Relieving Consumer Overindebtedness in South Africa: Policy Reviews and Recommendations

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A large fraction of South African consumers are highly leveraged, inadequately insured, and/or own little to no assets of value, which increases their exposure not only to idiosyncratic risk but also to severe indebtedness and/or default. This scenario can present negative ramifications that lead well beyond the confines of individual households. Thankfully, it can also be remedied by well-tailored legal debt relief mechanisms. This article reflects on the uncertainties surrounding the consumer debt relief framework of the National Credit Act in an attempt to show why it is not up to the challenge of providing meaningful relief to debt-distressed consumers. Ultimately, a comprehensive review of the current framework in favor of a discharge mechanism on simple, stated terms is proposed.

Keywords: debt relief, debt review, discharge, fresh start, National Credit Act (NCA), overindebtedness

Consumer credit has become an important facet of the South African household sector's welfare, and although it continues to boost consumption possibilities for many families, it is also a source of financial distress for many others with a background of stagnant or declining incomes. A large fraction of consumers make consumption choices subject to overwhelming material constraints, so when they find themselves with more debt than they can afford to pay, theirs and their dependents' socioeconomic functioning is likely to be severely impaired and several negative knock-on effects may yet come into play including impairment in future access to borrowing because of deteriorating credit ratings and overall disruptions in work and family life as well as stress-induced health problems (Archuleta, Dale, & Spann, 2013; Hojman, Miranda, & Ruiz-Tagle, 2013; O'Neill et al., 2006).

It has been argued that notwithstanding the lending and borrowing behaviors, consumer debt problems can be an inevitable feature of the credit system because of the concomitance of unfortunate events (Getter, 2003; van Apeldoorn, 2008; Viimsalu, 2010). Empirical studies conducted in South Africa appear to suggest that unfortunate stressor events beyond consumers' and/or lenders' control (e.g., job losses, illnesses/death or family breakdowns) play a big part not only in the accumulation of most debts (e.g., Collins & Leibbrandt, 2007; FinScope, 2015) but also in the erosion of the debt repayment capacity especially by disrupting income streams (Ssebagala, 2016). For instance, Collins and Leibbrandt (2007) find that the costs associated with death and funerals dominate the financial behaviors of a significant portion of the household sector, whereas a significant majority, according to FinScope (2015), borrows to make ends meet without intent to overconsume. Like in South Africa, studies elsewhere have suggested that these factors are the most common causes of debt problems worldwide (e.g., Getter, 2003; Keese, 2009) and have been widely invoked to rationalize regulatory interventions to alleviate consumer indebtedness, both as a consumer protection mechanism and a form of consumption insurance (Pace & Lown, 2016; White, 2007).

It is useful to note that consumer debt problems can also result from irrational credit practices (e.g., Anderloni & Vandone, 2011), and this is addressed via a separate set of legislation (which is outside the scope of this discussion) which is basically preventive rather than curative and essentially aims to influence pre-contractual behaviors and decision making—for instance, disclosure, education, or reckless lending statutes (Kelly-Louw, 2009; Lee & Hogarth, 1999; Renke, 2011; Stoop, 2009). Although preventive regulations might create a clean environment for

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credit contracting, they are unlikely to control for debtors' post-contractual situational changes and therefore unlikely to prevent financial distress that might result from such changes. The need for alleviative interventions may then become more apparent, inter alia as an antidote to such unanticipated adverse changes.

The South African National Credit Act 34 of 2005 (NCA; Department of Trade and Industry [DTI], 2006) introduced the debt review and restructuring provisions (Sections 85–87) for the alleviation of debt problems of natural persons "based on the principle of satisfaction by the consumer of all responsible financial obligations" (NCA, Section 3[g] and [i]). The process essentially entails a petition to have a debt counselor evaluate and declare the applicant overindebted (in a prescribed manner and form) so that the court may rearrange his or her obligations either by extending the period of the agreement; reducing the amount of installments, interest and fees payable; and/or postponing the dates on which payments are due. Although this mechanism is a great improvement to its predecessors (Otto, 2009), it is fraught with its own problems, notably, the lack of solid provisions on discharge, its inability to override cumbersome preexisting overlapping regulations, and lack of clarity on other pertinent issues. This article analyzes these provisions and the major issues surrounding them with the aim of providing an understanding as to why these might not be up to the challenge of providing meaningful relief and rehabilitation for consumers. In the end, comprehensive reforms to the law are proposed while taking stock of recent developments in the discourse on the treatment of personal insolvency within the framework of the "fresh start"—note that this work should not be construed as a comparative analysis of the different legal systems out there.

The analysis begins with the rationale for consumer debt relief, reflecting on the pathways to consumer overindebtedness, its effect on consumers' well-being, and the benefits of implementing legal relief measures. This is followed by an introduction of the NCA's approach to relief and its perceived caveats and then followed by a brief reflection on the lessons policymakers can glean from the recent developments in treatment consumer insolvencies, particularly drawing on the World Bank's 2013 report and the American approach, and then regulatory recommendations are offered. Throughout this article, the terms *insolvency*, *overindebtedness*, and *debt distress* are mutually interchangeable to mean a situation in which debtors are unable to continue paying their due debts or appear to have no reasonable prospect of doing so, without causing undue strain on their personal or family welfare (NCA, Section 86[7]).

The Rationale for Consumer Debt Relief

> Making it harder for over-indebted consumers to avoid repaying their debts is easily justifiable if purchases of iPods, plasma TVs, Hummers, or sable fur coats cause most consumer over-indebtedness. But empirical data collected by prominent U.S. academics show this is not the case; medical debts, a divorce, or a job interruption cause most consumer bankruptcies . . . (Dickerson, 2008, p. 146)

Both the causes and effects of overindebtedness can sufficiently rationalize the need for regulatory intervention to relieve consumers of excessive debt, and the earlier statement explains this rationale in the narrowest sense, regarding the pathways to debt distress. It speaks to an individual for whom the inadequacies of state social welfare and private insurance renders him or her so financially vulnerable that even mild interruptions to income streams may have large and lasting effects on well-being, economic stability, and, ultimately, debt sustainability. Similarly, there is a presumption of an unfortunate consumer forced into debt by social circumstances he cannot control, someone in need of the state's legal protection, so he or she can return to a productive life (Kilborn, 2008; Reifner, Niemi-Kiesiläinen, Huls, & Springeneer, 2010). Imagine a consumer "down on his/her luck after getting sick and losing a job, using credit cards to pay medical bills and make ends meet" (Pace & Lown, 2016, p. 315).

The alternative view is that the democratization of credit has increased open access to borrowing even among higher risk borrowers (Dickerson, 2008; Livshits, Macgee, & Tertilt, 2016), but the legal innovations introduced to ameliorate the risks of open access often play a pervasive role. For instance, information disclosure regulations appear to increase the extension of credit to riskier borrowers (Livshits et al., 2016) or bestow a sense of legitimacy on predatory lenders (Reifner, 2009) and in the end, even some of the most careful consumers will wind up hopelessly in debt. Thus, consumer debt relief regulations are necessary to insure society against the risk of such failures (Kilborn, 2008).

Regarding the effects of overindebtedness, the rationale is based on the premise that leaving consumers in a perpetual state of debt distress is likely to lead to further deterioration in theirs and their dependents' overall well-being and therefore, the overindebted would appreciate a new opportunity to start over (van Apeldoorn, 2008). Some of the risks may include diminished productivity, sociopsychological problems, or exclusion from social settings (Hojman et al., 2013; O'Neill et al., 2006; Rueger, Schneider, Zier, Letzel, & Muenster, 2011). It may also engender more dangerous coping mechanisms including borrowing from more dangerous, often underground sources, liquidation of valuables, and antisocial behaviors or relationship breakdowns especially as frustrations come to a head (Patel, Balmer, & Pleasence, 2012).

On the broader policy perspective, the driving concerns behind a consumer insolvency regime are about amending the negative systemic effects of unregulated distressed debt so as to tap into the benefits that flow from debtors, creditors, and society which include reducing wasteful collection costs, encouraging responsible lending, and reducing social costs of negative shock (World Bank, 2013). However, on the social standpoint, the overarching benefit is the premise of a financial fresh start to enable overindebted consumers to rebuild their lives and the ability to allocate the risks of financial distress among those best suited to spread them (Oei, 2014).

In terms of context, South Africa is a proper case study for rationalizing a consumer insolvency regime in the mold of the fresh start and might even be more relevant here than it is in many of those countries where it is already an established law. Here, in spite of the strict preventive provisions of the NCA, many still borrow from lenders of ill repute (e.g., James, 2013), while reckless lending (which the NCA narrowly defines as the act of granting debt to someone who cannot afford it) is still a serious problem, even among major credit providers (e.g., Arde, 2015). In addition, idiosyncratic shocks pose so great a threat that provisioning for their costs dominates household financial behavior yet personal savings and insurance are chronically absent (Collins & Leibbrandt, 2007; van den Heever, 2012). Similarly, poverty and unemployment are still exceedingly high (Chibba & Luiz, 2011; Magruder, 2012) with anecdotes of people losing jobs and staying jobless for years quite ubiquitous.

The South African Approach to Consumer Debt Relief

Consumer debt relief under the NCA is essentially a coordination of two intertwined processes: (a) the debt review or "debt counseling" (NCA, Section 86), which is the initial process conducted by the debt counselor and entails fact finding to determine whether there are grounds to declare the debtor overindebted or at risk thereof, and (b) debt rearrangement (NCA, Section 87), which is conducted by the court based on the debt counselor's recommendation and involves the actual declaration of overindebtedness and the subsequent restructuring of claims.

Introduced amid great fanfare in 2007, the NCA is a broad piece of legislation that not only emphasizes prevention of overindebtedness but also addresses alleviation of debt already incurred. Until this point, debtors who could not keep up with their debt repayments could be subjected to sequestration (under the Insolvency Act 24 of 1936) or to administration (governed by Section 74 of the Magistrates' Courts Act 34). These mechanisms had been widely criticized as being inadequate for the rehabilitation of consumers and creating incentives for reckless credit provision (DTI, 2004; Kelly-Louw, 2009).

The sequestration process which primary goal is the realization of debtors' assets for the collective benefit of creditors especially where these assets are insufficient to satisfy all the creditors' claims (Roestoff & Renke, 2005; van Heerden & Boraine, 2009) is widely seen as ineffective to both debtors and creditors. Notably because it offers no clearly defined property exemption and debtors often have to part with most of their pre-sequestration possessions (Boraine & van Heerden, 2010; Roestoff & Coetzee, 2012). Although, as a general rule, sequestration has to be to the advantage of creditors (van Heerden & Boraine, 2009), creditors often fail to recuperate meaningful values owing to the expensive high court procedure.

The alternative approach of administration, which is only available to debtors with debts not exceeding R50,000 (around US$3,700), requires an insolvent debtor to make regular payments to an administrator until the administration costs and all the listed creditors have been paid in full. According to Kelly-Louw (2009), this process is equally flawed in a sense that, in practice, debtors rarely maintain regular payments, and even when they do, most of the payments go to administrators as fees (and these are unregulated), and in the end, not enough is paid to creditors to reduce the debts or to enable exit.

With the introduction of the NCA came the debt review and restructuring provisions to enable debt reorganization and debt counseling in cases of overindebtedness of natural persons (NCA, Section 86 and Section 87). Overindebtedness is defined under these provisions as a situation of existing or future inability to satisfy all of one's obligations under credit agreements governed by the NCA, subject to determination of this inability (NCA, Section 79). The NCA also introduced the National Credit Regulator (NCR) to regulate the entire credit industry, enforce the Act; advise government on consumer credit policy issues; and perform other tasks inter alia, registration of credit providers, credit bureau, and debt counselors (NCA, Sections 54–59). Moreover, it appears that the debt review and restructuring provisions largely rest on the statutory definition, evaluation, and declaration of "overindebtedness" as well as the competence of the debt counselor (Kelly-Louw, 2009; Otto, 2009).

A "debt counselor" under the Act is a registered natural person tasked with assisting the debtor through the debt review process. He or she must satisfy certain minimum requirements as contemplated under Sections 44–46, for instance, successfully completing an NCR-accredited debt-counseling course, a minimum working experience of 2 years in certain relevant fields (e.g., legal or complaints resolution), and must demonstrate the ability to manage his or her own finances. Section 26 of the Act also introduced the National Consumer Tribunal to adjudicate on applications made in terms of the Act by consumers, credit providers, credit bureau, debt counselors, and the NCR.

Under the debt review and restructuring provisions, a debtor who is overburdened with more debt than he or she can pay may apply or be referred by a credit provider or the NCR (in a prescribed manner and form) to a debt counselor to have himself or herself declared overindebted, so that the court may relieve his or her indebtedness. The court may also declare and relieve overindebtedness despite any provisions of law or agreement to the contrary in any court proceedings in which a credit agreement is being considered (NCA, Section 85).

A debt counselor who accepts a petition shall have 30 business days to investigate the debtor's financial situation and make a determination (NCA, Section 86[6]) and another 30 business days to make recommendations to the court (i.e., either a rejection, declaration of overindebtedness, or other actions contemplated in Section 86[7] and [8]). Upon declaration of overindebtedness, the debt counselor shall recommend that the magistrate's court rearrange one or more of the debtor's obligations. However, for credit agreements found to be "reckless" (i.e., debts extended without reasonable evaluation of the debtor's capacity to repay), the debt counselor shall recommend that the court suspend all or part of the consumer's obligations or the force and effect of those agreements, subject to Section 83(4).

The debt counselor may also reject the application if he or she finds no proof of overindebtedness. However, in this regard, the debtor, with leave of the magistrate's court, may apply directly to court for an involuntary debt restructuring order. Nonetheless, if there is reason to believe that the debtor is at risk of financial distress (even without proof of overindebtedness), the debt counselor, at his or her own discretion, may recommend an amicable settlement.

Commencement of the debt review process places certain restriction on the parties involved. For instance, debtors are debarred from entering into any further credit agreements (except consolidation agreements), and any form of enforcement of the credit agreements in question (including any rights to security) will be stayed until the process is terminated, except those claims for which legal action had already been commenced pursuant to other statutes. In addition, according to van Heerden and Coetzee (2011), the debt review process does not end or lapse automatically on the nonhappening of a specific event or the expiry of a specific time. However, the process may end if the debtor satisfies his or her rearranged obligations, in which case, a clearance certificate shall be issued to the debtor and the credit bureau, and the NCR shall expunge from their records all the facts of the matter, a contentious provision with future adverse selection implications.

Because the debt counseling procedure is not fully prescribed in the NCA, debt counselors largely rely on their discretion or the so-called *work stream guidelines* agreed to in a series of meetings between major credit providers, debt counselors, and the NCR. The uncertainties surrounding the application of the debt counseling process also compelled the NCR to implement other fixes such as the issuance of debt counseling regulations in May 2009 and to secure the high court's declaratory order in terms of Section 16(1)(b)(ii) of the NCA (Roestoff, Haupt, Coetzee, & Erasmus, 2009).

In summation, as a matter of practical reality, an over-extended debtor applies to a debt counselor who in turn notifies the respective creditors. Meetings are arranged and repayment proposals are presented to creditors, and if agreed to, the debt counselor will collect a court order (consent order) and deliver it to the affected debtor and each creditor. Thenceforth, the debtor will commence re-paying the restructured obligations in a manner ordered by the court. Creditors do not often agree to debtors' proposals which inevitably necessitate the court's intervention.

The Shortcomings of the Legislation

In principle, the debt review and restructuring provisions of the South African NCA allow debt adjustment for over-indebted consumers so that they are able to meet daily life expenses and still keep up with monthly debt repayment. Although this can provides a certain degree of relief, the current realities of a South African debtor seem to suggest that this approach does not go far enough and may not be equal to the challenge of providing meaningful alleviation of consumer overindebtedness. With the increasing spread of consumer debt among vulnerable groups coupled with the socioeconomic pressures to consume, and the high prevalence and far-reaching implications of income and health shocks, legislators are called on to consider more far-reaching remedies. The main caveats discerned in the law include the absence of provisions for debt discharge on simple, stated terms, the inability to override overlapping legislations, and the absence of comprehensive legislation in some key areas.

Discharge

The interest groups and the literature which provided policy direction during the formulation of the NCA made no effort to rationalize debt discharge. Obviously, this reticence can be explained by the fact that these authorities blamed consumer debt problems solely on market behaviors (especially reckless lending), while the potential role of unfortunate circumstances beyond everyone's control was largely ignored (DTI, 2003, 2004). Hardly surprising, then, that in its current form, the law does not provide for a clear and straightforward debt discharge mechanism (discharge is possible only in case of reckless credit and even then might prove untenable subject to Section 83[4]).

Currently, the court (barring any special impediments) can only rearrange insolvency obligations; reduce the installments payable, interest, or fees; and/or extend the terms of payment. Suffice it to say, such arrangements might benefit some consumers with strong future income prospects, or those in transitory financial distress, but ignore the fact that overindebtedness is often a long-lasting affair, stripping consumers of even the basic subsistence capabilities. For example, the World Bank Report (2013) noted that an overwhelming majority of debtors who petition in every existing system of consumer insolvency have few if any assets or income to repay and hardly enough for their families' subsistence. So, for consumers with little to no assets, such arrangements might simply exacerbate (rather than solve) their financial problems.

Without a simple, clear, and straightforward mechanism for debt discharge, the idea of debtor rehabilitation becomes implausible especially in a context such as South Africa where most consumers are unable to muster even the modest precautionary investments. Some debtors might even stay encumbered for generations trying to repay the rearranged obligations with interest and fees especially given that there is no time limitation on the process.

Overlapping Procedures

The NCA states in Section 2(7) that it should neither be construed as limiting, amending, repealing, or otherwise altering (and does not excuse anyone from the provisions of) any laws other than those specifically mentioned. Sequestration and administration orders are some of the preexisting procedures for dealing with insolvencies (personal or business) not repealed or limited by the NCA, and individual consumers are still subjected to these. But as noted earlier, these were passed simply to enforce payment at any cost (not to relieve) and therefore ineffective in the context of natural persons and thus remain in conflict with the objectives of the NCA.

Sequestration and administration laws are not even mentioned anywhere under Schedule 1 of the Act, which sets out the rules regarding conflicting legislation. According to van Heerden and Boraine (2009), had the legislature intended to oust the working of such laws in respect to consumers, it should have been clearly stated under Schedule 1. An important enabler of the regulatory overlap is the NCA's provision that debts already under litigation (pursuant to other laws) cannot be restructured under the NCA, and as a consequence, for instance, salaried workers are still routinely subjected to the widely abused garnishee and emolument orders even before they completely lose the ability to pay or often before notifying them (e.g., Haupt & Coetzee, 2008; James, 2013), and the NCA is powerless to stop that.

The multiplicity of laws and procedures might also not only explain creditors' indifference to concessions or amicable settlements with debt counselors, as observed in NCR's own investigation (NCR, 2015), but also presents incentives for creditors to become wastefully litigious even when they cannot recuperate meaningful value or to rush on debtors' wages even where it leaves debtors with nothing to live on.

Inadequate Legislation and Lack of Clarity

Given that insolvency proceedings result in significant interferences in the legal and economic positions of debtors and creditors, it becomes imperative that processes and responsibilities are clearly stipulated. The NCA does not provide for a comprehensive, integrated, and standardized system for consumer debt relief and rehabilitation especially regarding process and terms for the rearrangement order. Notable oversights include the amount of assets to be committed to repayment, limits for exempt assets (or the minimum portion of the debt to be repaid), and no clarity on repayment options (whether from future employment incomes or by liquidating available assets).

Furthermore, debtors' and creditors' overall rights and responsibilities during the debt review process are not clearly spelled out and therefore largely rely on the debt counselor's judgment and discretion. Ironically, the debt counseling process is itself not well articulated in the Act and neither are the court's processes, not to mention the agonizingly low minimum education requirement (Grade 12) for such a crucial professional. These issues, according to the NCR (2015), have spawned a multitude of problems including process weaknesses, neglect of regulations and arbitrary standards of engagement, downright misinformation of debtors, lack of cooperation between creditors and debt counselors, and rolling backlogs in court. Some debt counselors have even placed debtors under debt review without their consent or even before signing the mandatory form.

Citing a University of Pretoria Law Clinic study, Roestoff et al. (2009) had noted similar problems earlier, notably, credit providers not cooperating, the insufficiency of the Act and regulations, uncooperative consumers, incompetent debt counselors as well as unrealistic proposals, and magistrates' lack of knowledge.

Unfortunately, the work stream guidelines that were formulated to close some of the loopholes in the debt counseling process are to a larger extent not adhered to. Many credit providers and debt counselors continue to breach these guidelines either because they feel they are not bound by them (because they did not participate in the formative negotiations) or out of sheer dereliction of responsibilities (Roestoff et al., 2009). In addition, the payment distribution agents (PDAs) mandated under these arrangements to distribute restructured payments by debtors to creditors appears to be an unnecessary duplication of duties and likely to render the process unnecessarily convoluted and prone to fraud.

Other unclarified issues by the Act, yet important elements of contemporary consumer insolvency regimes include time limitation, the treatment of creditors with encumbered collateral, and provisions for no-income/no-asset debtors. Although the Act provides grounds for closure of proceedings, the length of the process or repayment plan is not stipulated. The law's implicit position is an indefinitely process, subject to fulfilment of the rearrangement order. This will then mean that poorer insolvency debtors might have to stay under bankruptcy for generations (subject to very severe financial and material constraints), even though majority of these will not have the wherewithal to pay anything substantial beyond covering their basic needs. It may also create disincentives to productivity.

The absence of special provisions to deal with collateralized debt is likely to both disadvantage creditors and increase repayment burdens on debtors. On one hand secured debts are usually bulky, so restructuring these together with the rest of the unsecured debts will inflate the repayment plan, yet on the other hand creditors are denied the chance to exercise their security rights. Furthermore, the absence of provisions for debtors with no reasonable income prospects or assets with which to pay the restructured claims defeats the very essence relief and rehabilitation. In addition, the provision for insolvency fees (e.g., application, debt counselor, and after-care fees or court order costs) is discriminatory and burdensome to highly distressed debtors.

In a nutshell, in light of the issues raised earlier, it is submitted that in the current form, the debt review and restructuring provisions of the NCA are not up to the challenge of providing meaningful relief and rehabilitation of overindebted debtors. The expectation that the consumer must satisfy all responsible financial obligations and the absence of a simple, straightforward provision for discharge suggest that these mechanisms can only offer very limited relief to the few consumers who may still have the means to pay. Moreover, the interaction of overlapping provisions may even deny debtors access to this limited protection. For a household sector tormented by frequent income and health shocks, high unemployment, and a very low personal saving rate, one cannot go far in solving consumer debt distress by simply rescheduling debt or recalculating the interest and fees.

Lessons From Recent Developments in Treatment of Consumer Insolvencies

There is a certain degree of agreement among consumer protection scholars that when an overindebted person with no reasonable prospects of resuming payments in a foreseeable future is faced with constant threats of turning his or her accounts over to debt collectors or courts, chances are his or her socioeconomic functioning will spiral out of control. Although creditors have a right to repayment, such actions may prove wasteful and futile because they are less likely to recuperate any meaningful value. Unlike businesses which can be liquidated and disposed of, natural persons need some form of protection to enable them to continue supporting themselves and their dependents should they lose repayment capacity (certainly without incentivizing moral hazard). Having identified some of the deficiencies of the debt review and restructuring provisions of the NCA in dealing with debt problems of individuals, this section considers possible lessons policymakers can draw from the 2013 World Bank's *Report on the Treatment of the Insolvency of Natural Persons* and some aspects of the American system.

The report is described as a "reflective" document with suggestions and guidance on the different policy issues and options that need to be involved in developing modern legal regimes for the treatment of personal insolvency (World Bank, 2013, p. 4), giving regard to the diverse social, legal, and economic sensitivities around the world (Kilborn, 2015). The report not only underscores the need for a careful balance between debtors' and creditors' interests but also notes that the principal purpose of a consumer insolvency system is to reestablish debtors' economic and repayment capability and some of the benefits of which being, freedom from excessive debt (and its adverse effects on family and economic well-being), alteration of financial behavior, and increasing payment to creditors, with the fresh start as its tailpiece. Among the broad themes tackled by the report which are most pertinent to this discussion include relief and rehabilitation, repayment, and design.

Section 11.6 of the report suggests that the most effective form of relief and rehabilitation is the fresh start wherein the most impecunious debtors may get a straight discharge without any form of payment, whereas those with payment capacity may be required to pay a portion of the debt according to a regulated period of good conduct considered as the price of "earned fresh start" (World Bank, 2013, p. 363). In addition, it is argued that although the scope of discharge should be as wide as possible, even the most debtor-friendly systems often exclude liabilities not created in the market context (e.g., child/spousal maintenance). The principle of good faith both in obtaining debt and in disclosure for the purpose of rearrangement of claims is also an important aspect of discharge.

Regarding repayment, many modern systems continue to focus on the debtors' assets as a means to recuperate creditors' claims. They thus discount the fact that the overwhelming majority of insolvency debtors often have few if any assets of any value to liquidate and distribute to creditors or even to warrant the significant administrative expenses involved (World Bank, 2013, p. 220). As such, the report suggests that regimes would do well to focus on contributions from future income as the more meaningful approach to repayment but cautions against coercing debtors into onerous payment plans that may not be viable. It adds that the notion of property exemption which safeguards certain properties from execution plays an important role in alleviating the condition of the insolvent debtor even though property exemption by itself is insufficient to provide a debtor with a real opportunity for a fresh start. Thus, insolvency debtors have to keep a certain portfolio of assets with which to support themselves and their dependents (e.g., tools of a trade, family home).

Other issues that arise regarding repayment include the lengths of the repayment plan. The report asserts that a long plan is likely to provide disincentives to productivity for debtors, whereas a very shorter one is likely to depress creditors' returns. Hence, Section 11.5 of the report recommends predefined clauses with a duration that lasts 3–5 years, with possibilities for compliance monitoring and modification based on the changing circumstances of the debtor. Regarding the issue of no-income/no-asset debtors, the report notes that a significant number of debtors in all insolvency systems might have some resources to cover their basic needs, but they often have no extra to pass on to creditors. In which case, the so-called *zero plans* (which foresee no payment) or an alternative system which reduces the formalities and expenses of the court-based procedure are recommended.

Regarding design, it is noted that an essential aspect of the design of an insolvency regime for natural persons is its interaction with amicable, informal arrangements albeit with some institutional support and incentives. The report informs that in many jurisdictions, attempts at amicable settlement are either encouraged or have been made a prerequisite to formal engagement. The arguments advanced in this regard inter alia are, debtors may avoid the stigma of insolvency, costs are lower, debtors may have incentives to make higher offers to creditors to avoid court procedures, or informal attempts prepare the parties for formal procedures. In addition, where to locate the formal system should be a major consideration, either within an existing insolvency regime or in a separate, perhaps even freestanding law. The report notes that although both have their merits, a separate law for natural persons may be desirable as it takes into account the special needs of fresh and blood individuals.

The design also speaks to the nature of the support system for the institutional framework, notably the intermediaries who help with screening and channeling individuals through the insolvency procedure (e.g., lawyers, debt counselors, insolvency practitioners, state officials, and judges).

Furthermore, there are also lessons to be garnered from the American approach to consumer insolvency under the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA), one of the few preexisting systems which seems to have had a considerable influence on the drafters of the World Bank Report most notably on issues regarding the viability of resources (current or future), discharge, and the presumptions of good faith (see Dickerson, 2008; van Apeldoorn, 2008). It is noted that the main impetus behind the reforms to the U.S. bankruptcy code which introduced the BAPCPA was the complaint that debtors were walking away from their obligations far too easily, even before losing repayment capacity (White, 2007). The main innovation was the "means test" which seeks to limit access to a quick discharge (under Chapter 7) while attempting to force more consumers into Chapter 13 debt repayment plans.

The means test is an elaborate quantitative test which debtors are subjected to in order to ascertain their eligibility to a fast-track discharge under Chapter 7 by turning over part of their nonexempt wealth for liquidation (if any) but keep complete control of their future incomes, with exemptions defined at state level (Pace & Lown, 2016). Debtors who fail the means test may file a Chapter 13 case under which they get to keep a greater share of their properties but pay a bigger fraction of the debt using future incomes over a period of 3–5 years before discharge (Gerhardt, 2009). It is noted that the biggest percentage of Chapter 7 cases are often non-asset cases and are dischargeable within a few months of filing, and despite the presumption of a "fresh start," more than a third of Chapter 13 plans are dismissed because of nonpayment (Pace & Lown, 2016, p. 316).

In summation, although the World Bank Report (2013) does not recommend uniform treatment of personal insolvency because of the different political, cultural, and social considerations, it emphasizes that the characteristics of existing systems that have proven most effective speak to not only pursuing a meaningful balance between creditors' and debtors' objectives but also recognizing the inherent power imbalances between these two constituencies. In addition, the design of the system should crucially be guided by objectives of accessibility, cost-effectiveness, and efficiency.

Specific Recommendations

Both the International Federation of Insolvency Professionals' *Consumer Debt Report* (INSOL International, 2001) and the World Bank Report (2013) agree that a key element of any consumer insolvency law or rehabilitation procedure is a balanced approach where an insolvency debtor may have to contribute toward repayment insofar as it is possible, and within a reasonable period, but most important, ample resources should be reserved to that debtor to allow him or her to maintain a reasonable standard of living. Beyond this tenet, it is submitted that there are no standards to guarantee the best set of regulations, as sound standards in some contexts might not be so in others. Nonetheless, the recommendations provided as follows take stock of some of the opinions contained in the INSOL International's (2001) report and the Word Bank Report (2013) in the context of relief and rehabilitation, repayment, efficiency, and accessibility.

Relief and Rehabilitation

A comprehensive review of the entire insolvency system in favor of a single, simple, and straightforward mechanism for consumer debt relief is recommended. More specifically,

- Discharge should be the implicit objective for admission to proceedings—on specific and simple terms, with precisely worded clauses on the rights and responsibilities of each party.
- Prescribe a specific period of good conduct: long enough to allow time for adjustment of behavior and repayment but one that allows for a quicker exit and rehabilitation—ideally between 12 months and 3 years, giving regard to individual circumstances and/or future income prospects.
- Enable expedient discharge for no-income/no-asset debtors. Ideally discharge without any further action or after a short period of community service.
- Regulations should clarify alternative measures for those who, for some reason, are unable to get a discharge. If an appeal is possible, clarify grounds and procedures thereof.

Repayment

The Act or regulations should clearly explicate the terms and provisions of the rearrangement plan (including the scope of assets) to the extent that they are predictable and discernible so that consumers can readily decipher the opportunity cost of availing themselves to the procedure before they do. Where reasonable nonexempt assets exist, the law should make provisions for liquidation to enable early exit, and debtors with reasonable permanent incomes may be compelled to pay out of that to enable reasonable recuperation of claims or both, if assets and income are good.

- The proportion of resources necessary for repayment should be fair enough to represent a meaningful contribution to the debt repayment.
- The proportion and type of exempt assets should be clear and fair enough for debtors and their dependents to live a minimally acceptable and clearly defined standard of well-being.
- Treat secured debts separately—except in case of the principal homestead.

Efficiency

Because the Act provides for a facts-sensitive test of overindebtedness, it should also enable a comprehensive system with standardized procedures for entry, observance, and exit to prevent ambiguities and potential overreach of judicial authority and debt counselors alike. All possible abuses by all the parties to the process and their sanctions should be clarified:

- Enable earlier commencement of the proceedings while there is still value for creditors and/or debtors to rescue.
- Clarify the boundaries of activities of debt counselors and court.
- Codify and unify the laws in respect of natural persons' overindebtedness: Where the credit agreements in question fall under the NCA, the provisions of the NCA should supersede any other procedures—with a narrowly worded clause to that effect.
- Keep insolvency filings on record for at least 5 years after closure to aid creditors' decision making.

Accessibility

Legislators should evaluate ways to minimize the role of courts and eliminate fees. This should help to expedite the process, reduce case backlogs, and reduce the potential for profiteering. Overindebted debtors are often unable to meet even the modest fees while a long unwieldy process may further damage both debtors' and creditors' positions.

- Integrate amicable out-of-court and alternative workout arrangements, ideally as prerequisites for admission to judicial proceedings.
- Maintain a nonprofit environment around the process by empowering state-sponsored local agencies, professionals, and paralegals to take the central role in the review and readjustment process.
- Regulate mechanisms for post-insolvency debtor education, monitoring, and counseling to prevent a possible vicious cycle.

Conclusion

Surely, consumers have a duty to pay their financial obligations, and certainly, the vast majority of them have every intention to do so. Unfortunately, unanticipated negative events beyond their control such as illness, divorce, or sudden unemployment often make this impossible. The choice in most credit markets has always been to leave defaulting debtors at the mercy of their creditors who would naturally attempt to collect on them by any means necessary. The expectations have been that traditional safety nets (e.g., unemployment benefits), market forces, or restrictions on lending would counteract the causes and/or consequences of severe debt distress. Unfortunately, available studies have shown that neither is the case. Consumer debt distress is inevitable regardless of the market conditions, yet traditional safety nets are often too inadequate to free consumers of excessive indebtedness. Thus, it becomes imperative for states to activate legal means through which consumers facing severe debt distress are able to discharge some of that debt so they can be able to reclaim their financial health.

Although the NCA promises in its preamble to provide for a consistent and harmonized system of debt restructuring, enforcement, and judgment, currently, this does not seem to be the case given the inadequate drafting of the debt counseling process and the multiplicity of laws and procedures. The situation is muddled further by the absence of a debt discharge framework on simple, stated terms. In the end, the provisions amount to nothing more than a statutory rescheduling of debt wherein only the few consumers with viable resources are able to benefit, whereas others continue to be cornered by creditors through other alternative yet undesirable debt-enforcement procedures even when under debt counseling. Hence, the NCA is not up to the challenge of providing meaningful alleviation of consumer overindebtedness. Thus, a complete realignment of its debt review and restructuring provisions in favor of a simple, straightforward mechanism for debt discharge akin to the fresh start debt relief mechanism is recommended. In clarifying the need for a tightly regulated relief framework, this article seeks to provide a basis for further quantitative and qualitative empirical investigations.

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