set out in s 364. This section provides that the Assignee must not admit a debtor to the procedure if the Assignee is satisfied on reasonable grounds that:

> (a) the debtor has concealed assets with the intention of defrauding his or her creditors, for example, by transferring property to a trust; or
> (b) the debtor has engaged in conduct that would, if the bankrupt were adjudicated bankrupt, constitute an offence under this Act; or
> (c) the debtor has incurred a debt or debts knowing that the debtor does not have the means to repay them; or
> (d) a creditor intends applying for the debtor's adjudication as a bankrupt and it is likely that the outcome for the creditor if the debtor is adjudicated bankrupt will be materially better than if the debtor is admitted to the no asset procedure.

The NZITS statistics for last the six financial years indicate that only a very small number of applications were rejected for any of these reasons;[58] a finding that appears to indicate that few debtors are attempting to abuse the procedure. A debtor's application will also be unsuccessful if the debtor has already used the NAP procedure or have previously been bankrupt.[59]

B Moratorium and impact of NAP

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55 *Insolvency (Personal Insolvency) Regulations 2007* (NZ) reg 66.

56 David Brown, 'The Financial Health Benefits of a quick 'NAP' - New Zealand Solutions to Consumer Insolvency?' (Paper presented at the INSOL Conference Academic Programme, Vancouver, 20 June 2009) 10.

57 For example, for the reporting year 2012-2013 only 17% of debtors recorded themselves as employed in their Statement of Affairs, and in 2013-2014 this percentage was recorded as 20% of all NAP debtors.

58 For details of the source of these statistics, see: <http://www.insolvency.govt.nz/cms/site-tools/about-us/statistics>.

59 *Insolvency Act 2006* (NZ) s 363(1)(b)-(c).

Once a person has been admitted to the NAP, there is a moratorium on his or her debts.[60] Similar to bankruptcy, there are restrictions placed on a debtor who is admitted to the NAP on obtaining credit without first informing the credit provider that the debtor is subject to a NAP. However, in contrast to bankruptcy and in line with the rehabilitation objective of NAP, debtors in NAP can be directors or involved in the management of a business. A NAP can be terminated during the 12 months, with the most common ground for such termination identified as having debts over $40,000. Between 1 and 2 percent of NAPs were terminated each year in the five financial years identified above.[61] After 12 months, a debtor is discharged from NAP and from liability for all debts, other than in certain exceptions that are discussed below.

The procedure does not require a debtor to undergo any financial literacy or budgeting skills courses as a pre-condition of discharge. The rationale is that the NAP was designed to meet the situation of the 'unfortunate' debtor, whose debt has arisen from circumstances such as loss of employment, relationship break-up or some unforeseen life event. Such debtors have managed financially up to the tipping point into over-indebtedness and therefore the regime does not require a pre-condition of discharge that the debtor completes such courses.

Student loans are neither provable nor dischargeable with the NAP, because the NAP has a 'less punitive effect than bankruptcy'. All other debts (apart from debts that are non-dischargeable in bankruptcy, such as child maintenance orders) are dischargeable through NAP. In 2009, the *Insolvency Act 2006* (NZ) was amended to ensure that if a debtor commits an offence when in NAP, such as obtaining credit by false representation, the fraudulent debt is not written off upon discharge. Specifically, s 377A(3) clarifies that such a debt becomes enforceable again once the debtor is discharged from the NAP, and that the debtor is liable to pay interest and penalties accrued during the procedure. Finally, the regime also provides a right of appeal, by way of judicial review of the decisions of the Official Assignee.

Once a NAP has been discharged, the debtor's name remains on a public register for four years. When the *Insolvency Act 2006* (NZ) was originally enacted, information about a debtor in NAP was on a public register only until discharge. As discussed below, in 2009 this rule was amended by the adoption of the one + four system for information on a public register.

III UPTAKE OF NAP[62]

As the *Insolvency Act 2006* (NZ) took effect from 3 December 2007, the data for the 2007-2008 financial year only included approximately 7 months when the NAP

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60 Ibid s 369.

61 For details of the source of these statistics, see: <http://www.insolvency.govt.nz/cms/site-tools/about-us/statistics>.

62 Ibid.

procedure was available as an alternative to bankruptcy. Accordingly, the total number of accepted NAP applications was only 32% of the total number of insolvency procedures dealt with by the NZITS during the financial year 2007-2008. The balance was made up of bankruptcies, either as a result of an application by a creditor or the debtor, and SIOs.

In the 2008-09 financial year, the percentage of NAPs in relation to total insolvency procedures (the total of bankruptcy adjudications, SIOs and no NAPs) increased to 50%. However, since then the percentage of NAPs has decreased to 36% for the financial year ending 30 June 2013, although this percentage has increased 39.3% for the 2013-2014 year. In actual numbers accepted into a NAP, the highest number was in the 2009-2010 financial year, when 3026 were accepted into the procedure. In 2012-2013, this number had dropped to only 1449, although this decrease reflects not only a reduction in the relative number of debtors adopting the NAP, but also a significant drop in the number of insolvency procedures overall. This decrease in accepted NAP applications appears to be continuing, although this drop in accepted applications is in line with a continuing overall decline in the total insolvency procedures for this period. The compiled NZITS Report for the 2013-14 financial year states that only 1145 were accepted during this period.

In terms of SIOs, although the initial take up when it was amended from 3 December 2007 reflects in part the same initial trajectory as the NAP, since 2007 the number as a percentage of the total insolvency volume has risen from 1% to 8% in 2012-13 and to 10.25% in 2013-14.

When reviewing the incidence of bankruptcy from 2000 onward, it is clear that the introduction of NAP had the greatest impact on debtor application bankruptcy. For example, in the 2005-2006 financial year, debtor applications contributed 80.4% of the total personal insolvency volume, with creditor application bankruptcy making up the balance.[63] With the introduction of both NAP and SIO, the number of bankruptcies, especially debtor-initiated applications, significantly dropped to around 30% of the total volume; although in the 2012-13 financial year, such applications contributed 32% by volume to the total number of applications. Interestingly, creditor application bankruptcies since 2000 have slowly been decreasing from approximately 31% of total insolvencies to less than 20% by the 2006-07 financial year. Since the respective introductions of NAP and SIO, this percentage decreased to approximately 16% in 2009-10 and 2010-11, but in the last 3 years has slowly increased to 23.2% in 2012-13. In the 2013-14 financial year, this percentage has increased to 40%.

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[63] New Zealand Insolvency and Trustee Service, *ITS Statistical Data Report 2005-2006* <http://www.insolvency.govt.nz/cms/site-tools/about-us/statistics/statistical-data-reports/itsstatisticaldatareport05-06.pdf/view>. Note that prior to the enactment of the *Insolvency Act 2006 (*NZ), Summary Instalment Orders were not administered by the Assignee. Accordingly, the number of such Orders was not included in the statistics published by NZITS.

Although the total annual number of personal insolvencies was reasonably fluid during the 1990's, between 2000 amd 2006 it was more stable, and ranged from a low in 2003/04 of 2792, to a high of 3087 in 2005/06. The total number then steadily increased to 5654 in 2009/09, and then to 6426 in 2009/10. The NZITS statistics do not provide any explanation for this increase, but it likely reflects the impact of the global financial crisis, as well as both the inclusion of the 2007 SIO numbers in the total figure and the possibility that some debtors may have entered into NAP instead of negotiating with creditors.[64] Since mid-2010, the total personal insolvency figure has decreased to only 3950 in the 2012-13 financial year, and then to 3433 in the 2013-14 financial year.

IV EVALUATION OF THE NO ASSET PROCEDURE

A The Insolvency Amendment Act 2009

The first government led review of the operation of the Insolvency Act 2006, including the NAP regime occurred in 2009 and led to the enactment of the *Insolvency Amendment Act 2009* (NZ).[65] In addition to the change discussed above, allowing debts incurred fraudulently to be recovered after the debtor has been discharged from a NAP, the other significant amendment to the NAP regime was the decision to increase the period of time that the name of a NAP debtor is on a public register. The 2009 amendment increased this time-period to a total of five years, consisting of the one year while subject to NAP and four years post-discharge.

The 'one-year' period was controversial when the NAP was first debated in the House of Representatives in 2006. The National Party, which was then in opposition, considered the 12-month discharge period undermined 'personal responsibility' and did not take into account the interests of creditors whose debt is wiped. As Kate Wilkinson stated during the second reading of the Bill, 'Insolvency laws should balance the responsibility for failure and opportunity to start again. But they should also never forget the creditors.'[66]

The enactment of one + four-year record on a public register in 2009 was after a change in government and the National Party was in power. The MED briefing to the Commerce Select Committee outlined four grounds for the change in time-period and illustrates the change in policy to the NAP. These grounds were to not disadvantage

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[64] See Ministry of Economic Development, New Zealand, *Evaluation of the No Asset Procedure: Final Report* (2011) [4.1] <http://www.med.govt.nz/about-us/publications/publications-by-topic/evaluation-of-government-programmes/NAP-final-report-july-2011.pdf>. This document reported that some creditors considered that in the absence of NAP, debtors would have been encouraged to attempt to manage difficult situations and pay debt. That the cost displaced across the economy by NAP may be costs that might not otherwise have occurred without the policy intervention of NAP.

[65] This Act came into force on 17 November 2009.

[66] New Zealand, *Parliamentary Debates*, House of Representatives, 26 October 2006 (Kate Wilkinson MP).

creditors' access to information to make prudent business decisions; that prudent business decisions would reduce any costs being passed to other consumers; that it would limit the perception that NAP is too debtor-friendly and that debtors would not be deprived of access to credit, but the cost of credit would reflect any risk they pose to the potential lender.[67] The Report on the Insolvency Amendment Bill prepared by the MED states this change of focus in the following way:[68]

> The State grants individuals who are discharged from NAP the privilege of becoming debt-free after only year. Creditors are entitled to get something valuable in return, which is reliable information about debtors' insolvencies for a reasonable amount of time as a means of ascertaining creditworthiness.

There is no doubt that this change diluted the underlying 'clean slate' objective of the NAP as originally introduced. This amendment, together with changes to the treatment of gifts received by a debtor during a NAP, aligned NAP more closely with bankruptcy and its associated social stigma.

INSOL in 2001 had cautioned that while discharge from debt will be the desired objective for most consumer debtors, discharge 'should however not be seen as an easy way out.'[69] Further for the:[70]

> law to be respected, legislators should seek to avoid a dichotomy between the debtor and society. The barriers to obtain a discharge should on the one hand not be so high that the debtor is discouraged from using the procedure. On the other hand, sufficient recognition of the system should be created so that society is willing to forgive and permit a fresh start.

Although the number of persons entering into NAP has dropped since the 2008-2009 highpoint of 50% of total insolvency procedures, in the last three years the relative number of NAPs has steadied to range between 36% to 40% of total procedures. This indicates that the change from 12 months to five years on the public register has not significantly deterred persons from using the procedure. However, given that for these three years, on average over 60% of the debts levels of those who used the NAP were under $20,000, the stigma of appearing on the public record does appear to be a high cost for those who use the procedure for their 'fresh start'.[71]

B 2011 Ministry of Economic Development Evaluation of the No Asset Procedure

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67 Lisa Barrett, 'Insolvency Amendment Bill' (Briefing to Commerce Select Committee, New Zealand Parliament, 2009) [11] <http://www.parliament.nz/resource/0000170483>.

68 Commerce Select Committee, New Zealand Parliament, *Officials' Report on the Insolvency Amendment Bill* (2009) [34].

69 INSOL International, above n 14, 6.

70 Ibid.

71 See Brown, above n 56, 19.

In 2011, the MED carried out a more detailed review of NAP, although it was relatively limited in scope. The Report prepared by the Evaluation Team of the MED and titled *Evaluation of the No Asset Procedure—Final Report* (‘*2011 Evaluation*’) only focused on four aspects of NAP. These were (a) the cost-effectiveness of NAP compared to other options; (b) the impact of the scheme on users; (c) the reach and uptake of NAP and (d) the quality of the scheme administration.[72] The methodology used for the evaluation included surveys of NAP debtors[73] and budget advisors, focus groups with budget advisors and selective interviews with creditors, banks and financial institutions. Overall, the 2011 Evaluation found that for debtors in genuine, unmanageable debt situations, there are real social and economic benefits from NAP.[74] Budget advisers also saw the benefit of NAP, with 93% of those surveyed rating NAP as a worthwhile government policy.[75]

However, many ‘budget advisers reported frustration that the longer-terms strategies for financial management, such a financial literacy and budgeting courses, were dispensed with once the immediate debt situation was resolved with some NAP debtors.’[76] Also, many creditors viewed the benefits of NAP as one sided and largely to their disadvantage. Although, clearly some of the debt written off under NAP would likely have been unrecoverable under other procedures, creditors were critical of the lack of compensatory procedures to promote fiscal responsibility.

In terms of the cost effectiveness of NAP, originally the MED had forecast net fiscal savings to the government, mainly though the retention of student loan liabilities, that otherwise would be written off under bankruptcy. Also, the NZITS would be required to spend fewer resources on NAPs, in comparison to bankruptcy, due to their shorter duration. A number of the creditors reported high costs with NAP, brought about by the need to identify NAP clients and then writing off and closing accounts. The 2011 Evaluation states that these costs are significant. In addition, significant unanticipated and unintended costs to other parts of government, including administration costs to the Ministry of Social Development and the Inland Revenue were identified.[77]

Also, evidence of misuse and gaming behaviour was reported by some creditors. Both government and commercial creditors reported that they had observed behaviour such as last minute spending in the period just prior to the NAP application.[78] However, the MED was unable to identify whether the reason for such spending was due to

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72 See Ministry of Economic Development, above n 64.
73 Ibid. Footnote 7 states that the survey was sent to NAP debtors between 2007 and June 2010, who provided an email address in their statement of affairs. The respondents were those who had internet access. This difference may partially explain why the demographics of the respondents differed from the NAP population as a whole over the time period.
74 Ibid [2.5].
75 Ibid 3.
76 Ibid [4.1].
77 Ibid [5.4].
78 Ibid [4.1].

difficult financial problems becoming more uncontrollable or premeditated last-minute purchases in the knowledge that a NAP application was pending.

The 2011 Evaluation made a number of suggestions to mitigate the potential for moral hazard, including eliminating debts from NAP which were incurred in the 6 months prior to an application or extending the time period over which debtors who come into means of repayment should be expected to pay debts. Another suggestion was that the NAP procedure should last for longer than 12 months to encourage better financial management practices for debtors, as the current discharge period encourages short term thinking. A number of budget advisers compared NAP to SIO and bankruptcy, which last longer and are 'better at facilitating change in spending and budgeting habits, encourage responsibility for financial decisions and mistakes and preventing gaming behaviour.'[79] Many creditors had also formed a view that NAP allows debtors to easily exit responsibilities or consequences arising from previous irresponsible spending behaviour, without sufficient incentives to encourage NAP debtors to learn from their mistakes or change behaviour.[80]

C World Bank Report on the Insolvency of Natural Persons

The recent World Bank Report[81] affirms that effective rehabilitation may require some measures that attempt to educate debtors. This Report identifies that one of the principal purposes of an insolvency system for natural persons is to re-establish the debtor's economic capability; that is, the debtor's 'economic rehabilitation'. The Report identified that there are three requisite elements for effective rehabilitation, as follows:[82]

> First, the debtor has to be freed from excessive debt. …Second, the debtor should be treated on an equal basis with non-debtors after receiving relief (the principle of non-discrimination). Third, the debtor should be able to avoid become excessively indebted again in the future, which may require some attempt to change debtors' attitudes concerning proper credit use.

V CONCLUSION

The NAP procedure has now been operating for over 7 years in New Zealand. It was designed to offer a fresh start to certain debtors where bankruptcy and other insolvency procedures were considered to be either an excessive response or unavailable. As the NAP procedure has been predominately been used by persons who were unemployed or on some other form of benefit, it can be seen as a success.[83]

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79 Ibid.
80 Ibid.
81 Working Group on the Treatment of the Insolvency of Natural Persons, above n 22.
82 Ibid [359].
83 See Hermie Coetzee and Melanie Roestoff, 'Consumer Debt Relief in South Africa—Should the Insolvency System provide for NINA debtors? Lessons from New Zealand' (2013) 22

However, one of the weaknesses of the NAP regime is that it was designed to deal with the situation of the 'unfortunate' debtor. Such debtors were characterised as having managed financially up to the tipping point into over-indebtedness and therefore the regime does not require a pre-condition of discharge that the debtor completes financial literacy or budgeting skills courses. This characterisation is not completely supported by the NZITS statistics, in that debtors in the 20-30 year age-group over the six financial years considered in this article generally accounted for between 25 and 30% of the total debtors entering into NAP.[84] The 2013 World Bank Report stated that for rehabilitation to be effective, it not only requires debt relief, but also that the rehabilitation may require some attempt to change a debtor's attitudes concerning the proper use of credit. The 2011 MED Evaluation indicated that many creditors and budget advisers were critical of NAP for its failure to facilitate changes in spending and budgeting habits. The brevity of the 12-month NAP procedure and the absence of mandated budgeting or financial literacy course potentially were identified as challenges to the success of NAP in terms of the objective of economic rehabilitation. It is recommended that the NAP be amended to require mandatory participation in such courses as a pre-condition of discharge. The completion of an 'earned' fresh start would not only encourage changes in behaviour, but may also increase the legitimacy of NAP in the eyes of society. Increasing the perceived legitimacy of the procedure may operate to influence policy makers to remove NAP debtors from the public record after discharge. This change should assist the achievement of a level playing field in which debtors are treated on the same basis as non-debtors after discharge. This would ensure that the NAP in New Zealand provides all three elements for effective rehabilitation.

International Insolvency Review 188, where the New Zealand 'No Asset Procedure' is argued as a possible model for South Africa.

84 New Zealand residential population statistics indicate that in the residential population aged 15 and over, 18% of the population are aged between 20 and 29: see Statistics New Zealand, *Demographic Trends: 2011* (2012) <http://www.stats.govt.nz/browse_for_stats/population/estimates_and_projections/demographic-trends-2011.aspx>.