DEBT ADJUSTMENT FOR PRIVATE INDIVIDUALS

BY

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1. INTRODUCTION

In October 1990 the Commission on Insolvency presented its interim report entitled *Skuldsaneringslag* (Debt Adjustment Act).[1] The Report contains a proposal for an entirely new institution in Swedish law which would mean that over-indebted physical persons not engaged in commerce would under certain circumstances be able to have their debts reduced or written off through a court decision.

The possibility of debt adjustment may be of key importance for the future of many who are encumbered with debts. At the same time, as so often when dealing with something new, it is natural for some people to express a certain scepticism. Several objections have already been raised among grantors of credit. Does not this proposal entail a risk that the general readiness to pay one's debts will be weakened? And how can the proposal be reconciled with the fundamental thesis of *pacta sunt servanda*—agreements shall be kept?

Yet the proposal is not entirely revolutionary. Rules of similar import exist in other countries, and the Commission's chief pattern has been the Danish *gældssaneringsinstitut*, the institution of debt adjustment. Experience of these rules gives some reason to believe that concern over consequences of the proposal may be exaggerated.

In this article, the main features of the proposed debt adjustment institution will be presented (section 4). First, however, a background to the proposal is given (section 2), and this is followed by a comparative review of corresponding rules in other countries (section 3) and a summary of some considerations underlying the proposal.

2. BACKGROUND

The question of debt adjustment for over-indebted physical persons became more topical during the 1980's. By "over-indebted" is meant not only that a debtor has many large debts. The point is, rather, that

[1] *SOU* 1990:74. Referred to in what follows as 'Rep'. The single investigator was Appeal Court Division Head Trygve Hellners. The present author acted as an expert.

the person is so indebted that his inability to pay his debts is either permanent or at least will presumably remain for the foreseeable future.[2] In the general discussion many striking expressions have been used to describe the debtor's hopeless predicament: he has been caught in the debt trap, landed in the River Debt, to take but two.

Two categories of debtor are in particularly poor straits. One, to use the Report's expression, is the credit consumers. It is well known that household indebtedness has markedly increased in the last few years. Many households cannot manage even the interest on their loans.[3] One cause of the increased indebtedness is naturally the de-regulation of the credit market which took place in the middle of the 1980's. The appreciable increase of the number of "consumer insolvencies" is not, however, a limited national occurrence: the same phenomenon has been observed in other countries. There, too, legislation or proposals for legislation have been presented in an attempt to solve these problems. The nearest example is Denmark, which in 1984 introduced rules on *gældssanering*—debt adjustment.[4] Other examples are France[5] and Germany.[6] In the German discussion, phrases such as *der moderne Schuldturm* and *die neue Schuldknechtschaft* occur.[7] Developments have followed similar lines in the USA, with a large increase in the number of consumer bankruptcies. At the time of the 1978 American bankruptcy reform, nine out of ten bankruptcy debtors were consumers. Even after the reform the number of consumer bankruptcies continued to increase, which in turn caused certain further changes in the law.[8]

However, it is not only credit consumers who need help to have their economies restructured. Another group that has been particularly noted consists of people formerly engaged in commerce, that is, private

[2] *Rep*, p. 187. See also section 4.2.2 below concerning the qualified requirement on insolvency.

[3] *Rep*, pp. 17, 59 ff, 184 ff. See also *SOU* 1988:55, Hushållens skuldsättning (Household Indebtedness) and *Konsumentverket, Rapport 1989/90:1*, Hushåll in ekonomisk kris (Households in Economic Crisis).

[4] See *Bet* nr 957/82 om Gældssanering (Danish Report on Debt Adjustment), e.g. pp. 7 ff.

[5] E.g. Bouteiller, *Les Petites Affiches*, 16 Feb 1990, p. 14.

[6] Bundesministerium der Justiz, *Referentenentwurf*, Gestetz zur Reform des Insolvenzrechts, 1989, p. A 33 and Uhlenbruck in *Monatsschrift für deutsches Recht (MDR)*, 1990 p. 4, Scholz, *Zeitschrift für Wirtschaftsrecht (ZIP)*, 1988 p. 1158, both with references, Westerman in *Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht (ZHR)*, vol. 153 (1989) p 124.—All statements relating to the period before 3 October 1990 refer to the former West Germany.

[7] Uhlenbruck, Westermann, Scholz, (above, note 6) and Wochner, *Betriebs-Berater* 1989, p. 1354.

[8] Rendleman, 58 *North Carolina Law Review* (1979–80), p. 724 and refs. *Rep*, pp. 137 ff.

persons who started their own businesses but who for various reasons not of their own creating were forced to stop operations, thus incurring such large personal debts that they lacked real means of paying them.[9] A serious small businessman who is forced into bankruptcy because of a poor economic climate can—if he has not run his business in the form of a limited liability company—be forced to use all his future income over and above the existence minimum to repay his creditors.[10]

The negative consequences of the debtor's practically life-long indebtedness are considerable for the debtor himself and for his family, for his creditors and for society. If the debtor's predicament is totally hopeless, e.g. because he has through sickness become incapable of work for the rest of his life, his debts will never be paid and they can only run up costs for the creditors in fruitless attempts at collection. If the debtor has in fact some working capacity, there is still an appreciable risk that his having incurred such large debts as to be unable ever to pay more than a fraction of them will mean that he has no motivation to gain an income through ordinary work. He will be tempted to work 'black' or to join the unemployed. Other debtors may make desperate attempts to clear up the mess with new loans, which cannot be repaid, and so on. All this leads to costs for society, the debtor becoming a charge upon the social services, the medical services and perhaps also criminal care.[11]

Naturally the problems are by no means new, but the developments of the 1980s have focussed attention on the deficiencies in the legal system relating to insolvency.[12] Wishes for reform have also been made known in different quarters. Particular reference can be made here to the *Law Committee's Report* LU 1987/88:12 on debt adjustment, etc., arising out of private bills 1985/86:L224 and L251; 1986/87:L301; to the Debt Committee's report *SOU* 1988:55 *Hushållens skuldsättning* (Household Indebtedness), and to the Tax Collection Committee's proposals regarding composition and remission in claims in public law, *SOU* 1987:10, Indrivningslag (The Law of Collection), etc.[13]

[9] *Dir* 1988:52 p. 6 f. *Law Committee Report* LU 1987/88:12, p. 25. *Rep*, p. 54, 57, 167, 184. *Report* 957/1982(DK), p. 76.

[10] *LU* 1987/88:12, *Bet* 957/1982 (DK) (above note 9). Also, it is not that easy for a small businessman to avoid personal payment liabilities even if he runs his business as a limited company, since the banks, as a condition for credit, normally require personal guarantees for the company's engagements.

[11] *Rep* p. 18, 21, 189, 192 f, 248 f. *LU* 1987/88:12 p. 25 f. *Bet* 957/82(DK) pp. 73 ff. Weistart, *Law and Contemporary Problems*, Autumn 1977, p. 110. *Referentenentwurf* (above, note 6), p. A33.

[12] *Rep*, p. 186.

[13] *Rep*, p. 163 ff.

The Swedish bankruptcy and composition rules are basically intended for companies, and are unsuited for private persons. From the creditor's point of view it is normally pointless to have an over-indebted person declared bankrupt since in most cases the debtor has no distrainable assets to speak of. The result can be quite the reverse, that the creditor is forced to meet a portion of the bankruptcy costs (14:3 KL (Bankruptcy Act)). From the debtor's point of view, too, bankruptcy is pointless in that liability for debts unpaid in the bankruptcy proceedings nevertheless persists since the debtor is not discharged from his bankruptcy debts. Composition is not appropriate for private persons, either. Private composition presupposes the creditors' concurrence, and the rules regarding compulsory composition are so arranged that they have chiefly been used for companies.

In addition, however, there are certain other, unregulated, forms of "debt adjustment" to which a debtor already has recourse. In particular, there is what is termed the Accounts Council which, concerned primarily with credit-card credits, was started on a trial basis in a limited number of social service districts in 1987. (Up until August 1990, 75 cases had been received by the Council). The help given to indebted clients of the criminal care services may be mentioned, as may also the special debt reconstruction projects of a number of Swedish enforcement services. The role of the social services should also be mentioned in this connection. Lastly, there exist special rules on remission of certain debts such as tax debts and study loans.

Yet it is obvious that all these possibilities, which are considered in detail in the Report,[14] are insufficient to achieve any real effect on the problems that over-indebtedness entails.

3. THE PROPOSAL IN GENERAL. COMPARATIVE REVIEW, ETC.

3.1 Comparative review[15]

A radical method which would considerably ease the situation for those burdened with debt would be, analogously with the Anglo-American

[14] See *Rep*, pp. 16 ff, 63 ff, 183 f, 187 ff.

[15] Chapter 4 of the Report contains an account of the American, English, French and German rules on debt adjustment and discharge, written by the present author. She sees no reason to repeat this, but would refer generally to the Report pp. 105 f, 134 ff., with excerpts from the legal text in Annexes 6–8 (p. 391 ff.). The Report also contains an account of the Danish Debt Adjustment institution, p. 106 ff and Annex 5 (p. 385 ff), to which reference is also made. See also p. 195, 198 ff, 252 ff.

tradition, to introduce rules on discharge from debt following bankruptcy. Such an approach has begun to make itself felt even in countries which do not share the tradition of common law. The right to discharge from debt following bankruptcy was introduced in France with the bankruptcy reform of 1985.[16] A similar proposal has been made in Germany.[17]

In England and the USA it has long been the case that a debtor is discharged from his liability for any debts not paid in bankruptcy proceedings. In England the principle became law in 1705, in the USA in 1800. Initially, however, it was more nearly a form of compulsory composition, since discharge presupposed approval by a majority of the creditors. However, this prerequisite disappeared at the end of the 19th century.[18]

When the rules on discharge were originally introduced into English law, they had a different purpose from what is now held to embody the principle. The rules were intended to make it easier for creditors to gain access to the debtor's property and discharge represented a reward to the debtor who made his property available for distribution among his creditors, without concealing any portion of it. The reward meant that the debtor was released from liability to imprisonment for his unpaid debts.[19]

In time, however, the principle has come to be justified primarily through consideration for the debtor. Thus in American law it is customary to maintain that the institution of bankruptcy serves two different purposes, not only to give creditors the possibility of payment on conditions that are as equitable as possible, but also to free "the honest but unfortunate debtor" from his debts and give him a chance to start afresh. The rules on discharge are nowadays supported primarily for humanitarian reasons.[20] The basic idea of the fresh-start doctrine is that the honest but unfortunate debtor should be protected.

To prevent abuse of the system by the "dishonest" debtor, a number of exceptions have been listed, which refer either to the debtor and his

[16] Art. 169, Loi du 25 janvier 1985 relative au redressement et à la liquidation judiciaires des entreprises. *Rep*, p. 147 f.

[17] See below, note 30.

[18] See e.g. Riesenfeld, 31 *Minn. L. Rev.* (1947) pp. 406 ff., and *Cases and Materials on Creditors' Remedies and Debtors' Protection*, 3rd ed., St Paul, Minn, 1979, pp. 728 f.

[19] Sward, *Wisconsin L. Rev.* 1987, p. 410. Sullivan, Warren & Westbrook, *Wisconsin L. Rev.* 1983 p. 1098 with refs. Shuchman, *Law and Contemporary Problems*, Autumn 1977, p. 148 f.

[20] Weistart, *Law and Contemporary Problems*, Autumn 1977, p. 110 f.

behaviour or to the nature of the debt. In the American Bankruptcy Code of 1978, exception is made of debtors who have attempted to deceive their creditors or the bankruptcy court (for example by withholding assets) and in the case of certain debts which it is considered the debtor should pay for social or similar reasons (e.g. maintenance and certain taxes, damages and fines).[21] English law earlier placed great weight on the debtor's behaviour. These rules were very demanding for the courts and have now, not least for reasons of expense, been simplified. Discharge is received automatically after three years or, in the case of summary bankruptcy proceedings, two years, reckoned from the start of the proceedings (Insolvency Act 1986, sec. 279). However there are exceptions in the case of debtors who have rendered themselves liable to criminal bankruptcy, and where certain debts are involved (e.g. those arising through fraudulent breach of trust).[22]

In modern American doctrine the principle of discharge has also been linked with bankruptcy as a question of risk placing, in which the creditor has been found more suitable than the debtor to support the risk of payment default.[23]

There are also a number of other arguments in support of the principle. One is the comparison with the situation in which a legal person has been declared bankrupt. Why should a person who has managed a business avoid all debts if the operation has been run in limited company form, but be encumbered with life-long debt if he has run the business as a private trader?[24] This, moreover, was a main argument when discharge following bankruptcy was introduced into French law.[25] The argument is naturally relevant from the French point

[21] *Rep*, p. 135 ff. See e.g. *Collier on Bankruptcy*, 15th ed., vol. 3, New York 1989, vol. 4, New York 1990, chs. 5 and 7; Jackson, *The Logic and Limits of Bankruptcy Law*, Cambridge, Mass., 1986, p. 225 ff.; Cohen & Klee, *North Carolina L. Rev.* vol. 58 (1979–1980) p. 681 ff, 700 ff; Rendleman (above, note 8) p. 723 ff.; Riesenfeld, *Cases* (above, note 18) p. 728 ff; Sullivan, Warren & Westbrook (above, note 19) p. 1097 ff; Sward (above, note 19) p. 407 ff; Weistart (above, note 20) p. 107 ff. and the debate on p. 147 ff; and Note, *Harv. L. Rev.* vol. 97 (1983–84) p. 759 ff.

[22] *Rep*, p. 143 f. See e.g. Fletcher & Crabb, *Insolvency Act 1986 with annotations*, London 1986, p. 227 ff.; Berry & Bailey, *Bankruptcy: Law and Practice*, London 1987, p. 248 ff; Grier & Floyd, *Personal Insolvency—a Practical Guide*, London 1987, p. 116 ff, and Grenville, *Bankruptcy: the Law and Practice*, London 1987, with supplement, Nov. 1988, p. 280 ff.

[23] See Jackson (above, note 21) p. 228 f., with ref. to Eisenberg.

[24] E.g. Jackson, *op.cit.* p. 229 f.

[25] *Rep*, p. 148 and refs. The same argument has also been put forward in the German discussion: see e.g. Ackmann, *Schuldbefreiung durch Konkurs?* Diss (Bonn) Bielefeld 1983, p. 3 ff with refs. Cf. *Referentenentwurf* (above, note 6) p. A34, *Bet* 957/1982 (DK) p. 76–

of view, since only legal persons, together with merchants, craftsmen and farmers, but not private persons, can be declared bankrupt under French law.

The principle of debt discharge after bankruptcy is indeed not without objections. Inevitably, it can be abused. The fundamental weakness of "the fresh start doctrine" appears to be that, despite the many exceptions, it is too general. It permits no account to be taken of the debtor's *future ability to pay*, which may of course vary considerably from debtor to debtor. A basic notion underlying debt discharge is precisely that the debtor's future income, his "human capital" must be safeguarded. However, this implies that debt discharge is granted both to a debtor whom illness has rendered incapable of work for the rest of his life and who can never reasonably be in a position to pay his debts, and to a well-educated debtor who, though temporarily embarrassed, should be able to pay at least part of his debts during the next few years. The arguments in favour of debt discharge are naturally of differing weight and content in these two cases.

Presumably, such thoughts as these have contributed to the growth, in the USA and England and alongside the rules on discharge in connection with bankruptcy, of debt adjustment rules which are not connected with bankruptcy and which consider precisely the debtor's ability to pay.

The purpose of debt adjustment rules is to make it possible for a physical person, under court supervision and protection, to draw up and follow a plan for repayment of his debts over a limited period. In some cases the plan relates to full payment. In others, it may offer a certain percentage (possibly right down to nil) as full payment. When the debtor has completed the plan, he receives discharge of the debts then outstanding. Hence the debt adjustment procedure does not involve automatic remission of the debtor's debts. The debtor must pay as much as he can; the court makes an assessment of his ability to do so.

For creditors, a debt adjustment procedure has clear advantages compared with a bankruptcy which ends in discharge, since the possibility of obtaining any payment at all increases. In addition, the rules are so designed that creditors cannot obtain less through debt adjustment than they would from bankruptcy. The procedure has advantages for the debtor, too: he avoids being declared bankrupt and can himself actively help put his finances on a better footing.

For Swedish law, however, the argument has carried less weight, partly because a small businessman may find it hard to avoid personal payment engagements even if he runs his business in limited company form. See above, note 10.

Rules on debt adjustment without connection with bankruptcy exist in American law in ch. 13 of the 1978 Bankruptcy Code (Adjustment of Debts of an Individual with Regular Income).[26] A predecessor of the institution was introduced in 1938 in Chap. XIII of the Bankruptcy Act then in force.

The legislator has attempted to encourage consumers to choose debt adjustment rather than bankruptcy, primarily by making the debt adjustment rules more advantageous for the debtor (more types of debt covered, fewer exceptions), but also by empowering the courts to reject a plea in bankruptcy from a debtor who has mainly consumer debts, if the court finds that debt adjustment is to be preferred.

The English debt adjustment institution, the administration order, regulated in the County Courts Act of 1984, originates from 1883 and somewhat resembles the American one, but is of narrower scope in that it sets a fairly low limit (£5,000) for the debt. The institution has been called "the little man's bankruptcy".[27]

In Denmark an institution of debt adjustment was introduced in 1984, inspired by Anglo-American experience.[28] Note that Denmark, like the other Nordic (and most Continental) countries has no rules on general discharge in connection with bankruptcy.

As mentioned above, rules on discharge in connection with bankruptcy were introduced into French law in 1985. A special debt adjustment procedure was added recently through the *Loi n° 89–1010 de 31 dé-*

[26] See for the American debt adjustment procedure *Rep*, p. 135, 137 ff and e.g. *Collier on Bankruptcy* (above, note 21) vol. 5, New York 1989, ch. 13; Butler & Morris, *Emory L.J.* vol. 28 (1979) p. 759 ff. Comment, *Wisconsin L. Rev.* 1981 p. 333 ff; Hughes, *North Carolina L. Rev.* vol. 58 (1979–80) p. 831 ff; Riesenfeld, *Cases* (above, note 18) p. 778 ff; Sward (above, note 19) p. 407 ff; Wickham, *North Carolina L. Rev.* vol. 58 (1979–80) p. 815 ff, and Nimmer, *Law and Contemporary Problems*, Spring 1987, p. 89 ff.

[27] *Rep*, p. 145 ff. See e.g. Grenville (above, note 22) p. 335 ff. and *Insolvency Law and Practice*, Report of the Review Committee, Cmnd 8558, 1982 (the Cork Report) p. 23 f., 43 ff., 72 ff.; Fletcher, *Journal of Business Law* 1983 p. 98 f.; Samuels, *New Law Journal* 1977 p. 731 f.; Thompson, *New Law Journal* 1976 p. 329.

[28] See for the Danish institution of debt adjustment *Rep*, p. 106 ff. and *Bet* nr 957/1982 om Gældssanering, Munch, *Konkursloven med kommentarer* (Bankruptcy Act with annotations), 6 ed. (Copn) 1988, Hindborg, *Gældssanering i praksis*, (Copn) 1990, Ørgaard, *Betalingsstandsningsreformen af 1984*, (Copn) 1984 p. 18 ff, and von Eyben in *Festskrift till Hessler*, 1985, p. 161 ff, ibid. *UfR* 1985 B p. 337 ff; Polack, *UfR* 1985 B p. 382 ff.; Lyhne & Werlauff, *UfR* 1986 B pp. 209 ff., Andrup & Meyhoff, *UfR* 1986 B pp. 215 ff., Dybdahl & Rasmussen, *UfR* 1988 B p. 260 ff; Duus & Elmer, *Juristen* 1984 p. 213 ff; Mette Christensen, *Pantefogden* 1985 p. 37 ff.; Holm, J.A. Andersen, Espersen, Esdahl and Grubert in *Fuldmægtigen* 1985 p. 16–36, J.A. Andersen, *Fuldmægtigen,* 1986 pp. 1 ff, and 1987 pp. 1 ff.

Proposals for legislation on debt adjustment are now under preparation in both Finland and Norway.

cembre 1989 relative à la prévention et au règlement des difficultés liées au surendettement des particuliers et des familles, which came into force on 1 March 1990.[29] Here the debt adjustment procedure is of a somewhat different design, largely because, with certain exceptions, it cannot include any writing-down of the debtor's debts. Instead, the idea is that the debtor receives a breathing space through a respite for a certain period.

A further variant is proposed in the planned German insolvency law reforms through the rules on *Restschuldbefreiung*, which represent a form of debt adjustment after bankruptcy, i.e. a combination of the two forms of debt discharge. To be discharged from liability for debts remaining after a bankruptcy, the debtor must first pay these off as best he can for a period of seven years after the bankruptcy.[30]

Thus there are several different ways of designing rules intending to ease the debtor's burden. One model, which exists in the USA, England and France, is that the debts more or less automatically cease after bankruptcy. Another model is debt adjustment after bankruptcy, which implies that the debts do cease after the bankruptcy, but not until after a debt adjustment procedure of the type proposed in the planned German reforms. A third model is an independent debt adjustment procedure with possibilities for writing-off or writing-down the debtor's debts independently of bankruptcy. A debt adjustment institution of this kind exists in the USA, England and Denmark.[31] Lastly, a fourth model, a variant of the latter, was hinted at: a debt adjustment procedure, independent of bankruptcy, with adjustment possibilities primarily through respite and similar measures. This model has recently been introduced in France.

In Sweden, the Insolvency Commission has proposed a debt adjustment institution which, independent of bankruptcy, will permit writing-down of the debtor's debts, not only respite. The closest pattern is the Danish procedure, which in turn was inspired by the Anglo-American equivalents.

To propose general debt discharge after bankruptcy appears at present to be too drastic; nor does the Commission see any advantages in having debt adjustment tied in an obligatory manner to bankruptcy. As

[29] See *Rep*, p. 148 ff. and refs.

[30] *Rep*, p. 151 ff. with refs, and e.g. Gravenbrucher Kreis, *ZIP* 1990 p. 478; Uhlenbruck, *MDR* 1990 p. 4 ff; Wochner, *BB* 1989 p. 1065 ff.

[31] In Danish law there is also the possibility of using the debt adjustment institution in connection with bankruptcy, secs. 231–237 DKL, but this possibility has not been used to any large extent. *Rep*, p. 254.

opposed to this, there is naturally nothing to prevent a debtor requesting debt adjustment after completed bankruptcy proceedings.[32]

3.2. Some notions underlying the proposal. Pacta sunt servanda and general readiness to pay

In the Report, the proposed institution of debt adjustment is compared to a compulsory remission, conditioned by economic and social considerations and decided upon by an authority.[33] Thus it is not a question of an economic agreement between the debtor and his creditors, but the winding-up of a debt after a court hearing. The winding-up means the debtor being wholly or partly released from liability to pay his debts. The court must make an aggregate assessment of the debtor's ability to pay within the foreseeable future and decide what he should reasonably be able to set aside for payment of his debts. As opposed to the case in bankruptcy, the focus in debt adjustment is primarily upon the debtor's future income and assets.[34]

On the other hand, the court is not to decide upon the reasonableness of different creditors' separate demands; it is only the combined burden of debt that is of significance. Hence no account is to be taken of the debtor's action in connection with the giving of credit, i.e. possible poor credit checking or unethical marketing of the credit. Questions of this nature will probably be regulated in a new consumer credit law instead.[35]

The Report stresses that debt adjustment must be based on an economic view. What is provided is essentially an alternative in the law of insolvency to bankruptcy and composition. The debtor must not be able to "gain" by requesting debt adjustment instead of pleading bankruptcy. His creditors (here meaning mainly those without preference) must be assured of gaining from the adjustment at least what they would have received if the debtor had been declared bankrupt instead.[36] At the same time, it should be noted that the proposal is intended primarily for debtors who have no distrainable assets.

A basic idea is that the procedure should make possible the debtor's economic rehabilitation, so that he can start afresh if he has failed in his

[32] *Rep*, p. 19, 252 ff., 267.
[33] *Rep*, p. 215.
[34] *Rep*, 202 f., 211, 213 f., 253, 265, 267, 319 f.
[35] *Rep*, p. 13 f., 56, 184, 205, 227.
[36] *Rep*, p. 20, 214, 223 f.

activities thus far.[37] It is maintained, however, that this does not prevent a social perspective from being applied to debt adjustment as well. Thus for example a debtor who has become an alcoholic in consequence of his unemployment and can no longer manage his large debts would, as a side effect of the debt adjustment, receive help to overcome his alcoholism. But it is not intended that debt adjustment should be used as a panacea for social problems.[38]

The institution of debt adjustment is based on the debtor's showing willingness to pay his way in the future. Debt adjustment must only be considered for those who have always intended to pay their debt but who later, because of essentially altered circumstances or unforseen events, cannot manage to repay.[39]

It is important to stress that a debtor cannot claim debt adjustment as a kind of right when he has incurred sufficiently large debts. Ultimately, there must be an assessment of reasonableness regarding all the circumstances in the individual case.[40]

From the creditors' point of view it is essential to underline that writing-down can apply only to debts judged impossible to collect. Thus debt adjustment is not to cause the creditor any substantial loss. On the contrary, it should bring creditors economic advantages in two respects: they can refrain from fruitless attempts to collect worthless claims, leading to reduced supervision costs. It may be hard for a creditor acting on his own to establish that a claim really is worthless. Secondly, creditors' chances of obtaining payment may increase when the debtor has an incentive to cooperate in his own economic shake-up. And if the debtor has no available resources his creditors would not get quicker payment through bankruptcy proceedings anyway.[41]

If the debtor is motivated to rehabilitate himself economically, i.e. manages to find employment (outside the black zone) and in future to pay new debts arising, instead of using the social, health and perhaps criminal services, there are also savings in costs—and reduced loss of tax revenue—for society.[42]

Thus far, then, one could say that the value for creditors of being able

[37] *Rep*, p. 202 f., cf. also p. 228, 253.

[38] *Rep*, p. 20, 223. According to sec 15 the court—before deciding on recourse to debt adjustment—shall obtain particulars from the social security authorities (and a statement from the collection officer).

[39] *Rep*, p. 19, 210, 304.

[40] *Rep*, p. 220 f.

[41] *Rep*, p. 18, 193, 211, 212 f., 228.

[42] *Rep*, p. 18, 21, 192f., 248 f.

to retain their claims, worthless on the best assessment, bears no reasonable proportion to the social costs and the debtor's and his family's suffering which his—in many cases life-long—indebtedness entails.[43]

Another question, however, is what importance to ascribe to objections that the debt adjustment concept conflicts with the thesis *pacta sunt servanda*, or that the possibility of obtaining debt adjustment can have an adverse effect on general readiness to pay.

As an argument in legal discussion, reference to *pacta sunt servanda* is, on a closer look, fairly hollow.[44] Surely what the tenet as a legal rule can be said to mean is, rather, that what has been agreed shall stand unless an exception to this main rule is applicable. There are of course a number of such exceptions: the beneficiary rules in distraint and bankruptcy represent one.[45] Another is the possibility of adjustment of contracts owing to altered circumstances.[46] One purpose of the legislation on debt adjustment is precisely to set up such an exception from the main rule. It can be stressed that there is no question of the debtor being allowed to avoid his payment undertakings on his own. Strict prerequisites are laid down and the case must be assessed by a court.

A reference to *pacta sunt servanda* may in reality be a way of clothing other arguments for the necessity of keeping agreements. In this case, however, these arguments should be discussed explicitly.[47] One such argument can be that the possibility of debt discharge means that the creditor can hardly reckon on receiving any repayment, which makes the credit more expensive.[48] Against this argument it may be objected for example that debt discharge does not make any difference to the creditor if the debtor *cannot*, anyway, pay more than what the creditor would get through the debt adjustment decision.

Debt adjustment should not, either, have any weakening effect on the general readiness to pay, if the rules are so designed that, first, they make it plain that adjustment is not a right which a debtor can commonly count on receiving; but that it can be granted—in theory only once—on strict conditions, by a court decision. Secondly, that the decision means that the

[43] Statement taken from the German *travaux préparatoires*. *Referentenentwurf* (above, note 6) p. A 33, B 232. *Rep*, p. 153.

[44] See on this point Hellner, "Pacta Sunt Servanda" in *Samfunn Rett Rettferdighet, Festskrift to Torstein Eckhoff*, Oslo 1986, pp. 335 ff., esp. pp. 335, 338, 342 ff.

[45] See on these *Rep*, p. 77 ff.

[46] This aspect is developed specially in the Danish *travaux préparatoires*, *Bet* 957/1982 p. 77 ff. See also Weistart, *Law and Contemporary Problems*, Autumn 1977 p. 111 f. and the discussion p. 160 f; and Nimmer, *Law and Contemporary Problems*, Spring 1987, p. 89.

[47] Hellner, *op.cit.*, p. 344.

[48] Thus Uhlenbruck, *MDR* 1990 p. 9.

debtor must pay as much as he is able during the next few years, and, thirdly, that sanctions can be employed if, for example, the debtor gives incorrect information on his financial and personal circumstances. In Denmark, no weakening of the readiness to pay as a consequence of the institution of debt adjustment has been observed.[49]

4. DETAILS OF THE PROPOSED DEBT ADJUSTMENT INSTITUTION

4.1. General. Creditors' influence, etc.

As has emerged above, the decision on debt adjustment is to be based on the notion that the debtor's debts are either cancelled or written down by a certain percentage (Draft Bill sec 2, para 2). As a rule the debtor should be charged with paying his creditors at least something.[50] In the debt adjustment decision, the court is to fix a payment plan, normally covering five years (sec 27, para 1, pt 3).[51]

According to sec 6 of the Draft Bill, adjustment may be granted to a debtor who is a physical person and who is not engaged in commerce. As indicated by way of introduction, the institution of debt adjustment is intended for ordinary private persons (credit consumers) and for those formerly engaged in commerce.[52]

A debtor formerly engaged in commerce must have entirely ceased to do this, and the Commission do not wish to allow any form of part-time activity, either. If the debtor is managing his business, bankruptcy is a more suitable recourse. Debt adjustment is intended to be a quick, simple and inexpensive procedure, not to be hampered by, for example, the necessity of winding up an estate.[53]

If the debtor continues his business covertly, so that, for example, it is formally managed by a relation or close friend, debt adjustment should be refused, with reference to the special assessment of reasonableness covered in sec 7 (see below).[54]

Sec. 6 para 2 states that a debtor who has been served with an injunction against carrying on a business, according to the Disqualification Act of 1986, during the previous five years may not be granted debt

[49] Cf. *Rep*, e.g. p. 14, 19, 212 f., 273 and p. 107, 213 (for Danish law).
[50] *Rep*, p. 242.
[51] *Rep*, p. 318.
[52] Above, sec 2. *Cf. Rep*, p. 184.
[53] *Rep*, p. 217 f., 272, *cf.* p. 264. See text accompanying note 106 f. below.
[54] *Rep*, p. 272 f and p. 280 ("circumstances when the debts arose").

adjustment. It is also stressed that a debtor cannot in theory be granted debt adjustment more than once.

If the wishes underlying the institution of debt adjustment are to be met, the procedure advocated by the Commission cannot be voluntary.[55] It must be possible to make the decision irrespective of the creditors' desires. It is because the procedure will thus include intervention in relation to individual parties, and between individuals and the public interest, that the task of deciding upon debt adjustment has been entrusted to a court, which must be presumed to have the required competence, can be perceived to be impartial and also has sufficient local connection.[56]

That competence lies with a court and that decisions can be taken against the wishes of the creditors does not, however, imply that the latters' views are of minor significance. On the contrary, the creditors' view of the debtor's request for debt adjustment should be allowed weight in several respects.[57] One example of this is where there are particular types of claim such as damages, fines and study loans, but there are also other examples. If the large majority of creditors are without objection to the debtor's application, the court's examination of the matter can be correspondingly limited. If on the other hand the majority have strong objections, this can give the court reason to examine the matter with especial care.[58] The Draft Bill also provides that creditors are to be informed when debt adjustment is introduced and that they shall have opportunity to present their views.[59]

4.2. Prerequisites for debt adjustment

4.2.1 Introduction.

The prerequisites for granting an application for debt adjustment are given in sec. 7 which, according to the Draft Bill runs:

> An application for debt adjustment may be granted if,
>
> 1. the debtor is so indebted that he is unable to pay his debts within a foreseeable period and
>
> 2. there are special reasons with regard to the debtor's personal and economic circumstances.

[55] *Rep*, e.g. p. 18 f., 202 f.
[56] *Rep*, p. 20, 201 ff., 233 ff.
[57] *Rep*, p. 267.
[58] *Rep*, p. 231 f.
[59] Secs 21, 24 and 25. *Rep*, p. 267.

> In the examination according to para 1, point 2, particular attention shall be paid to the debtor's need of economic rehabilitation, the age of the debts, the circumstances under which they arose and the way in which the debtor has attempted to fulfill his obligations to pay and has cooperated during the processing of the debt adjustment case.

A difficult question of legal technique is naturally how the prerequisites can be formulated suitably. The choice is mainly between a strict rule expressly specifying the various requirements (e.g. how large the debtor's debts must be), and a more flexible rule. Of the greatest significance in this choice must be the question of how abuse of the regulation can best be avoided. By abuse is meant chiefly that a debtor may intentionally attempt to fulfil the conditions necessary to make him eligible for debt adjustment (incur sufficiently large debts, etc). Strictly specified requirements may invite such exploitation of the rules. Then again, it is almost impossible to foresee all the situations that may arise. The Commission have therefore elected to follow the flexible Danish line, which appears to have worked well in practice. Here—apart from a qualified criterion of insolvency—a "reasonability requirement" is established, which however, is specified in the second paragraph of the provision where the circumstances to be observed in the assessment are expressly stated. As stated in the Report, the general reference to the debtor's circumstances is in this way given a tangible content and application of the law is thereby directed towards scrutiny of certain circumstances that may be objectively established.[60] The assessment of reasonableness shall cover all circumstances and the judgment of all the points specified in the second paragraph must be in the debtor's favour.[61]

It is up to the debtor himself to show that the factual circumstances are such that debt adjustment should be granted.[62]

4.2.2 The qualified insolvency requirement

It follows from sec 1 of the Draft Bill that a debtor who is insolvent can apply for debt adjustment. "Insolvency" refers to a debtor who cannot duly pay his debts, provided that this inability to pay is only temporary, 1:2 KL (Bankruptcy Act). Temporary inability to pay can exist for

[60] Rep p. 222. See *Rep*, p. 219 ff. See also *Bet* 957/1982 (DK) p 80 ff., 94.

[61] *Rep*, p. 221, 278. That the circumstances are in the debtor's favour need not in fact mean that the application is granted: the court is not obliged to grant debt adjustment ("may"). *Rep*, p. 278.

[62] *Rep*, p. 14, 221 f., 279.

example when the debtor has in fact sufficient assets to pay his debts but these are bound and it may take a certain time to realise what is needed.[63] The period intended by "temporary" is not specified, but it should naturally be relatively short.

The insolvency prerequisite is further defined in sec. 7, para 1 point 1 of the Draft Bill. For an application for debt adjustment to be granted, it is required that the debtor be so indebted that he cannot pay his debts within a foreseeable time. Thus this constitutes a qualified insolvency requirement.

In Swedish law the normal assessment of insolvency is also based on a more or less long-term forecast (except for cases where claims already due exceed the value of the debtor's assets), in which the decisive question is whether the debtor, despite the use of all conceivable resources, must be deemed incapable of paying his debts as they fall due.[64] As to how *long* insolvency must last, there is no requirement. The qualified insolvency requirement specified in the Draft Bill on Debt Adjustment means, however, not only that the debtor shall be insolvent in the usual sense but that his payment ability must be expected to last a fairly long time, i.e. either permanently or at least for a foreseeable period (5–10 years).[65]

The case where the debtor through sickness or accident has been rendered completely incapable of work in the future is a clear example of the situation intended in the provision. In other cases it may be rather more difficult to estimate the future inability to pay. The court shall, however, make an all-round assessment with regard to the size of the debts, the debtor's age, occupation, education, family circumstances, etc. One point of departure must, for example, be that the debtor shall use the training he has, unless there are special medical or labour-market circumstances.[66] If the debtor's future occupation and income are uncertain, this argues against debt adjustment. In Danish

[63] *SOU* 1970:75 p. 75. Walin & Palmér, *Konkurslagen* (The Bankruptcy Act), 1989, p. 12.

[64] Welamson, *Konkurs* (Bankruptcy) 8th edn., 1980, p. 20; ibid. *Konkursrätt* (The Law of Bankruptcy), 1961, p. 47 f.; *SOU* 1970:75, p. 60 f.; *cf.* Govt. Bill 1975:6 p. 116; Walin & Palmér *ibid*, and e.g. *DsJu* 1983:17 p. 49 f.

[65] *Rep*, p. 14, 187, 221, 266, 274 ff.

[66] *Rep*, p. 275 f. Concerning the question of what work a debtor shall be considered obliged to take, a comparison can be made with, e.g., the assessment made when fixing child maintenance, *Rep*, p. 276. Cf. also the corresponding assessment in connection with the question of exclusion from unemployment benefit (on this, Anna Christensen, *Avstängning från arbetslöshetsersättning* (Exclusion from Unemployment Benefit), 1980.

practice, debt adjustment has been refused on these grounds, e.g. in the case of debtors who at the time of application have started new training.[67] Naturally, special care must be taken in the case of young debtors.[68]

How large the debts shall be in absolute figures is not specified—the relative assessment is naturally the most important—but reference is made to Danish law where, as a guide, net indebtedness of about DKR 250,000 for those in full-time employment has been required and about DKR 100,000 (the absolute minimum appears to be DKR 50,000) for pensioners and other persons without work.[69]

4.2.3. The requirement as to reasonableness

In the assessment of reasonableness under sec 7, para 1, point 2, the court shall observe particularly the circumstances specified in the second paragraph.

The first circumstance is *the debtor's need of economic rehabilitation.* As stressed earlier, the approach shall be primarily an economic one. A need for economic rehabilitation obtains above all where there is an obvious disproportion between burden of debt and ability to pay. However, it is also important that the debt adjustment can spur the debtor to improve his economic situation, e.g. by re-training for a job at which he can support himself, thus paying his way from then on.[70]

If there is reason to presume that the debtor's economic situation will continue to be uncertain and precarious after debt adjustment, for example where it can be foreseen that he, because of various undertakings will have to incur new debts in the future, the application has as a rule been refused in Danish practice.[71]

The age of the debts should according to the Report be given considerable significance.[72] Normally, of course, it ought not to happen that a debtor who has incurred large debts, e.g. through extensive use of a

[67] V 1743/86, 6 afd. (Vestre Landsret), Ø 175/85, 16 afd. (Østre Landsret), Hindborg (above, note 28) p. 65, 67.

[68] In Danish practice, debt adjustment has been granted to a 25-year-old divorcee with two minor children, unemployed and without training. Her debts originated from a course of training terminated some five years previously, and it was considered that her income circumstances would not improve essentially in the foreseeable future. V 747/86, 7 afd., Hindborg p. 25.

[69] *Rep*, p. 14, 276 f. Hindborg p. 24, 28.

[70] *Rep*, p. 223 f., 278 f.

[71] Hindborg, p. 34, 68.

[72] *Rep*, p. 224 f., 279.

credit card, should be released from his payment liability after only a few years. On the other hand, if there are large debts of older standing, which the debtor has been labouring to pay for a number of years, the age of the debts is a point in favour of debt adjustment. This applies even more if the indebtedness stems from an earlier business which has since ceased.[73] One is reluctant to specify any times regarding the age of the debts. Normally, however, a number of years must have passed since the first sign of over-indebtedness appeared.[74]

Debt adjustment should not be excluded only because one or more debts—as opposed to the major part of the indebtedness—are of more recent date. If however the debtor has incurred large debts shortly before the application for adjustment, or even thereafter, this can be a point against debt adjustment.[75] On the subject of Danish practice an example can be mentioned of a case where the debtor, shortly before the application, had bought a new car for DKR 120,000 on credit without having any particular need of the car in his work or for other reasons,[76] or a case where the debtor, following the application, had bought a radio, colour television and a solarium on credit for a total of DKR 45,000.[77] That the debtor has taken a loan to manage his living costs, etc., need not, however, according to Danish practice, prevent the prerequisites for debt adjustment from being considered as fulfilled.[78]

The circumstances under which the debts arose naturally play a very important part.[79] Of fundamental significance is that criminal, unfair and speculative debt incurrence shall not be rewarded.

Particular attention is given in the Report to how claims for damages shall be treated. One possibility would be for the court to refuse debt adjustment if the debtor is liable for indemnity, at least because of a crime; another would be simply to remove claims for damages from the scope of the Act. However, the Commission did not find either alternative attractive. The former cannot, naturally, apply without exception and the latter (i.e. that certain claims shall remain in their entirety) can lead to the concept of debt adjustment disappearing altogether.[80] The

[73] *Rep*, p. 279.
[74] *Rep*, p. 225, 279.
[75] Cf. *Rep*, p. 19 f., 225.
[76] V 79/89, 2 afd., O/ 408/86, 16 afd., Hindborg p. 34 f.
[77] V 737/85, 3 afd., Hindborg p. 55.
[78] V 2490/85. 4 afd., Hindborg p. 36.
[79] *Rep*, p. 20, 225 ff., 279 ff, cf. p. 218.
[80] *Rep*, p. 226 ff. Cf also the adjustment rule in the Swedish Torts Act ch. 6 sec. 2.

conclusion is therefore that each case must be judged on its merits. Naturally, such a judgment should be very restrictive, particularly when it concerns damages in relation to an individual plaintiff as a consequence of serious criminality.[81]

In Danish practice, debt adjustment has been refused in a long series of cases because the debtor has incurred a substantial part of his debts in transactions of a speculative nature or because his debt incurrence has exhibited such economic frivolity and irresponsibility that there should be no question of debt adjustment, and also where the debts have arisen through luxury purchases (a condominium in Spain, a large motor boat, etc.).[82]

Finally, the provision states that particular account shall be taken of *the manner in which the debtor has attempted to fulfil his payment obligations* and *cooperated during the treatment of the debt adjustment case*.[83]

The manner in which the debtor has attempted to fulfil his payment obligations may afford a good picture of how deserving his case is. This requirement leads to the exclusion, for example, of all debtors who have accumulated large debts without even trying to repay them. Debt adjustment should naturally be refused if the debtor has used what income he has had for large private consumption or for the purchase of property in the names of family or friends, instead of making payments on his debts. Similarly disqualified are debtors who have knowingly withheld creditors' property, for example by making it over to their spouses. Aggravating circumstances also obtain if the debtor has chosen to make payments only on those debts for which his family and friends stand guarantor. Conversely, it is in the debtor's favour if he has made great efforts to comply with a repayment plan, etc.

The debtor's own action during the handling of the debt adjustment case may in certain cases lead to his application being rejected. Examples are that the debtor has given misleading information regarding his finances, has remained silent concerning significant circumstances or refuses to give information regarding circumstances judged to be important in the case.

Finally, the Report lists as a summary examples of a number of possible cases where application for debt adjustment should appropriately be granted or rejected.[84]

[81] *Rep*, p. 228.
[82] Hindborg p. 40 ff.
[83] *Rep*, p. 230 f., 281. Example from Danish practice in Hindborg p. 50 ff.
[84] See *Rep*, p. 282 ff.

4.2.4. Details of the claims covered by the debt adjustment procedure

According to the main rule in sec. 8 para 1 of the Draft Bill, a decision on debt adjustment covers all claims on the debtor which have arisen before the day on which the court ordered the introduction of debt adjustment. The decree on the introduction of debt adjustment represents an important point in the timing of the procedure (see below, sec 4.3).

The question of the point at which a claim has arisen must be judged using the same guidelines as the corresponding requirement in 5:1 KL (Bankruptcy Act) which defines the concept of "bankruptcy debt" (and sec. 12 *Ackordslagen* (The Composition Act)).[85] The situations are fairly analogous. Certain claims hereby fall automatically outside the scope of the decision. This applies specially to claims relating to future maintenance contributions, which on the view now adopted must be considered to arise successively, as do claims on future rent.[86]

It follows from what has been said that claims not yet due, and conditional claims, are also theoretically covered by debt adjustment. Since, however, special problems can arise concerning such claims, sec. 9, para 2, point 3 empowers the court to rule, on reasonable grounds, regarding these claims.[87] This means that parts of a claim not yet due, and a conditional claim, e.g. regarding a guarantee undertaking on the part of the debtor,[88] may in some circumstances be excluded from the adjustment (cf. below regarding study loans).

The decision may also be limited to claims that have arisen before a given date other than that decreed by the court for the introduction of debt adjustment. A typical example can be that the decision refers to debts from an earlier business activity which ended in bankruptcy, but not to debts subsequently incurred by the debtor.[89]

No separation between different claims is permitted on other grounds than those mentioned. Thus the court cannot decide upon complete cancellation of certain debts (e.g. those remaining after liquidation), or percentage reduction of others (e.g. debts arising subsequently).[90]

[85] *Cf. Rep*, p. 285 f.
[86] *Rep*, p. 229, 286.
[87] *Rep*, p. 229 f,, 286, 290.
[88] *Rep*, p. 243, 290.
[89] *Rep*, p. 15, 224 f., 267 f., 287. See also p. 268 regarding debts remaining after an compulsory sale of property.
[90] *Rep*, p. 287.

The Commission maintain as an important matter of principle that all types of debt should be covered by the debt adjustment procedure, both those under private law and those under public law. All creditors involved have equal rights (sec. 9, para 1). The principle of equal treatment applies.[91] (An exception can be made only for claims not yet due, etc, as just mentioned: see sec. 9 para 2).

Should certain types of claim be excepted, for example *tax demands*, this could easily lead to debt adjustment becoming a half-measure. The burden of debt for a person formerly engaged in commerce may consist largely of tax debts, and if these were excluded, the debtor's economic rehabilitation would not mean much. On the other hand, the nature of certain claims makes it by no means evident that they should be included in a debt adjustment decision. What may occasion doubt in the case of tax debts is that they would have had general preference if the debtor had been declared bankrupt. Now, a creditor with a preferential claim does not share in public composition unless he abstains from his right of preference, sec. 12 *Ackordslagen* (Composition Act). At the same time, however, debt adjustment can represent an advantage to the State as tax creditor over a longer period. The purpose of tax adjustment is to give the debtor a chance of economic rehabilitation, rendering him capable of paying his way in the future, for example when he is to pay future tax debts. A debtor who is suitable for debt adjustment normally has no assets to speak of, which means that the general right of preference enjoyed by the State would not have given the state any sizeable sums; in brief, abstaining from the right of preference need not entail any great loss. Should the debtor in one case or another have assets, or should the State consider debt adjustment particularly undesirable, there is always the possibility of having the debtor declared bankrupt.[92]

Study debts, especially in the form of repayable funds for study, raise two questions. The first is whether such debts shall be covered by debt adjustment. The second is, if so, how reduction shall be effected.[93]

The system of study loans, grants, etc. was reformed with effect from 1 January 1989. Under the old system, the loan must be repaid through annual payments depending on the size of the debt and the number of repayment years. The new system involves annual repayment with a sum corresponding to four percent of the borrower's income. Thus, repayment periods can be very long.

[91] *Rep*, p. 203, 205, 208, 226, 228, *cf.* p. 13.
[92] *Rep*, p. 203 ff.
[93] For study funds, see *Rep*, p. 86 ff., 206 ff., 230.

The treatment of study debts was a greatly-discussed topic during the preparation of the American bankruptcy reform,[94] the main point of discussion being the possibility of discharge after bankruptcy. According to some arguments, it would be too easy for a student with few assets to go bankrupt and thus get rid of his study loans: since the purpose of the loan was to increase the debtor's future earning capacity, there should at least be a time requirement that would enable a court to see whether the debtor was going to have any use of his studies. Other arguments, however, were that study loans should be treated like any other loans. The result was a compromise. Educational loans made, insured or guaranteed by a governmental unit, or made under any programme funded in whole or in part by a governmental unit or a non-profit institution are *excepted* from discharge under two conditions: that the first due date for the loan fell at least five years before the bankruptcy plea, and that the exception is not too hard on the debtor and his dependents. Payment liability for study loans whose first due date fell more than five years before the bankruptcy plea thus ends after bankruptcy. In addition, it may be repeated that the exception does not apply to all study debts.

However, this discussion was *not* carried on in connection with the rules on discharge after debt adjustment proceedings (chap 13 BC), where no exception whatsoever is made for study debts.[95] The conclusion is easy to draw. Since in debt adjustment proceedings express account shall be taken of the debtor's future earning capacity, there is no reason to except study debts; the reservations that arose over the question of discharge after bankruptcy are, so to speak, cleared up in this case.

The Insolvency Commission also reaches the view that study loans and grants (and other study debts) shall not be excepted from the scope of a Debt Adjustment Act. Even if the study loan has been intended as a long-term investment to give dividends later in life in the form of a higher salary, this investment is nevertheless a poor one if it turns out that the debtor cannot use what his studies have given him because he has been afflicted by a protracted illness or a catastrophic change in his profession, etc.[96] The key question in the debt adjustment procedure is whether the debtor has any long-term prospect of being able to pay. If it can be expected that the debtor can obtain well-paid work in the future,

[94] See *Rep*, p. 136 with refs.; sec 523(a)(8)BC.
[95] *Cf.* sec 1328 BC; *Rep*, p. 140.
[96] *Rep*, p. 206 f.

it is meaningless to grant debt adjustment. To counter abuse, clear evidence should be required that the debtor cannot benefit from the result of his studies in the foreseeable future. There are often grounds for requiring that a considerable time shall have elapsed since the conclusion of studies.[97]

The relief from payment liability for study debts so far aimed at applies primarily to payments on the study loan that have already fallen due. Regarding payments that have not yet become due, the general provision in sec. 9, para 2, point 3 become of interest. According to this, a court is empowered to decide, on reasonable grounds, regarding claims that have not yet become due. This means that the court can elect to reduce already due sums; or to also reduce the items that become due during the validity of the payment plan, or to reduce the whole loan, i.e. including items that become due subsequently.[98]

To conclude this section it may be mentioned that a *right to security* which the creditor has in the debtor's property survives debt adjustment. To the extent the creditor's claim is secured, the claim shall thus not be reduced. By security is meant, according to sec. 8, para 2, pledge, mortgage and lien. The same applies to reservation of title clauses, etc.[99]

If instead the debtor's security is in the form of guarantee or collateral made available by a third party on behalf of the debtor, the debtor's payment liability is reduced in the normal manner, but on the other hand the creditor's claim on the guarantor, or on another party who is responsible for the debt jointly with the debtor, continues to apply unchanged, sec 28, para 3. The lien on the property of a third party naturally also continues to apply after debt adjustment. That the guarantor's and the co-debtor's payment liability vis-a-vis the creditor is not affected by debt adjustment corresponds to what is provided concerning public composition in sec 21 of the Composition Act. The principle is a logical one, since a third party has (more or less voluntarily) accepted some responsibility for the debtor's ability to pay and the debt adjustment decision can be considered to have established that the debtor cannot pay more than what is thus enjoined upon him.

As against this, the guarantor's and the co-debtor's recourse against the debt adjustment debtor is reduced in the same way as all other claims, sec 28, para 1, point 2. Where the debtor is charged to pay, for example, 20% of the debt, this must mean that the creditor and the

[97] *Rep*, p. 208 f.
[98] *Rep*, p. 230.
[99] *Rep*, p. 13, 205, 232 f., 287 f.

person with the right of recourse can *together* demand payment of 20% of the sum claimed.

Set-off is permitted according to general rules of private law. The Bankruptcy Act rules on set-off in bankruptcy do not apply.[100]

4.3. The procedure, etc.

The procedure is divided into three steps.[101] The *first* involves a rough screening in which erroneous applications are rejected (sec 14). If the application is accepted, the *second* step follows, and this consists of deciding whether debt adjustment is to be introduced at all (sec 15). The court shall ensure that the matter is sufficiently examined (sec 16).[102] Statements shall be sought from the enforcement service and information from the social welfare board (if considered necessary), (sec 15, paras 2 and 3). Negotiations are possible (sec 17). The application shall be rejected if there is no due reason to assume that debt adjustment can be established (or if the debtor does not personally attend the negotiations just mentioned) (sec 19). Otherwise, debt adjustment is started. The intention is that most applications which are going to be rejected, should be rejected at this early stage of the proceedings.[103]

If debt adjustment is introduced, no executive measures against the debtor may be taken for the time being in respect of claims arising prior to the decision and included therein (sec 20).

If necessary the court can appoint a trustee to help the debtor sort out his personal and economic circumstances and to produce proposals for clearing the debts (sec 13). While the trustee can be appointed at different times, the appointment is probably less frequent at the application stage and more so once it has been decided to introduce debt adjustment.[104] The debtor can also obtain help from the enforcement service and the social welfare board.[105]

The *third* step leads to a possible decision on debt adjustment. The debtor must now submit a proposal for clearing his debts (a payment

[100] *Rep*, p. 290. *Cf.* below, section 4.3 regarding recovery. Since the Debt Adjustment Act contains no rules on recovery, it ought not to contain any rules corresponding to the those on set-off in the case of bankruptcy either. These, after all, as regards 5:16 of the Bankruptcy Act, are closely related to the recovery rules.

[101] See *Rep*, p. 236 ff, the explanatory notes to the provisions stated; and p. 15, 21.

[102] *Rep*, p. 15, 238 f., 280 f, 294, 299 f.

[103] *Rep*, p. 303, cf. p. 282.

[104] *Rep*, p. 294 f.

[105] *Rep*, p. 295.

plan) (sec 23). The plan is studied during a hearing to which the debtor, known creditors and the trustee (if there is one) shall be called (secs 24, 25). The court then decides whether the application for debt adjustment is to be approved or rejected (secs 26, 27).

The decision on debt adjustment is binding on all creditors, including unknown ones (sec 28, para 2).

The decision may be reviewed under special circumstances (secs 30, 31). The decision can be quashed if for example the debtor has seriously disregarded his obligations under it.

As should now be clear, the institution of debt adjustment is intended primarily for debtors without distrainable assets. The intention is for the procedure to be quick, simple and inexpensive, naturally without disregarding considerations of legal security.[106]

For this reason the proceedings should not be encumbered with any real treatment of estate. As stated above, it is thus not suitable for those actively engaged in commerce.[107]

Nor should the procedure be encumbered with time-consuming and costly investigations of other types. Thus it is proposed in sec 22 of the Bill that disputed claims shall be dealt with as if they were not disputed: the court shall not carry out any enquiry into the debtor's objections.[108] The parties must, instead, seek litigation on this point in the normal manner.

The foregoing also introduces the circumstance that the Bill lacks rules on recovery of the type that exist for bankruptcy (and composition). If there is reason to assume that there has been some circumstance that could occasion recovery in bankruptcy proceedings (cf. sec 16, point 4) the application for debt adjustment should instead, depending on circumstances, be rejected.[109]

5. CONCLUSION

An important question the Commission has had to observe is how to design the rules on debt adjustment so that the institution will not be abused or have a poor influence on general readiness to pay. One of the purposes of the foregoing presentation has been to show how the Commission has proceeded in the solution of this problem.

[106] *Rep*, p. 21, 236, 238, 264.
[107] See text accomp note 53 above.
[108] *Rep*, p. 242, 308 f.
[109] *Rep*, p. 263 ff, 278.

Of particular interest, of course, is the success met with by the corresponding Danish institution. W.E. von Eyben, in an essay some years ago, maintained that the Danish bill on debt adjustment resulted in solutions which seemed shocking but which were implemented nevertheless, largely with good results that have led to improvements.[110] It is to be hoped that it will be possible to say something similar about the Swedish Bill.

[110] von Eyben, "Kampen mellem kreditorerne" (The Struggle among the Creditors), i *Armannsbók, Festskrift udgivet i anledning av Armanns Snævarrs 70 års fødselsdag* (Armann's Book. Memorial Volume published on the Occasion of Armann Snævarr's Seventieth Birthday), Reykjavik 1989, pp. 127 ff, on p. 147.