

Bankruptcy is a scary word. Although bankruptcy provides debt relief, it also conjures up images of losing your home, no hope of rebuilding credit, and other unpleasant thoughts.

Bankruptcy: the B Word

Let's address those concerns with an analogy. Do you remember going to see the doctor when you were a child for your yearly check-up? You dreaded getting jabbed in the finger for a blood sample, but before you knew it, it was done and over with and the sting went away. One can think of the bankruptcy process in the same way – you dread filing for bankruptcy and expect it to be painful, but before you know it, your debts are gone and you've moved on with your life.

The bankruptcy process has the objective of rehabilitating the debtor, so that he can become a productive member of society without the burden of crushing debt. The bankruptcy system also ensures that all creditors are treated fairly and get an appropriate share of any debtor assets. Therefore, you should be aware that the bankruptcy system exists to work for you as well as your creditors.

The Bankruptcy Process

The bankruptcy process is governed by a federal statute called the *Bankruptcy and Insolvency Act* ("BIA"). Under the BIA, the major steps in the bankruptcy process are:

1. Meet with a trustee to evaluate your financial situation
2. File an assignment in bankruptcy with the Office of the Superintendent of Bankruptcy ("OSB")
3. Attend two financial counselling sessions
4. Meet with the trustee to discuss your discharge

Each of these steps will be discussed below.

Step 1: Meet with a trustee to evaluate your financial situation

Just as you would see a doctor to assess your symptoms when you're not feeling well, one sees a trustee in bankruptcy when experiencing great financial distress. The trustee's evaluation includes a review of your assets, debts and household budget (i.e., income and living expenses). Upon completing the evaluation, the trustee will give you options in dealing with your debt, including the option of bankruptcy.

Step 2: File an Assignment in Bankruptcy

Once you've made a decision to file for bankruptcy, the trustee prepares a legal document called an Assignment in Bankruptcy. By signing the Assignment, you are indicating that you are voluntarily filing for bankruptcy. At the time you sign the Assignment, the trustee will explain that you have duties as a bankrupt individual. These duties are to:

- Disclose all of your assets and liabilities to the trustee
- Advise the trustee of any property disposed of in the past year
- Surrender all credit cards to the trustee
- Attend an examination at the OSB, if required
- Attend the first meeting of creditors (if a meeting is requested by the creditors)
- Advise the trustee in writing of any address changes; and
- Generally assist the trustee in administering the estate

The Assignment is filed with the OSB, a branch of the federal government that monitors bankruptcy and insolvency filings. Once the OSB receives the Assignment, it issues to the trustee a Certificate of Appointment, appointing him as the trustee of your bankruptcy estate. There are three things that happen once the trustee is appointed:

1. Once the Certificate of Appointment is issued to the trustee, you are legally bankrupt. At that point, your assets vest in the trustee (i.e., he becomes the legal owner) for the purpose of liquidation and distribution to your creditors.

In the majority of situations, you won't lose your assets, as Ontario law allows a bankrupt person to retain:

- Household furniture up to \$11,300
- Personal effects up to \$5,650
- Tools of the trade up to \$11,300
- A vehicle valued up to \$5,650
- Pensions
- Other special exemptions for farmers
- Certain life insurance policies and certain RRSPs

The trustee for the benefit of your creditors may sell other assets you have. However, in most cases arrangements can be made to allow you to keep assets that would normally be sold.

2. Wage assignments and garnishments are stopped, as well as most other legal proceedings against you.

3. You are required to keep track of your monthly income and expenses and may be required to pay a portion of your monthly income to the trustee. How much you have to pay is determined by the trustee based on guidelines set out annually by the OSB. These guidelines take into account the amount of your household income and the number of dependents.

Step 3: Attend two financial counselling sessions

During your bankruptcy you'll be required to meet with the trustee to discuss any potential non-financial issues that led to your filing for bankruptcy. For example, gambling, substance abuse, and marital breakdown are common problems in society that inevitably lead to financial hardship. In addition, the trustee will provide information to you on money management and ways in which you can rebuild your credit.

Step 4: Meet with the trustee to discuss your discharge

An important event in the bankruptcy process is obtaining your discharge from bankruptcy. Being discharged from bankruptcy essentially means that you are free of your debts (with certain exceptions – student loans, alimony/child support, fines for breaking the law, and judgments arising from fraud or physical/sexual assault, are not discharged), and that you are no longer “bankrupt” for legal purposes.

Your creditors, the trustee or the OSB have a right to oppose your discharge. Common reasons for opposing a bankrupt's discharge are:

- Failure to attend financial counselling sessions with the trustee
- Failure to make required payments to the trustee
- Failure to disclose all assets to the trustee
- Questionable transactions entered into by the debtor before or during the bankruptcy

If no one objects to your discharge and you are a first-time bankrupt, a discharge is automatically granted nine to 21 months after filing bankruptcy. Whether you are bankrupt for nine or 21 months will depend if your net monthly income exceeds a certain monthly living

allowance established by the OSB. If you are granted an automatic discharge, there is no court hearing and the Trustee sends you a copy of the discharge.

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If your discharge is opposed, the Trustee sends a discharge application to the Court. The Trustee will advise you if you are required to appear in Court for the discharge hearing. At

the hearing, the Trustee's report informs the Court of the circumstances surrounding your bankruptcy. The Court will then issue one of the following orders:

Absolute Discharge: You are no longer responsible for debts incurred prior to bankruptcy (save for the exceptions noted above).

Conditional Discharge: You maybe required to pay a certain amount of money to your creditors through the trustee for a specified period (e.g., \$100 per month for 24 months). Your discharge is subject to fulfilling the terms and conditions of the order. An absolute discharge will be granted when the specified conditions are fulfilled.

Suspended Discharge: This could be an absolute discharge but there is a delay before it comes into effect or is reviewed again by the Court.

Discharge Refused: The Court has the right to refuse a discharge in unusual circumstances. If you have been bankrupt before, your discharge application is sent to the Court for its review and determination. There is no automatic discharge for a second-time or third-time bankrupt.

If you've been bankrupt before, your discharge is automatically granted 24 months to 36 months after filing bankruptcy. Again, whether you are bankrupt for 24 or 36 months will depend if your net monthly income exceeds a certain monthly living allowance established by the OSB.

Who prepares my tax returns?

You must supply the trustee with documents to complete two income tax returns during the year in which a bankruptcy occurs. A pre-bankruptcy income tax return must be filed for the period from January 1 to the date of bankruptcy. A post-bankruptcy income tax return must be filed for the period from the date of bankruptcy to December 31.

Income tax refunds from prior years are an asset of the bankrupt estate and must be sent to the trustee. The trustee may request that refunds from the post-bankruptcy return be paid to the estate. Income taxes owing prior to the bankruptcy are discharged. Any amount owing on the post-bankruptcy tax return must be paid by the bankrupt.

Starting Over – Rebuilding your Credit

One concern for many individuals contemplating bankruptcy is the effect on their credit rating. Bankruptcy will bring a person's credit rating to an R9 with the credit bureau. It will remain so for 6 years after the bankrupt obtains his discharge, after which it will be deleted from the debtor's credit file.

Does this necessarily mean that you won't be able to get credit during this period? No, it does not.

Your credit rating is certainly an important factor in determining your credit worthiness. However, lenders will look at other factors such as your income and your ability to get a guarantor or co-borrower. There are also other devices through which you can rebuild your credit:

- Secured credit cards – Certain financial institutions issue secured credit cards. By providing a bank or trust company with a money order (usual minimum is \$1,000) along with the credit card application, you'll be issued a credit card with a maximum credit line equal to the money order. For example, you submit a \$1,000 money order along with the application form, and you are issued a credit card with a limit of \$1,000. The bank has your \$1,000 as security to ensure you pay your credit card balance.
- Mortgage brokers – If you are in the market for a home and need financing, a mortgage broker will shop around for the best mortgage rate available to you given your bankruptcy. However, due to your bankruptcy, the rate offered to you will usually be above current market rates.

We at Fong and Partners Inc. are in a position to help you rebuild your credit. We can refer you to organizations that can assist in financing a vehicle, real estate purchase, or credit card account notwithstanding your bankruptcy.

Conclusion

Bankruptcy is ultimately a rehabilitative process that relieves a debtor from the burden of crushing debt and allows him to become a productive member of society. From the creditors' stand-point, the bankruptcy process provides transparency into the debtor's financial affairs and ensures that they will be dealt within an orderly process.

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Starting Over
Personal Financial Difficulties is an overview rather than a complete analysis. Before applying any of these suggestions, consult your Fong and Partners Inc. advisor.

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