

Debt Management Guide: A Resource for Social Services Professionals

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(Resources used include Office of Consumer Affairs, Industry Canada; Office of the Superintendent of Bankruptcy Canada, Industry Canada; Financial Consumer Agency of Canada; and Ministry of Consumer Services, Ontario)

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INTRODUCTION

Debt and money are a constant concern for many people living on low or fixed incomes. As a key resource for these populations, staff at community-based agencies are called upon to inform and counsel clients who struggle with debt. It is crucial that we, on the front lines of this issue, have at least a basic understanding of the debt and collections systems, and of a debtor's options and rights.

We are the most trusted source of information for many low-income debtors. Social service providers' advice and referrals may have long-term consequences for client's financial health.

HOW TO USE THIS GUIDE

We need to know what we're talking about. This Guide can help.

This Debt Management Guide was created to assist volunteers at WoodGreen's groundbreaking Debt Management Clinic, who meet one-on-one with community members to educate them on their options. It is now available for social services staff who want to know how to help clients deal with debt.

This Guide provides a comprehensive explanation of the options available to any debtor in Ontario, with practical advice about what may make the most sense for low-income debtors. It starts with a chart outlining options, and later explains these options in detail. Wherever this Guide isn't exhaustive, it will direct you to other sources that may provide further and more detailed information on any given topic.

It's wise to check web resources when working with clients on debt management, as policies, amounts, and rights may change from time to time. This Guide is accurate as of March 2012.

Elaine Magil
WoodGreen Community Services
March 2012



WoodGreen's Debt Management Clinic and this Guide are made possible by the generous support of our funder, the TD/SEDI Financial Literacy Grant Fund.



Personal Steps to Reduce Debt

Can you manage repaying this debt on your own?

1. Budgeting 6 (tracking expenses and ensuring they are within the person's means)

ADVANTAGES

- Informal
- Low cost
- Quick results (contacting creditors works well for temporary financial setbacks)

DISADVANTAGES

- May not be able to achieve the desired results in reducing debt
- Creditors may be unwilling to accept partial or reduced repayment
- Debtor may feel anxious or have linguistic barriers in communicating with creditors
- Creditors will retain the information the debtor provides them with and may limit or refuse future credit based on it
- Overall payment may actually be increased if the repayment period is extended without lowering the interest rate
- Costs money (significant administrative fees will be charged)"

MOST SUITABLE FOR

- Individuals who usually make most or all of their required payments, but are temporarily having difficulties with their finances
- People with at least some money available to use towards debt repayment

2. Contacting Creditors 7 (debtor makes special arrangements regarding his/her debt)

3. Selling Personal Assets and Possessions 9 (in order to pay off debt)

4. Dealing with Collection Agencies to 9 arrange settlements or payment plans

1. Making a Budget

When a person starts falling behind on payments or when his financial obligations exceed his means, it can be helpful to create a budget (or spending plan). This can help the person identify areas of overspending and possibly put that money towards paying off their debts.

Steps to Follow:

- 1) Evaluate one's personal financial situation:
 - a. What are the person's needs?
 - b. What is the state of the person's current financial affairs?
 - c. What is the person's attitude towards money?
- 2) Set financial and personal goals:
 - a. This involves setting short-term, mid-term and long-term goals and placing them in order of priority.
 - b. The goals must be realistic, have a determined time frame, and be specific and measurable.
 - c. Essentially, the three sub steps here are:
 - i. Identify the objectives,
 - ii. Prioritize the objectives,
 - iii. Establish the necessary actions to achieve these objectives.
- 3) Establish the budget:
 - a. The person should plan his/her income and expenses for a set period of time (can be done daily, weekly or monthly).
 - b. It is important that the budget is realistic.
- 4) Track one's expenses:
 - a. This can be done over a one month period (all expenses, big and small) or ideally even longer.
 - b. It may be helpful to keep all receipts.
- 5) Compare the budget with the real expenditures:
 - a. Any discrepancies should be carefully reviewed and addressed. For example, if a budget shows expenses less than income, ask the client whether they actually end the month with money left over.

There are many budgeting tools available on the internet. Check websites such as OSB Canada , Industry Canada - Office of Consumer Affairs , and Canadian Banker's Association.

² For more information see Industry Canada, Office of Consumer Affairs, online: <http://www.ic.gc.ca/eic/site/oca-bc.nsf/eng/h_ca02145.html>.

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If not, the budget is missing something and doesn't reflect the reality of their situation.

- b. This helps in identifying where the person overspends, and it also helps in making the budget more realistic and accurate.

6) Review the budget regularly:

- a. By constantly being aware of the budget the person learns to control their expenses, and is better at finding ways to improve their financial situation and realize their financial objectives.

There are many budgeting tools available on the internet. Check websites such as OSB Canada³, Industry Canada - Office of Consumer Affairs⁴, and Canadian Banker's Association⁵.

³ <<http://www.ic.gc.ca/eic/site/bsf-osb.nsf/eng/bro2049.html#steps>>.

⁴ Supra note 2.

⁵ <<http://cba.ca/en/consumer-information/41-saving-investing/57-managing-money>>.

2. Contacting Creditors

Another way to ease debt repayment is by making arrangements with the creditors for one or more of the following:

- Lower monthly payments
- Longer time period to make the payments
- Lower rate of interest

This option is most suitable for individuals who can commit to paying off some amount, either in a lump-sum or ongoing. Someone with absolutely no money available for debt shouldn't bother contacting creditors because there's nothing to arrange. If the total debt load and the number of creditors that the person owes money to is excessive, the creditors may not be willing to make any arrangements and other debt management options (such as those laid out in the rest of this Guide) may be more suitable.

Steps to follow:

- 1) First step is to make a list of the creditors to contact. Reviewing the budget may reveal which creditors need to be contacted in order to make the debt repayment more manageable.
 - a. If reducing the monthly payment for a single debt is enough, it won't be necessary to contact all of the creditors.
 - b. If there is a need to contact more than one creditor, the debtor could contact the creditors to whom they owe the largest amounts of money. This will have a greater impact on the monthly budget.

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- c. If there are any creditors who have contacted the debtor already in regards to defaults on their payments, the debtor may choose to contact those creditors first.
 - d. If there is default on essential services such as hydro, heat, or rent, then these may be the first creditors to contact in order to avoid possible service cuts or loss of their home.
 - e. The debtor can try to make new payment arrangements for all types of debts except mortgages, although even these may sometimes be eligible depending on the financial institution and on the debtor's financial situation. Under certain circumstances (a job loss, for example), some financial institutions may offer a mortgage payment relief period of up to six months (deferred payment of principal).
 - f. A debtor may also choose to focus first on paying the highest-interest debts, since they will increase faster than others.
- 2) When contacting creditors by telephone, remind clients to write down the name and contact information of anyone they speak with, as well as any details about the debt that the creditor provides (interest rate, balance, status). The debtor may also wish to use registered mail for anything sent via Canada Post, and/or keep receipts or photocopies of anything mailed.
 - 3) The debtor can offer a proposal based on his/her budget and how much he/she is actually able to repay. Clearly explaining one's financial situation may help the creditor understand the person's difficulties. If a client can demonstrate that his/her only source of income is social assistance, for example, the creditor may be more able to accept a lower repayment amount.
 - a. The budget can be used to show the creditors how much the debtor is able to pay until his/her situation improves. It is important to be realistic and propose a payment plan that is feasible. The creditor is unlikely to be understanding if the debtor defaults on his/her new payment plan.
 - b. It is in the creditors' interest to negotiate with the debtor since they really want to recover the money owed to them. However, the creditors are not legally obliged to make any special arrangements with the debtor, nor are they required to abide by them. Their ongoing cooperation is completely voluntary⁶.
 - c. The debtor should be polite but persistent. Creditors will probably be less inclined to help if the individual is aggressive.
 - 4) It is advisable to get a written confirmation of the agreement.
 - a. The debtor can prepare a brief summary of his/her telephone conversation with the creditors and send it to them (by fax or

⁶ Industry Canada, Office of Consumer Affairs, online: <<http://www.ic.gc.ca/eic/site/oca-bc.nsf/eng/cao2155.html>>.

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Collectors have a great deal of flexibility in what settlement they accept. Less than 50% of the amount owed is not common, although certainly possible. Because the collectors have such leeway in determining what the settlement amount will be, debtors would be wise to consider their own negotiation skills in this process. Some debtors, for example those with limited English-speaking skills, may wish to enlist the assistance of a trusted ally to help negotiate a fair and manageable settlement amount.

by registered mail). If the creditors do not honour the commitments they made, having a copy of the letter of agreement may facilitate their rectifying the situation.

- b. The creditor may offer, or the debtor may ask for, a settlement of a debt: the creditor would reduce the total debt (for example, from \$5000 to \$4000) on the condition that it's paid with a lump-sum amount within a short time frame. If such a proposal is agreed upon, the debtor should get the agreement in writing, stating the terms (that there is no outstanding debt due and that the debt is now cleared with this creditor).
 - c. After a settlement payment has been sent, a debtor may wish to check that the information has been accurately updated on his/her credit report.
- 5) If, after making the arrangements, the debtor cannot honour his/her part of the agreement, he should contact the creditor as soon as possible and explain the new situation.

3. Selling Assets/Possessions

While not always easy to do, selling an asset is one way to alleviate a difficult financial situation. The debtor can sell something of value that he/she owns (but does not owe money on).

There are usually no costs involved in selling most assets. However, the debtor may incur costs if he/she has to hire a professional or has certain obligations to fulfill (for example, when selling a car, he/she may have to make repairs or to have it certified as roadworthy before selling it).

4. Dealing with Collection Agencies

A collection agency is a person or company hired to obtain or arrange for payment of money owed to a third party (creditor). If a collection agency contacts the debtor regarding an outstanding debt, the following steps may be taken:

- 1) If possible, the payment of the debt should be made immediately to avoid further interest charges. The agency will stop contacting the individual once the account has been cleared.
- 2) If it is impossible to pay the full amount at once, the debtor should contact the agency to explain why and to offer some alternative method of

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repayment, either in a lump-sum or a series of monthly payments. As always, it's wise to document this in writing and, if possible, enclose a good faith payment.

- 3) The payments should be made in a manner that provides proof of payment (and never in cash).
- 4) Once the account has been officially turned over to a collection agency, the debtor will be dealing only with that agency when making arrangements for payment. There is no need to contact the original creditor as this may create confusion, unless there's an error in the account in which case the debtor should advise both, the creditor and the collection agency.

Limitations on the Actions of Creditors and Collection Agencies

The debtor will be notified, by telephone or in writing (email does not qualify), that his /her file has been turned over to a collection agency. This notice must include the name of the creditor; the amount the creditor claims the debtor owes; and the name of the collection agency and its authority to demand payment on behalf of the creditor. After sending the notice, the agency must wait 6 days before it can contact the debtor in person or by phone.

The agency cannot continue to contact the individual if:

- The individual sends a registered letter to the agency saying that he/she disputes the debt and suggests the matter be taken to court;
- The individual (or his/her lawyer) sends a registered letter to the agency providing the lawyer's contact information and notifying the agency to communicate only with the lawyer;
- The individual has told the collection agency's representatives that he/she is not the person they are looking for, unless they take reasonable precautions to ensure the individual is that person.

Other Restrictions on the Collection Agencies

- 1) After the initial contact between the agency's representative and the debtor, the agency cannot contact the debtor more than 3 times in a 7 day period unless it is by regular mail, or they obtain consent of the debtor. "Contact" means the agents must actually speak with the debtor, email him/her, or leave a voice mail. If the debtor doesn't answer the phone and the agents don't leave a message, it doesn't count as a contact.
- 2) **The agency CANNOT:**
 - a. contact the debtor on Sunday, except between the hours of 1 pm and 5 pm;

If an individual feels that he/she was not notified, try to determine whether there's been a recent change of address, or whether mail was received but not



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- b. contact the debtor on any other day of the week between the hours of 9 pm and 7 am;
 - c. contact the debtor on a statutory holiday;
 - d. use threatening, profane, intimidating or coercive language;
 - e. use undue, excessive or unreasonable pressure;
 - f. give false or misleading information to any person regarding the debtor;
 - g. recommend to a creditor that a legal action be commenced against the debtor without first sending the debtor notice;
 - h. charge extra fees above the outstanding debt which the debtor owes to the creditor and the collection agency is attempting to recover.
- 3) In general, a collection agency can contact the debtor's employer once to obtain debtor's employment information. Otherwise, they cannot contact the employer unless:
- a. employer has guaranteed the debt;
 - b. the call is in respect of a court order or wage assignment given to a credit union;
 - c. the debtor provided written authorization to contact his/her employer.
- 4) A collection agency cannot contact the debtor's spouse, a member of the debtor's family or household, or a relative, neighbour or acquaintance except to obtain the debtor's address and telephone number, unless:
- a. the person contacted has guaranteed the debt;
 - b. the debtor gave permission for the person to be contacted.

If the collection agency has breached any of the above, the debtor can:

- send the agency a letter outlining why the debtor believes they have acted inappropriately and notifying them that he/she expects them to comply with the law;
- if their behaviour persists, the debtor can file a complaint with the ministry

Professional Assistance In Reducing Debt

- 1. Credit Counselling 14
(professional education and advice on dealing with debt)
- 2. Debt Management Programs 14
(when a credit counsellor makes special debt repayment arrangements with creditors on behalf of the debtor)

ADVANTAGES

- Counsellor may achieve better results than the debtor when contacting creditors
- Saves the debtor a lot of time (and possibly stress) as the counsellor makes all the phone calls and does all the negotiating
- Only have to make a single monthly payment

DISADVANTAGES

- Not everyone qualifies (need to have a sufficient source of income to cover regular expenses plus the arranged payment on debt)
- Credit counsellors may not have the necessary qualifications to provide credit counselling as the field is highly unregulated
- High cost (fees, interest charges)
- Strict monthly repayment schedules
- Debtor cannot incur other debt

MOST SUITABLE FOR

- Individuals that can demonstrate an ability to make the monthly payments on the plan, in addition to paying for their regular monthly bills and expenses
- People who feel that the stress of debt is a primary or major issue

- 3. Debt Consolidation Loans 15
(loans from financial institutions used to pay off other debt)

ADVANTAGES

- Lower interest rate than credit card debt
- All creditors will promptly be paid in full
- A chance to maintain a good credit rating
- Only have to make a single monthly payment
- Interest on loan may be lower than interest otherwise accruing on the debts

DISADVANTAGES

- No reduction in overall debt (still have to pay the entire amount back over time)
- Financial institution may not be as flexible as creditors about late payments (default on payments may result in financial institution calling the loan)
- Debtor may be required to give some form of security on the loan
- Financial institution may cancel the debtor's credit cards and other sources of credit to ensure the debtor does not accumulate any further debt

MOST SUITABLE FOR

- Individuals that have an acceptable credit rating and sufficient income to demonstrate that they will be able to manage the loan



1. Credit Counselling

Some agencies offer assistance by providing the debtor with credit counselling services. These agencies may be community based and may not charge for their services, or they may have fees for helping the debtor make a budget and helping him/her get out of debt.

Some of these agencies actually do relatively little counselling, and instead engage in administering debt management or debt consolidation plans (described below). Since the agencies often get monetary incentives from the creditors for administering these plans, they have a vested interest in servicing only debtors that qualify for such plans. This means that in a majority of cases those debtors that do not have a sufficient income to qualify for such a plan will not receive any credit counselling. Furthermore, because the agencies have a financial incentive to push these plans onto their clients, they may not provide the debtors with other viable or even better options, such as bankruptcy or no action at all.

2. Debt Management Programs

The debtor can register for a debt management plan through a not-for-profit organization or a private company. By using this service, the debtor authorizes a counsellor to speak to creditors on his/her behalf in order to make special arrangements regarding his/her outstanding debt. The counsellor may be able to negotiate a better payment schedule and lower interest rates in order to get a monthly payment plan that fits the debtor's budget.

Essentially, the counsellor sets up and administers a debt management plan for the debtor. In most cases, the plan involves the debtor making one regular payment to the agency, and the counsellor then divides the agreed upon amounts among the creditors. The debtor decides, with the help of the counsellor, which creditors the agency contacts on his/her behalf in order to accomplish debt settlement. Once again, the budget is helpful in making this determination.

Even non-profit credit counselling is rarely free. Before agreeing to work with a credit counselling agency on debt repayment, it is wise to get a clear and firm understanding of the fees and costs

Professional Assistance In Reducing Debt

Cost of Debt Management Plans

Depending on the organization, this service may be free, but in most cases it involves a fee. The fees vary based on the services offered. It may be a fixed fee, an hourly rate, a percentage of the payments made, or a combination of all three.

It is best to contact the organization offering these services directly and ask for their fee schedule. Before signing any contracts the debtor should make sure it includes all the services discussed and the exact costs he/she will have to pay. It may be a good idea to shop around for an agency before committing to anything.

Main Credit Counselling Agencies Servicing Ontario

1. Credit Counselling Canada (CCC)

- a. CCC is a national association of not-for-profit credit counselling agencies. It provides contact information for agencies throughout Canada.
- b. Phone: 1-866-398-5999
- c. Website: <http://www.creditcounsellingcanada.ca/>

2. Ontario Association of Credit Counselling Services (OACCS)

- a. OACCS is a provincial association of not-for-profit credit counselling agencies. It provides contact information for agencies in Ontario.
- b. Phone: 1-888-7-IN DEBT
- c. Website: <http://www.oaccs.com/agencies.html#Toronto>

3. Consolidated Credit Counselling Services of Canada, Inc.

- a. Toll Free: 1-800-656-3920
- b. Website: www.consolidatedcredit.ca

4. Credit Canada

- a. Toll Free: 1-800-267-2272
- b. Website: www.creditcanada.com

5. InCharge Canada

- a. Phone: 416-637-6820
- b. Website: <http://www.inchargecanada.ca/>



3. Debt Consolidation Loans

A bank or a financial institution can consolidate the person's debt: the bank or financial institution pays off all of the debtor's outstanding debt by issuing one new loan (not all debts can be combined into a consolidation loan, for example a mortgage or a car loan cannot be included). The debtor must then pay off this loan over a specified period of time at a set interest rate. Usually the debtor ends up saving money because the interest rate on the loan tends to be lower than other types of debt such as credit cards. The debtor is therefore able to pay off the debt faster, as well.

The debtor should contact several financial institutions before choosing a consolidation loan since the interest rates offered by competing financial institutions may vary. These include banks, credit unions and other financial institutions.

In order to qualify for a consolidation loan, a consumer usually needs to have an acceptable credit rating and sufficient income to demonstrate that they will be able to manage repaying the loan on top of paying for their regular monthly bills and expenses. A debtor may also be more likely to be approved for a consolidation loan from the institution with whom they do most of their banking. A solid banking relationship can be very helpful for a consumer in this situation.

Once someone has debts that have gone unpaid for a long period of time or been sold onto collections agencies, they may find it difficult to qualify for any new loans at reasonable interest rates.

Cost of Debt Consolidation Loans

It does not cost anything to apply for a loan in order to consolidate all the debts. However, there may be some administrative fees. Arranging a consolidation loan does not cause any additional damage to debtor's credit rating so long as he/she continues to make the monthly payment.

Steps to Follow:

- 1) Before meeting with a financial institution's loan officer, the debtor should draw up a complete list of his/her current debts to determine the total amount of the outstanding debt. Though the debtor doesn't have to include all debts, he/she should tell the loan officer about them (they will have access to this information anyways when they check the debtor's credit history).
- 2) The debtor can try to negotiate a better interest rate on the loan by shopping around the various financial institutions. It is important to keep in mind that the mainstream financial institutions (for example, the main banks in Canada) will usually offer a better rate than other financial companies. Note that if a debtor's credit is already somewhat damaged, mainstream banks may not approve the request but other lenders may, at higher rates of interest.

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- 3) The debtor should carefully review the terms and conditions of the loan (loan term, interest rate, special conditions, application or service fees, etc.) so that he/she knows exactly how much the loan will end up costing altogether.
- 4) In most cases, once the loan has been granted, the financial institution will pay off the outstanding debts to the creditors.
- 5) It is possible that the financial institution that extended the loan will close all other accounts that the debtor has (e.g.: with stores, businesses or credit card issuers), to make sure that the debtor doesn't increase the debts while paying off the consolidation loan.

4. Dealing with Mortgage Payment Difficulties

The Canada Mortgage and Housing Corporation (CMHC) suggests that in cases of unforeseen financial circumstances that impact the mortgagee's ability to make regular mortgage payments (for example job loss or family income reduction), the mortgagee should contact his/her mortgage lender right away so that they can help with finding a solution.

Steps to Follow:

- 1) **Talk to the mortgage professional:**
 - a. To increase the chance of successfully managing a financial situation through early intervention, the borrower should call his/her mortgage professional at the first sign of financial difficulty;
 - b. The borrower should ask the mortgage professional about information on the options available for managing his/her financial situation; and
 - c. Keep the mortgage professional informed as circumstances evolve.
- 2) **Clarify the financial picture:**
 - a. Before meeting with the mortgage professional, the borrower should prepare a detailed list of financial obligations including any credit cards, loans, and household bills with the amounts owing and their due dates, plus information about current income, savings accounts, investments, and any other assets.



Professional Assistance In Reducing Debt

3) Stay informed:

- a. The more information the borrower has at his/her disposal on managing his/her finances, the easier it will be to make the right decisions.

For mortgages insured by Canada Mortgage and Housing Corporation (CMHC), CMHC provides mortgage professionals with tools and the flexibility to make timely decisions when working with the borrower to find a solution to his/her unique financial situation. These tools include:

- Converting a variable interest rate mortgage to a fixed interest rate mortgage in order to protect the borrower from a sudden interest rate increase, should one occur.
- Offering a temporary short-term payment deferral. The mortgage professional may be prepared to offer greater payment flexibility, particularly if previous lump sum prepayments have been made, or if the borrower has previously chosen an accelerated payment schedule.
- Extending the original repayment period (amortization) in order to lower the monthly mortgage payments. Making a loan last longer means less is owed at each payment.
- Adding any missed payments (arrear) to the mortgage balance and spreading them over the remaining mortgage repayment period.
- Offering a special payment arrangement unique to the individual's financial situation.

CMHC is also willing to consider other alternatives proposed by the mortgage professional to resolve or avoid mortgage payment default. In every case, the options available will depend upon the individual financial circumstances.

A homeowner having trouble making mortgage payments will generally find the mortgage holder much more co-operative if they ask for help early, rather than after several payments have been missed.

Legal Assistance To Reduce Debt

1. Consumer Proposal 22 (negotiated agreement with creditors to pay off only a portion of the unsecured debt and to be released from the remainder of the debt)

ADVANTAGES

- Interest on debt stops accumulating and only part of debt to creditors needs to be paid
- Debtor retains all of his/her assets
- Actions against the debtor by unsecured creditors, such as wage garnishments, will be stopped
- Debtor can solve his/her money problems without having to declare bankruptcy
- Credit rating reduced to an R7 (compared to R9 for a bankrupt)

DISADVANTAGES

- Debtor cannot choose which debts to be included in the proposal
- Debtor cannot eliminate support and alimony obligations, student loan obligations, and secured debts such as a house mortgage and a car loan
- Debtor must still pay a portion of his/her outstanding debt
- All credit accounts must be cancelled
- Credit rating reduced to an R7 (as opposed to no effect on credit rating)

MOST SUITABLE FOR

- Individual's total debt does not exceed \$250,000, not including debts secured by their principal residence
- Individual is insolvent (unable to make payments and selling the net assets would not cover the debts)
- Individual has income to make some payment to the creditors
- Bankruptcy for this individual would require significant surplus income payments, and/or the individual has assets that would be lost in a bankruptcy (such as equity in a house or a car)

2. Bankruptcy 25 (a formal legal process in which the debtor declares bankruptcy and surrenders his/her assets to the trustee in bankruptcy, who then sells them and distributes the money among the creditors)

ADVANTAGES

- The debtor is released from the legal obligation to repay the debts he/she had at the date of bankruptcy, except for certain types of debts that are excluded
- Once the debtor is bankrupt, actions against him/her by unsecured creditors, such as wage garnishments, will be stopped

DISADVANTAGES

- Expensive
- Bankruptcies generally do not affect the rights of secured creditors (for example car loans, mortgages, etc)
- Bankruptcy does not absolve the debtor of alimony payments and spousal or child support payments, student loans, fines and penalties imposed by the Court, and debt arising from fraud or misleading representation
- Credit rating reduced to R9 (the worst possible) and remains on the credit report for at least 6 years from the date of discharge, which will occur at least 9 months from filing for bankruptcy

MOST SUITABLE FOR

- Individual has attempted other debt management options and has not been able to fix his/her debt problems
- Individual has a large amount of debt
- Majority of the debt is unsecured
- Individual has a small amount of assets that would be seized during bankruptcy
- Individual's credit rating is already poor
- The potential adverse effects of bankruptcy on the individual's spouse and/or family members must be considered



1. Consumer Proposals

A consumer proposal is a formal procedure governed by the *Bankruptcy and Insolvency Act* where the debtor works with a trustee in bankruptcy⁸ to put together an offer to pay his/her creditors a percentage of what is owed to them over a specific period of time, or to extend the time the debtor has to pay off the debt, or a combination of both. Payments are made through the trustee, and the trustee uses that money to pay each of the creditors. The debt must be paid off within 5 years.

This option is available to individuals⁹ whose total unsecured debts do not exceed \$250,000, not including debts secured by their principal residence. A consumer proposal will not allow the debtor to:

- pick and choose the debts to be included
- eliminate support and alimony obligations
- eliminate student loan obligations
- deal with secured debts, such as a house mortgage and a car loan

The unsecured creditors will not be able to take legal steps to recover their debt (such as seizing assets or garnishing wages) unless the proposal is withdrawn, rejected or annulled, or if the administrator is discharged before the proposal was fully performed. Creditors will accept a consumer proposal if they see that they will lose more if the debtor declares bankruptcy.

Steps to Follow:

- 1) Debtor should contact a person who is either a trustee in bankruptcy or a person appointed by the Superintendent of Bankruptcy to administer proposals. This administrator will assess the debtor's financial situation and provide advice on what kind of proposal may be best under the specific circumstances.
- 2) The debtor signs all the required forms and the administrator files the proposal with the Office of the Official Receiver¹⁰. At that time:
 - a. Debtor stops making payments to his/her unsecured creditors (will still need to make payments on the mortgage, car, and other property that can be repossessed),
 - b. Wage garnishments will stop,
 - c. Lawsuits against the debtor by his/her creditors will be put on hold.

⁸ The trustee can be found in the Trustee Directory of the Office of the Superintendent of Bankruptcy (OSB), online: http://www.ic.gc.ca/eic/site/bsf-osb.nsf/eng/h_bro1993.html, or by searching trustee bankruptcy" in the Yellow Pages.

⁹ Not available to businesses. Division I Proposals are available for both individuals and businesses.

¹⁰ Official Receiver is a federal government employee in the Office of the Superintendent of Bankruptcy and an officer of the court with specific duties under the Bankruptcy and Insolvency Act. The Official Receiver, among other things, accepts the documents that are filed in proposals and bankruptcies, examines bankrupt people under oath, and chairs meetings of creditors.

Legal Assistance To Reduce Debt

- 3) Within 10 days of filing the proposal, the administrator sends the Official Receiver a report with the administrator's opinion on whether the proposal is fair and reasonable, and whether the debtor will be able to perform it.
- 4) At the same time the administrator submits the proposal to the creditors. The administrator will also give them:
 - a. A statement of the debtor's affairs (including a list of assets and liabilities, a list of creditors, information about debtor's personal affairs, and debtor's budget),
 - b. Administrator's report on debtor's personal situation.
- 5) The creditors have 45 days to accept or reject the proposal, during this time:
 - a. One or more creditors with 25% or more of the outstanding debt can call for a creditor's meeting:
 - i. Each creditor is given votes equal to the dollar value of the debt owed to them.
 - ii. If 50% plus one vote in favour of the proposal, the proposal is accepted and applies to all creditors.
 - b. Any creditors that do not respond will be considered to have accepted the proposal.
 - c. The OSB can also direct the trustee to call a meeting of creditors at any time within this 45-day period. A meeting of creditors will be held within 21 days after being called.
 - d. If no meeting of creditors is requested within 45 days of filing the proposal, the proposal will be deemed to have been accepted by the creditors, regardless of any objections received.
- 6) After another 15 days, if none of the creditors try to block the proposal in the courts, then the proposal is considered to have been approved by the court.
 - a. Debtor is now required to attend 2 financial counselling sessions (which are arranged by the trustee).
 - b. Debtor is now responsible for paying either a lump sum or periodic payments to the trustee and adhering to any other conditions in the proposal.

Legal Assistance To Reduce Debt

- 7) Note, if the proposal is rejected, the debtor will no longer be protected by the Bankruptcy and Insolvency Act. The administrator will notify all of the creditors and the Official Receiver of this rejection within 5 days. The creditors will now be able to take legal steps to recover their debts.
 - a. Debtor may choose to make changes to the proposal and resubmit it for consideration, find other ways to manage his/her debt, or declare bankruptcy.
- 8) Once the debtor satisfies the conditions in the proposal in full, he/she will be legally released from the debts included in the proposal.
 - a. However, if the debtor misses three payments, or if the last payment is more than three months past due, the proposal will be deemed annulled. This means the creditors will be able to take action to collect the money owed to them, unless the court has ordered otherwise, or an amendment to the consumer proposal has been filed.
 - b. If the proposal is annulled and full debt load is restored, interest will have accumulated at the original rate of interest that applied to each debt.
 - c. An administrator can revive the proposal by providing notice to creditors about a temporary inability to make payment (for example due to an illness or temporary unemployment).

Cost of Consumer Proposals

The total cost of a consumer proposal is the sum of the payments agreed to in the proposal. The higher the payment and the longer the payment schedule, the more the overall cost. The amount can be paid as a lump sum or in regular instalments over a number of years as set out in the proposal.

The payment plan for a consumer proposal cannot exceed 5 years; however, 5 year proposals often end up failing and wind up in bankruptcy. Generally, a manageable consumer proposal with a good chance of success has a term of 3 years or less.

Unlike in bankruptcy, a debtor can keep his/her assets so long as the payments are being made to both:

- a) the trustee as set out in the proposal, and
- b) other creditors with the right to repossess debtor's property (secured creditors).

Legal Assistance To Reduce Debt

There are no additional payments to be paid to the trustee for fees and disbursements as they are included in the debtor's payments. The debtor pays the amounts set out in the consumer proposal to the trustee and the trustee deducts his fees prior to distributing the remainder to the creditors.

Note on Credit Rating

Filing a consumer proposal will result in a very low credit score. Consumer proposals create an R7 rating and, in Ontario, this will stay on the credit report for 3 years after the debtor makes the last payment. Some debtors will pay off the amount faster than scheduled or even in a single payment, in order to start the countdown on removing the R7 rating and begin restoring their credit rating.

As part of the proposal process the debtor will be required to cancel his/her credit accounts, and will likely not be able to get access to any credit until after the consumer proposal is removed from the debtor's credit report.

2. Bankruptcy

If the debtor has attempted to resolve his/her financial troubles through any combination of formal and informal steps (some of which are listed above) and nothing has worked, bankruptcy becomes a viable option.

Bankruptcy is a formal legal process governed by the *Bankruptcy and Insolvency Act*. When a debtor declares bankruptcy, his/her assets (except those exempt by law) are given to a trustee in bankruptcy who then sells them and distributes the money among the creditors. It's important to understand that bankruptcy usually doesn't mean that the person must give up all their belongings; there are clear rules about what an individual can "carry through" a bankruptcy, and these limits are explained in the Execution Act.

Note that only assets owned by the bankrupt are included in the bankruptcy. If assets are jointly owned with a spouse, then the bankrupt's portion may have to be sold and distributed to the creditors. A debtor's bankruptcy also does not affect the liability of anyone who guaranteed or co-signed a loan on his/her behalf (for example, a spouse may still be accountable for liabilities incurred jointly with the debtor). It is important to make the trustee aware of joint assets so that each case can be reviewed individually.

Once the debtor is bankrupt, actions against him/her by unsecured creditors, such as wage garnishments, will be stopped. However, bankruptcies generally do not affect the rights of **secured** creditors (for

All or part of the value of certain items, such as a principle residence, some furnishings, and tools needed for work, may be exempted under the Execution Act. These amounts differ by province. Each debtor's situation may vary, and a trustee will be best able to advise.

Legal Assistance To Reduce Debt

example creditors who have a valid security against the debtor's property, such as a car or a house).

Steps to Follow:

- 1) Debtor should contact a trustee in bankruptcy and attend a meeting with him/her to discuss the debtor's personal situation and available options. Once decided on bankruptcy, the trustee will help debtor complete the required forms, and will then file the bankruptcy with the Official Receiver from OSB¹¹.
- 2) Once the forms are filed, the debtor becomes officially "bankrupt". This means that:
 - a. Debtor stops making payments directly to the unsecured creditors,
 - b. Wage garnishments will stop,
 - c. Lawsuits against the debtor by his/her creditors will be stopped.
- 3) The trustee sells the debtor's assets, except those exempted by provincial and federal laws¹², and holds the proceeds in trust for distribution to the creditors. This includes all existing assets as well as those acquired prior to the discharge of the bankruptcy¹³.
 - a. Once the bankruptcy is filed, the debtor cannot dispose of any assets assigned to the trustee.
 - b. During the bankruptcy, the debtor is also required to make payments to the trustee for distribution to the creditors. The fee is determined by the trustee taking into account the debtor's total income, income standards issued by OSB, and debtor's personal and family situation¹⁴.
- 4) The trustee notifies the creditors of the bankruptcy, and there may be a meeting of creditors which the debtor is required to attend. Creditors' meetings are not common for low or no income bankruptcies, but they remain a possibility. The purpose of the meeting is to:
 - a. Allow creditors to obtain information about the bankruptcy,
 - b. Confirm the appointment of the trustee,
 - c. Appoint up to five inspectors to supervise the administration of your estate,
 - d. Allow creditors to give directions to the trustee.
- 5) After filing for bankruptcy the debtor may be examined under oath by a representative of OSB. The purpose of the examination is to question the bankrupt about his/her conduct, the causes of the bankruptcy and the disposition of debtor's property.

¹¹ See note 8

It's important to understand that it isn't free to declare bankruptcy. Even though they're already in debt, the individual will be required to make monthly payments to help cover some of the debt costs as well as the fees for the trustee's work. Any one considering bankruptcy should get a clear understanding of what fees will be charged and what monthly payment will be required.

¹² Each debtor's situation may vary, a trustee will be best able to advise.

¹³ s. 158 of the Bankruptcy and Insolvency Act states that the debtor has a duty to disclose to the trustee all property disposed of within a period starting 12 months prior to the date of the initial bankruptcy event and ending with the filing of bankruptcy. Furthermore, the debtor must disclose all property disposed of by gift or settlement without adequate valuable consideration within the period beginning 5 years before the date of the initial bankruptcy event and ending on the date of bankruptcy.

¹⁴ The costs of bankruptcy are discussed in the next section.

Legal Assistance To Reduce Debt

- 6) The debtor then attends 2 counselling sessions to help him/her discover and understand the causes of his/her bankruptcy. These sessions will also provide information to assist the debtor in managing his/her financial affairs in the future. These counselling sessions are typically provided by the trustee; in reality they vary widely in quality and content.
 - a. During the first counselling session, the debtor will be provided with information concerning money management, spending and shopping habits, warning signs of financial difficulties, and obtaining and using credit.
 - b. In the second session, the counsellor will help the debtor discover and understand the causes of his/her insolvency or bankruptcy, and will assist in establishing a rehabilitation plan.
- 7) The trustee prepares a report to the OSB describing the debtor's actions during the bankruptcy. In certain circumstances, the trustee prepares a report regarding the debtor's application for discharge. This report describes the debtor's financial situation and analyzes:
 - a. Debtor's financial affairs,
 - b. The causes of the bankruptcy,
 - c. The manner in which the debtor performed his/her duties under the *Bankruptcy and Insolvency Act*,
 - d. Debtor's conduct before and after the bankruptcy,
 - e. Whether the debtor was convicted of any offence under the *Bankruptcy and Insolvency Act* (sections 198 to 208),
 - f. Any other facts that could justify the Court refusing to debtor's discharge.
- 8) Debtor is automatically discharged nine months after filing for bankruptcy if the following conditions are met:
 - a. This is debtor's first bankruptcy. For a second bankruptcy, if payments from surplus income are not required (see (d) below), automatic discharge takes place 24 months after the date of the bankruptcy.
 - b. The discharge is not opposed by the OSB, the trustee or a creditor¹⁵.
 - c. Debtor did not refuse or neglect to receive counselling.
 - d. Debtor is not required to pay a portion of his/her surplus income into the bankruptcy estate as per the standard established by the OSB. If the debtor is required to make surplus payments¹⁶, he/she will be eligible for an automatic discharge after contributing part of the surplus to the estate for 21 months. Second-time bankrupts with surplus income are required to contribute part of the surplus

¹⁵ Opposition to discharge occurs in less than 14% of cases and can occur for example where there are personal issues, a perception of fraud or dishonesty, or the trustee hasn't been paid.

¹⁶ See the section on Cost of Bankruptcy

Legal Assistance To Reduce Debt

If the debtor cannot find a trustee in bankruptcy, he/she may be eligible for the Bankruptcy Assistance Program which is designed to facilitate access to bankruptcy trustees. To be eligible the debtor must have contacted at least two trustees who participate in the Bankruptcy Assistance Program and tried to obtain their services, is not involved in commercial activities; and is not in jail. If the debtor qualifies, he/she should contact OSB at **1-877-376-9902** (toll free) and they will send the debtor information and a list of trustees who participate in the program. **Furthermore, if the debtor is having a problem with his/her trustee, he/she should contact OSB at the same toll free number and they will investigate the complaint.**

to their estate for 36 months, after which they are eligible for an automatic discharge.

- 9) For those who have been bankrupt before, or who do not qualify for an automatic discharge, the trustee will apply to the Court for an appointment to hear the application for discharge. Debtor attends the discharge hearing. At the hearing, the trustee's report is used to inform the Court of the circumstances surrounding the debtor's bankruptcy. The Court will choose one of the following **discharge alternatives**:
 - a. **Absolute discharge**: debtor will be released from the obligation to repay the debts he/she had as of the date the bankruptcy was filed, except for certain types of debts that are excluded (see Step 10).
 - b. **Conditional discharge**: requires the debtor to fulfill certain conditions prior to obtaining absolute discharge. Typically, the debtor will be required to pay a certain amount of money, possibly over time. However, the Court may impose other types of conditions as well. Once the conditions are met, an absolute discharge will be granted.
 - c. **Suspended discharge**: this is an absolute discharge that does not take effect until a future date.
 - d. **Discharge refused**: the Court has the right to refuse a discharge.
- 10) The bankruptcy is discharged. The debtor is released from the legal obligation to repay the debts he/she had at the date of bankruptcy, except for certain types of **debts that are excluded**:
 - a. Alimony payments and spousal or child support.
 - b. Student loans, if it is less than seven years since the debtor ceased to be a full- or part-time student. However, after five years of not being a full- or part-time student the debtor can make an application for release from his/her student loans on the basis of hardship¹⁷.
 - c. A fine or penalty imposed by the Court (such as an award for damages in respect of an assault).
 - d. Debt arising from fraud or misleading representation.

Cost of Bankruptcy

There are a number of costs associated with filing a bankruptcy in Ontario. They are:

- 1) Monthly contributions mentioned in step 3b. above. The debtor is required to make a minimum contribution to his/her bankruptcy for each month during the bankruptcy. This contribution covers administrative costs such as government

¹⁷ The Court will only discharge the student loan debts if it is satisfied that the debtor acted in good faith in connection with the obligation to repay the student loans, and that the debtor experienced, and will continue to experience, financial difficulty that prevents him/her from repaying these debts. The Courts also look at how debtors used student loan money, their efforts to complete their educational program, their efforts to repay the loans and their use of available interest-relief programs when considering the question of good faith.

Legal Assistance To Reduce Debt

fees, trustee's time, mailing, etc. This fee is typically up to \$190 per month, although this cost may increase if there are unusual complexities in the debtor's circumstances. The trustee determines the fee by taking into account the debtor's total income and expenses, income standards issued by OSB, and debtor's personal and family situation (such as family size and assets).

- 2) Surplus income payments mentioned in step 8)d. above. The government has set net monthly income thresholds, for a person or a family, to maintain a reasonable standard of living in Canada. Every dollar that a bankrupt makes above this income threshold is subject to a surplus income payment of 50%. Each month the debtor is required to send the trustee a copy of his/her paystubs so the trustee can calculate debtor's net income and determine if any surplus income payments are required, and if so, how much they will be¹⁸.
- 3) All assets surrendered when the debtor goes bankrupt.

Note on Credit Rating

Usually when the debt reaches the point where bankruptcy is required, the debtor's credit rating is already poor. A person who declares bankruptcy is assigned the lowest possible credit rating score (R9). In Ontario, information that affects the credit score is usually removed from a TransUnion credit report 7 years after discharge and from an Equifax credit report 6 years after discharge¹⁹.

To ensure that the credit record is updated, the debtor should send a copy of the discharge order to the major credit-reporting agencies (such as the two mentioned above). It is also important to keep all documents relating to the bankruptcy for reference by future lenders.

Here's how social service providers can help people who are considering bankruptcy:

- Remind debtors that **they can choose a trustee**. They may want to shop around or negotiate fees. As the "customer" in this process, they are not powerless.
- If the cost of bankruptcy is an obstacle, refer them to OSB to ask about the Bankruptcy Assistance Program. It is generally not advertised but can be a great help to low-income people.

¹⁸ For information on how the trustee calculates surplus income see Office of the Superintendent of Bankruptcy, online: <<http://www.ic.gc.ca/eic/site/bsf-osb.nsf/eng/bro2566.html>>.

¹⁹ For more information on credit reports and credit scores see Financial Consumer Agency of Canada, online: <<http://www.fcac-acfc.gc.ca/eng/resources/publications/budgetMoneyMgmt/CreditReportScore/PDF/CreditReportScore-eng.pdf>>.

No Action Towards Reducing Debt

1. Ignore/Disregard Collection Calls 32 (professional education and advice on dealing with debt)

ADVANTAGES

- Debtor may be freed of a lot of stress related to the idea of needing to make debt payments
- Limited income can go towards more urgent needs (food, shelter, clothing, etc.)
- Debts will “age off” credit report if collectors take no action for 6 years

DISADVANTAGES

- Interest may continue to accrue as debts are unpaid
- Collectors can begin legal proceedings, possibly resulting in a judgement for monies owed, which can lead to garnishments¹

MOST SUITABLE FOR

- Debtor doesn't currently need “good” credit
- Household is on very low income, so meeting basic needs is a priority/struggle
- Bankruptcy is too complicated/stressful, or debtor feels that the amount owed doesn't warrant bankruptcy

¹ Very low-income individuals may in fact be “judgement proof”, meaning that even if a judgement is ordered, their lack of funds makes their income exempt from garnishment. If/when the income increases, however, garnishments may begin. See note 20.

Waiting To Respond To Collection Efforts

The strategy that many debtors may already unknowingly have undertaken is the option to do nothing in response to collectors' efforts. A debtor can decide to ignore collection calls, though certainly this has some significant consequences.

Note that this is a *strategy* for debtors to employ as they try to manage their debts, but ignoring collector's calls and letters will not present a *solution* to the underlying debt problem, because the debts won't go away for several years, if at all. It may, however, help reduce unnecessary stress and anxiety on the debtor's part to truly understand what can and what cannot be done to them in response to an unpaid debt.

If a debtor ignores collectors' calls, letters, and messages:

- Creditors will continue to pursue the collection: first- and third-party collectors will not cease their efforts to collect on the debt. Debtors may continue to receive phone calls and correspondence about the debt.

However, a debtor may be willing to ignore these messages. Debtors are not required to respond to collectors' calls.

- Damage to credit history and score: while debts remain outstanding, the debtor's credit profile will continue to deteriorate. Failing to address outstanding debts will likely significantly hamper the ability to access new credit.

However, many people struggling with debt have neither the need for, nor the interest in, gaining new credit in the short term. Thus, additional damage to their credit profile may be unimportant.

- Costs may continue to accrue: collectors may continue to add interest charges on outstanding debts. The amount owed may increase, sometimes substantially, until the debt is paid.

However, for people living on very limited incomes, the amount owing may already be unmanageable. When individuals cannot meet their basic needs because they are allocating money towards debt repayment, they may choose to ignore the increasing balances in order to address their more urgent needs.

Debts will only "disappear" from a credit report after 6 to 7 years (in Ontario – timelines vary in other provinces) **of no activity**. Actions including making a partial payment of the debt or written correspondence acknowledging the debt will count as "activity" and will re-start the time until a debt is removed from the credit report. The FCAC guide called "Knowing and Understanding your Credit Score" provides good information about this.

(<http://www.fcac-acfc.gc.ca/eng/resources/publications/budgetmoneymgmt/creditreportscore/PDF/CreditReportScore-eng.pdf>)

A collector still has the right to collect even after a debt has aged off the credit report, but the debt will no longer be listed on the credit report. Thus, the information would no longer be publicly visible.

If an individual is unable to take any action on debt repayment and is waiting to respond, it may nevertheless be advisable to communicate with creditors. If creditors are aware of a financial hardship, they may delay or limit their collection efforts. Open communication can also help demonstrate a debtor's good faith intention to repay in the future.

No Action Towards Reducing Debt

An unpaid account will be reported to credit bureaus (the companies that produce credit reports) as defaulted or a “bad debt”. It will show a credit rating of 9, the worst possible. This will hurt the debtor’s **ability to access credit** (get a credit card or loan). It may also impact his **ability to rent an apartment**, since many landlords check credit and may not want to rent to someone with accounts rated “9”. Having “bad credit” may also **limit a person’s employability** in some fields or companies, because many employers check credit as part of their hiring process. Whenever a debtor is considering not responding to collection efforts, it’s important that he is aware of what the effects might be, and makes an educated choice about what to do.

If a low-income person wants to reduce the amount taken through the Right to Offset, she can contact the relevant branch manager and ask to negotiate an arrangement, but **any agreement is at the bank’s discretion**. Even very low-income people can have assets seized this way.

- Money owed to a bank from an unpaid credit card or loan can be taken from another account at that bank through the Right to Offset. Specific information about this will be on the credit card or loan agreement and can vary by account or bank.

However, many low-income people maintain little or no balance at their bank anyway, and may have no money available to be seized. Sometimes, people who know they owe money to one bank may have already chosen to hold their savings or chequing accounts at another bank.

- Debtors may be taken to court over amounts owed: creditors have the right to collect on debts, and may access the legal system to do so. A creditor can sue to collect a debt, and a judge may determine that the claim is valid, resulting in a judgement against the debtor that will be listed on the debtor’s credit report. Judgements may result in garnishments to the debtor’s income, and can mean that up to 50% of a person’s income is taken .

A very low-income debtor may still be unable to pay. An individual with very low income may be deemed “judgement proof” , essentially indicating that their income is too low for garnishment. In this case, the judgement will remain on the credit record and may become actionable when and if the debtor’s income increases.

Many debtors worry about having their income taken before they get it; this is called **garnishment**. Many debts cannot result in garnishment without a court order or judgement, including most debts owed to banks or credit card companies. The most common source of **garnishment that doesn’t require a judgement is debt to the government**, including student loans, taxes, and child support payments.

Deciding to wait to respond to collectors may be the only option for many debtors, but it does have repercussions. When working with debtors to assess their options, social services workers can inform them that it is within their rights to ignore collection efforts, but ensure that they are aware of both advantages and disadvantages of this strategy.

Conclusion

As social services workers, it's important to help our clients know the truth about what can and cannot happen to them. Many people suffer through serious anxiety and stress over their debts, when in fact there are significant limitations on what a collector can do to a debtor. Knowing the facts can empower debtors to make better choices about how to respond to their debts.

People cannot be deported on the grounds of owing money.

Children cannot be removed from their parents because of debt.

People cannot be put in jail...another crime, or did not pay when given a Court Order to do so.

Generally people cannot be fired because of debt.

In Ontario, debtors cannot be evicted simply because of unpaid debts, as long as their rent is paid.

Dealing with debt is never pleasant, but social service providers can help people navigate this process with an eye towards reducing the negative impact and improving the client's overall quality of life. Equipping ourselves with better knowledge will help us to help more people.



Opportunity made here.