

THE INCIDENCE AND CAUSES OF PERSONAL BANKRUPTCY *in Australia*

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This paper examines recent trends in Australian personal bankruptcy by analysing a large data set obtained from the regulator, the Australian Financial Security Authority. It demonstrates a marked decline in Australian bankruptcy rates, since a peak in 2009, and a consistent rise in levels of unsecured debt among bankrupts. It identifies a number of distinct cohorts within the bankrupt population, and important differences between men and women, younger and older people, and professional and blue collar workers. We find that the debts of bankrupt individuals tend to fall into two distinct categories: a combination of taxation debts and legal liabilities; or a mixture of personal loan, overdraft and credit card debts, likely to be linked to consumer spending. These findings represent a significant contribution to Australian empirical bankruptcy research. They are also timely, in light of the Commonwealth Government's recent proposals to implement significant changes to Australian bankruptcy law.¹

Bankruptcy is a legal process enabling people with unmanageable debt to obtain a release from their obligations, and start afresh after a period of three years. The earliest English bankruptcy laws were enacted in 1542 and were essentially punitive in nature. The *Act Against Such Persons As Do Make Bankrupts* roundly condemned debtors who 'consume the substance obtained by credit of other men, for their own pleasure and delicate living, against all reason, equity and good conscience.' This Act, and subsequent early modern statutes, imposed harsh penalties upon bankrupts, ranging from imprisonment to being 'set upon the pillory' and 'having on[e]... ea[r] cut off' (*Bankruptcy Act of 1623*). At the same time, these early acts sought to establish a measure of fairness and order in the debt recovery process, by ensuring that debtors' assets were distributed equally among their creditors (Levinthal 1919, p. 14). This latter goal has gradually assumed greater prominence as the law of bankruptcy has developed, while the sanctions imposed upon debtors have become considerably less severe. Current Australian bankruptcy law (*Bankruptcy Act 1966* (Cth)) now stresses the pragmatic goal of equitable asset distribution, rather than the punishment of debtors (Law Reform Commission 1988, pp. 15–17).

When debtors declare bankruptcy, their assets must be handed over to a trustee.² For a period of three years, these individuals must submit to a range of legal restrictions and make contributions towards their debts, if their incomes exceed a certain threshold. At the end of this period, bankrupts are freed from their legal restrictions and their remaining debts are discharged. In 2016, the Federal Government announced its intention to reduce the period of bankruptcy from three years to one, in order to promote entrepreneurship and reduce the stigma associated with bankruptcy (Treasury 2016). If implemented, these changes would further emphasise the pragmatic, rather than punitive, function of Australian bankruptcy law.

Although a form of bankruptcy has been part of Australian law since the early nineteenth century (Allsop and Dargan 2013), the academic study of bankruptcy is a relatively recent phenomenon in this country. Some studies have considered the policy objectives underlying Australian bankruptcy law and ways in which the law could better meet these objectives (Howell and Mason 2015). Others have addressed specific topics such as the treatment of gambling debts and the interaction between bankruptcy and family law (Duns 2007; Fehlberg et al. 2014). Yet to date, few Australian researchers have carried out empirical studies of bankruptcy (Ryan 1995; Ramsay and Sim 2009; Ramsay and Sim 2010). By contrast, the United States (US) has produced

a great deal of empirical bankruptcy research, most notably the Consumer Bankruptcy Project. This collaborative project has been underway since 1981³ and has examined a vast body of data including court records, written surveys and interviews with current and former bankrupts. The Consumer Bankruptcy Project has explored the causes of bankruptcy; the obstacles that debtors encounter when attempting to seek bankruptcy relief; the bankruptcy experiences of specific groups, such as single mothers, African Americans and retirees; and many other topics. This US literature demonstrates the enormous potential for empirical techniques to improve researchers' understanding of bankruptcy law and guide policy makers in identifying areas requiring reform.

This article seeks to contribute to the developing body of Australian empirical research, by examining a large and unique data set obtained by the authors from the regulator, the Australian Financial Security Authority (AFSA). In line with its privacy policies and its commitment to facilitating bankruptcy research, AFSA has provided a data set of nearly 29,000 de-identified records of individual bankruptcies initiated between 2007 and 2016. The authors have analysed this data to form a clearer understanding of the trends in, and salient features of, Australian personal bankruptcies over the past nine years.⁴ This is the first Australian empirical study to be based on a data set of this magnitude and comprehensiveness, and the first to employ statistical techniques to analyse such data. It demonstrates the significance of AFSA's unpublished data as a resource for researchers and policy makers.

Data

AFSA provided the authors with 28,683 records entered between 1 July 2007 and 20 June 2016. The sample represents 10 per cent of all bankruptcies filed during this period, and has been selected randomly, to make it broadly representative of the bankrupt population as a whole. Of the records provided, 79 per cent⁵ (or 22,517) relate to personal (or non-business-related) bankruptcies. The remaining 21 per cent (6,166) relate to business-related bankruptcies. The data set includes each individual's sex, age, occupation, income, source of income, family situation and, if appropriate, spouse's income. It identifies each individual's state of residence and whether or not the individual lived in a 'major city', 'inner regional', 'outer regional', 'remote' or 'very remote' area, as defined by the Australian Bureau of Statistics (ABS).⁶ The data set includes the cause of bankruptcy, as nominated by each individual when completing his or her Statement of Affairs (SOA) form at the commencement of bankruptcy; or, in the case of an involuntary bankruptcy, on the basis of information supplied by creditors. It also provides details of each individual's unsecured assets and liabilities at the time of bankruptcy. It lists the primary source from which each debtor obtained information about bankruptcy, and whether or not each debtor had ever been bankrupt before.

While this data set is extremely rich, it has a number of limitations. In the first instance, the data is provided by bankrupt debtors themselves, at the commencement of their bankruptcies. Existing empirical studies demonstrate that the period leading up to bankruptcy is frequently marked by intense stress and a sense that one's financial problems have become overwhelming and unmanageable (Sullivan et al. 1999, p. 244). For this reason, it is likely that some of the data reported by debtors at the commencement of bankruptcy is inaccurate or incomplete. The format of the data set also imposes some limitations. Key financial data – income, assets and (unsecured) liabilities – is recorded in bands, such as '\$0.01–\$4,999.99', rather than in precise figures. Banded data tends to obscure true distributions and thus to reduce the accuracy of statistical calculations such as means and medians. Moreover, the data set does not include secured assets or liabilities, such as homes and home mortgages, as AFSA is unable to guarantee the reliability of such data. Since homes are the primary source of wealth, and debt, in most Australian households, this is a significant omission. Still, even taking into account these limitations, the data set provides valuable insights into the circumstances of Australian debtors at the time of their bankruptcies.

Trends in the rate and incidence of Australian personal bankruptcies

Bankruptcy rates have been falling relatively steadily since 2009.⁷ This may reflect the growing popularity of debt agreements, or 'Part IX' agreements, among Australians in financial distress (Ramsay and Sim 2011; Wyburn 2012). Debt agreements allow individuals to enter into a legally binding repayment arrangement with their creditors and usually involve the payment of ongoing fees to a private debt administrator. They accounted for 25 per cent of all (non-business-related)

personal insolvencies in calendar year 2008. By 2015, this figure had risen to 44 per cent. Even taking account of the increasing role of debt agreements in the personal insolvency system, the decline in bankruptcy rates in recent years represents a striking contrast with the trend in the lead-up to 2009. Total bankruptcies rose dramatically from 8,552 in 1990 to 21,830 in 1997, and 27,483 in 2009 (Ramsay and Sim 2010, p. 289). By contrast, there were only 17,762⁸ bankruptcies in 2015.

During this period, both men and women have experienced steadily declining rates of bankruptcy. In 2009, 16,689 men and 12,030 women declared bankruptcy. By 2015, only 10,798 men and 6,945 women declared bankruptcy.⁹ As a proportion of the total adult population, the incidence of personal bankruptcy over the nine financial years from 2007–08 to 2015–16 is 108 per 100,000. The male incidence is 121 per 100,000 and the female rate is somewhat lower, at 95 per 100,000. Thus the probability of an adult becoming bankrupt in any given year is approximately one in 926.

Figure 1 shows the incidence of personal bankruptcy by geographic location. It indicates a downward trend in all regions except for the ‘remote’ category.¹⁰ It also shows that the decline in bankruptcy in outer regional areas has been less marked than the decline in inner regional areas and major cities. The rate of bankruptcy in remote areas has fluctuated between 2007 and 2016.

FIGURE 1: Trends in the incidence of personal bankruptcies, Australia – by region, 2007/08 to 2015/16

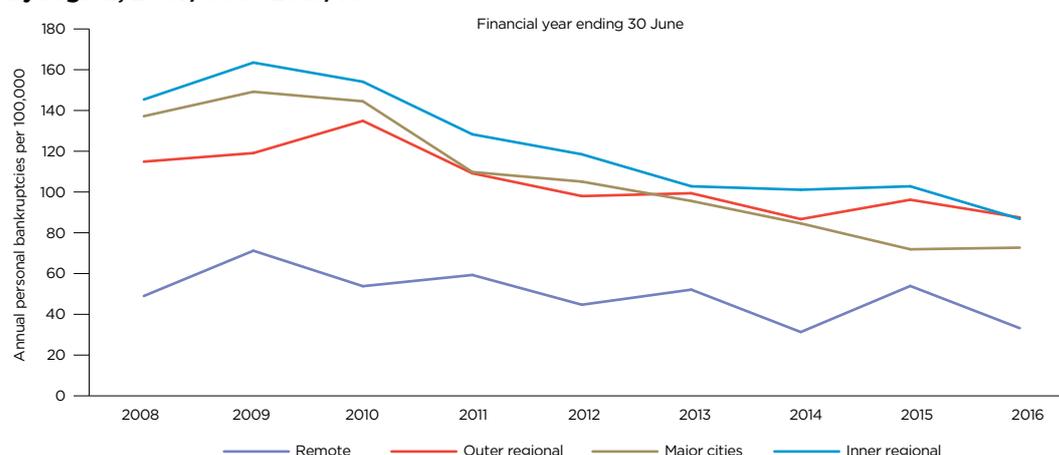
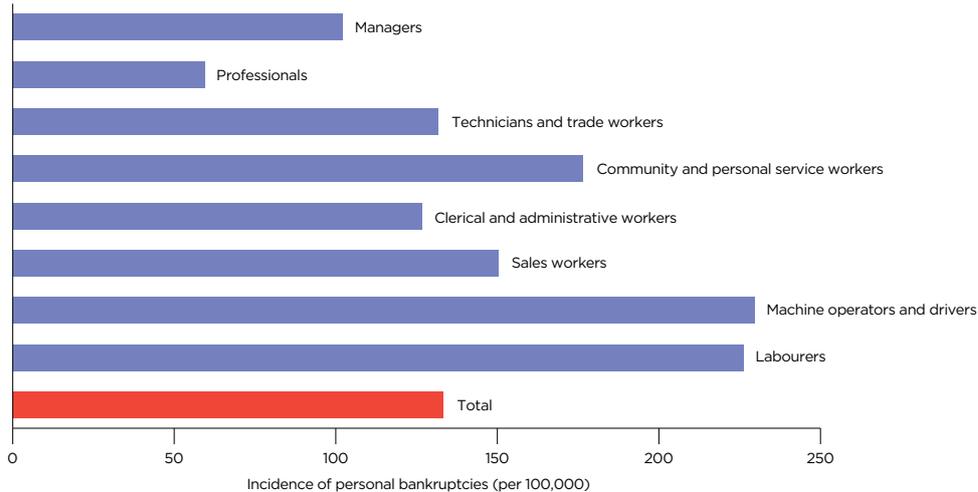


Figure 2 shows the incidence of personal bankruptcy for certain occupational categories. Here, the denominator in the incidence calculation is the adult population *in work*, rather than the Australian population generally. This figure shows significant variation between occupational categories. Professionals experienced a relatively low incidence of personal bankruptcy, averaging 60 personal bankruptcies per 100,000 over the nine-year period examined. By contrast, those in traditional blue-collar occupations, such as machine operators and drivers, and labourers, experienced much higher incidence rates: 230 per 100,000 and 226 per 100,000, respectively. Across a typical working life of 40 to 45 years, around 10 per cent of all adults in these ‘blue collar’ categories might be expected to experience personal bankruptcy.

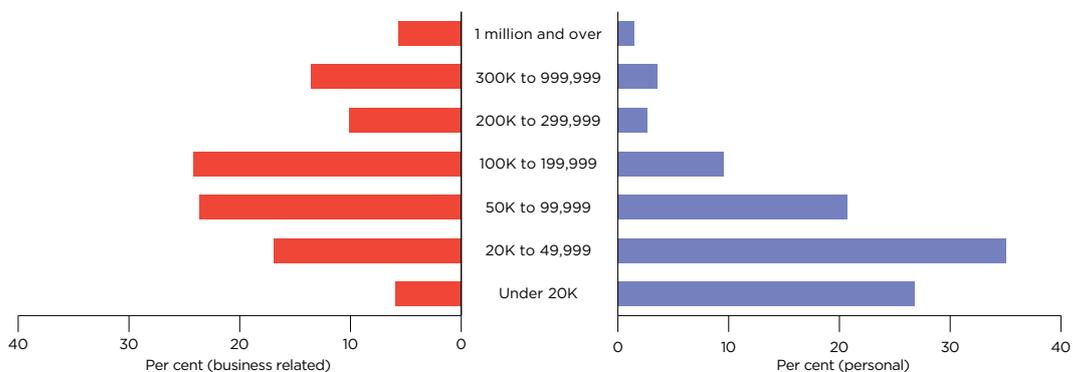
FIGURE 2: Incidence of personal bankruptcies, by occupation (average 2007/08 to 2015/16)



Unsecured debts in personal bankruptcy

Most personal bankruptcies involve relatively modest amounts of debt compared with business-related bankruptcies. Figure 3 compares the total unsecured liabilities involved in personal and business-related bankruptcies in the data set. It shows that a clear majority of personal bankruptcies – 62 per cent – reported unsecured liabilities of less than \$50,000. Some 27 per cent reported unsecured debts of less than \$20,000. The median level of unsecured debt for personal bankruptcies in the data set was \$37,500, representing roughly 25 per cent of the median level of unsecured debt for business-related bankruptcies, which is estimated at \$147,916.

FIGURE 3: Percentage breakdown of bankrupts according to total unsecured liabilities (business related v personal)



Levels of unsecured debt vary considerably according to age and gender. Among those in the personal (non-business related) bankruptcy sample, 56 per cent of males reported unsecured liabilities under \$50,000, with a median level estimated at \$42,500. By contrast, almost 70 per cent of females reported unsecured debt of less than \$50,000, with an average level of unsecured debt estimated at \$32,500. Unsecured debt levels were also much lower among younger debtors.

Across all age groups, 27 per cent of debtors reported debts of less than \$20,000, with an estimated median debt of \$37,500. However, 43 per cent of those aged under 25 reported unsecured debt of less than \$20,000, with an estimated median debt of \$22,500. The proportion of personal bankrupts with debts of \$50,000 and over rose steeply with age. While 9 per cent of those aged under 25 reported debts of this magnitude, this rose to 31 per cent for those aged 25 to 34, and 44 per cent for those aged 55 to 64. The rate declined slightly for people over 65 (32 per cent).

Overall, levels of unsecured debt have been rising over the past nine years. Figure 4 indicates the rise in the percentage of personal bankruptcies involving debts of \$50,000 and over. It also shows a concomitant fall in the overall number of personal bankruptcies involving debts of less than \$20,000. It is possible that this is partly attributable to the increasing popularity of debt agreements. Debt agreements may be attracting a greater percentage of individuals with smaller debts.

FIGURE 4: Trends in the size of unsecured liabilities of personal bankruptcies, Australia – by year, 2007/08 to 2015/16

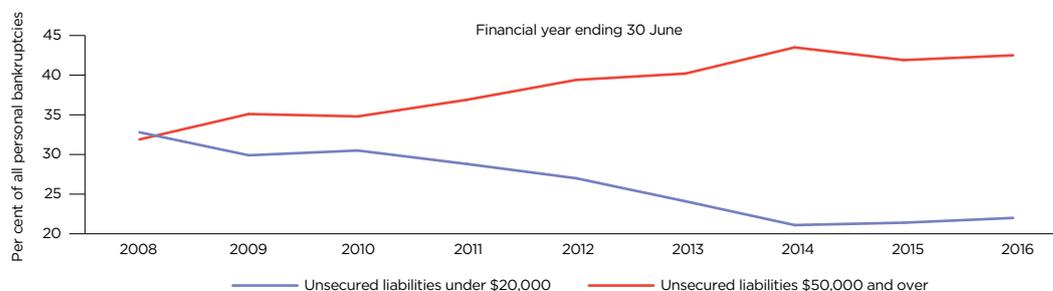


Table 1 shows the relationship between unsecured debt and multiple demographic and personal attributes occurring in combination. It reports the results of an Ordinary Least Squares (OLS) regression, which tests the effects of a number of selected demographic and personal characteristics on the dependent variable – the level of unsecured debt. The coefficient column captures estimates of unsecured debt levels, depending upon the characteristic (or combination of characteristics). The most potent indicator appears to be age: consistent with the analysis above, the results indicate that the level of unsecured debt generally rises with age. The results also suggest that debt levels rise with income: the greater an individual's earning potential, the more likely it is that they will report a high level of debt. This is consistent with the finding that those in managerial and professional roles generally report higher debt levels than those in labouring occupations.

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The results also demonstrate that those living in metropolitan areas tend to incur higher levels of debt than those in regional and remote areas. They also indicate that couples tend to incur more debt than singles; that men incur more debt than women; and that those who have never been bankrupt previously incur more debt than those who have been bankrupt at least once before. Individuals working in labouring occupations tend to experience a higher incidence of personal bankruptcy; yet when they are made bankrupt, they report much lower levels of unsecured debt. By contrast, those in higher income occupations, such as professionals and managers, report a much lower incidence of bankruptcy; however, when they do go bankrupt, they report much higher levels of debt.

TABLE 1: Relationship between unsecured debt and multiple demographic and personal attributes occurring in combination (OLS regression results)

Variable	Coefficient	St Err	Beta	t stat	p-value	Signif sign
Age	549.54	15.08	0.2368	36.4480	0.0000	+
Female	-3549.67	402.40	-0.0572	-8.8210	0.0000	-
Couple	4264.54	700.91	0.0678	6.0840	0.0000	+
Children	-489.60	449.26	-0.0077	-1.0900	0.2758	
Previously bankrupt	-7295.69	506.11	-0.0896	-14.4150	0.0000	-
Remote rural	355.84	1889.42	0.0012	0.1880	0.8506	
Metropolitan	5493.67	422.63	0.0818	12.9990	0.0000	+
Single income	226.33	708.85	0.0034	0.3190	0.7495	
Manager/Professional	11150.80	566.83	0.1329	19.6720	0.0000	+
Clerical/Machinery	2083.44	504.26	0.0274	4.1320	0.0000	+
Labourer	-3069.74	583.59	-0.0347	-5.2600	0.0000	-
Income	0.19	0.0082	0.1540	23.1450	0.0000	+
(Constant)	-15477.89	1094.11	-14.1470	0.0000		

Note: OLS regression diagnostics: Multiple R 0.3805; Adjusted R-square 0.1448; F-stat 317.55; signif p=0.0000; DF 12 (regression) and 22,504 (residual).

Factor analysis indicates that the debts of people who go bankrupt tend to be clustered into two distinct groups. The results of this analysis are reported in Table 2, in the form of a factor matrix. Generally there is a strong correlation between taxation debts and legal liabilities. Another distinct correlation emerges between personal loans, bank overdrafts and credit cards. This means that an individual who goes bankrupt is highly likely to accumulate a collection of legal and tax-related debts, or, alternatively, a mixture of personal loan, overdraft and credit card debts, more likely to be linked to consumer spending.

TABLE 2: Correlation between selected types of debts, personal bankrupts, Australia (varimax rotation)

Debt type	Factor 1	Factor 2
Other liabilities	.7354	
Taxation debt liabilities	.6301	
Legal debt liabilities	.4936	
Personal loan liabilities	-.3353	.6161
Bank overdraft liabilities		.6700
Credit card liabilities		.5427

Note: The ranges of liability amounts are grouped (since most are highly skewed toward the lower end of the range). Analysis performed on n=22,517 cases. The first factor holds together in a reliability analysis with a standardised Cronbach's alpha of 0.3186; the second factor is far less coherent (alpha of 0.1720) and supports the hypothesis that these three items are not loaded on the first factor.

Causes of personal bankruptcy

When individuals complete the SOA form at the commencement of a personal bankruptcy, they are asked to nominate the cause of the bankruptcy, choosing from the following options: 'unemployment or loss of income'; 'adverse legal action'; 'liabilities due to guarantees'; 'gambling, speculation and extravagance in living'; 'ill health or absence of health insurance'; 'domestic discord or relationship breakdowns'; and 'excessive use of credit facilities including losses on repossessions, high interest payments and pressure selling'. Individuals are also able to nominate '[an]other reason not listed'. The causes nominated by those in this sample are indicated in Figure 5, in descending order of prevalence. Figure 5 shows that 'unemployment or loss of income' is the single most common cause of personal bankruptcy.

FIGURE 5: Main causes of personal bankruptcy (reason stated by the bankrupt), Australia – average for 2007/08 to 2015/16

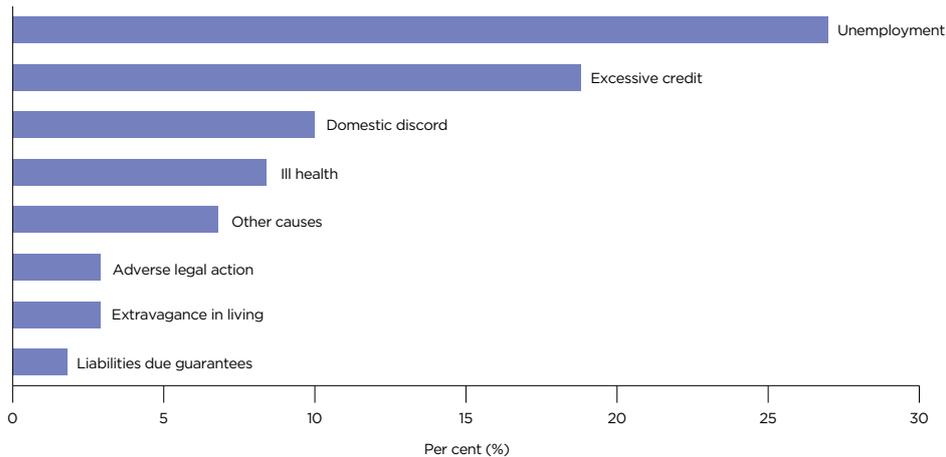
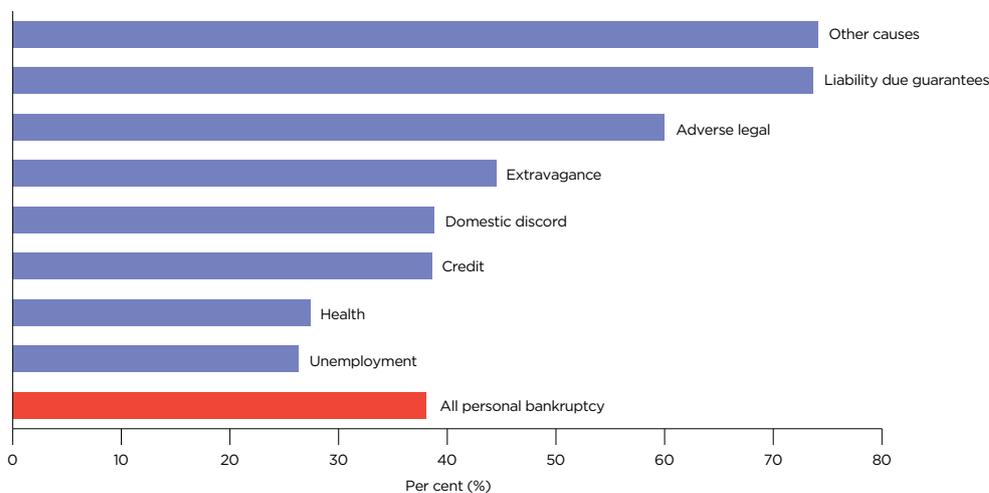


Figure 6 shows the relationship between cause of bankruptcy and the extent of unsecured liabilities. Those who went bankrupt as a result of giving personal guarantees reported very high levels of unsecured liabilities: they reported a median unsecured debt of \$162,500, compared with a median figure of \$37,500 across the data set as a whole. Some 73 per cent of bankrupts in this category reported unsecured liabilities of \$50,000 and over. By contrast, those who cited unemployment or loss of income as the cause of their bankruptcy reported only \$27,500 in median unsecured debt. Only 26 per cent reported debts of \$50,000 and over. Those who attributed their bankruptcy to domestic discord reported a slightly higher median debt of \$37,500. Some 39 per cent of these individuals reported debts of \$50,000 or more.

FIGURE 6: Percentage of personal bankruptcies involving unsecured liabilities of \$50,000 or more, by major causes of bankruptcy (average 2007/08 to 2015/16)



The data also shows that certain demographic groups are more likely than others to nominate particular causes of bankruptcy. In this sample, younger individuals were more likely to attribute their bankruptcies to unemployment or loss of income: 53 per cent of those in the under 25 age group cited this cause, compared with 34 per cent of the overall sample. Those aged 65 or older were more likely to attribute their bankruptcies to ‘excessive use of credit’: 37 per cent of those aged 65 and older selected this cause, compared with 24 per cent of the overall sample. Older individuals were also slightly more likely to cite ill health: over 16 per cent of those aged 55 and over selected this cause, compared with 11 per cent of the overall sample.

Those in managerial or professional occupations were less likely to cite unemployment: 24 and 27 per cent selected this cause, respectively, compared with 34 per cent of the sample as a whole. By contrast, unemployment or loss of income was selected as the primary cause by 43 per cent of labourers and 41 per cent of those in rural and remote locations. Domestic discord was more likely to be cited by women (16 per cent) than men (10 per cent). Of those who were single with dependants at the time of bankruptcy, almost one third cited domestic discord as the primary cause of bankruptcy. Over the nine years from 2007 to 2016, individuals generally became less likely to cite excessive use of credit as the cause of their bankruptcies. The proportion of individuals selecting this cause fell from 30 per cent in 2007–08 to 21 per cent in 2015–16.

Conclusion

This analysis demonstrates a consistent and pronounced decline in Australian bankruptcy rates, since a peak in 2009. Bankruptcy has become less prevalent among both men and women, and among people in major cities, inner and outer regional areas. At the same time, levels of unsecured debt in bankruptcy have been rising steadily. In conjunction with these broadly consistent trends, the data reveals significant variations within the bankrupt population. Statistical analysis identifies a number of distinct cohorts within the bankrupt population: debtors who are younger, older, male, female, professional or blue collar; debtors who are single with dependants; debtors with predominantly legal and tax-related debts; and those with debts more likely to relate to consumer spending. The distinct experiences of these cohorts emerge from their varying debt profiles and the factors they nominate as causing their financial problems, as well as their prevalence within the bankrupt population overall.

Drawing upon a very comprehensive data set, these findings make an important contribution to the growing field of Australian empirical bankruptcy research. They also illustrate the potential for empirical research to inform public policy, particularly the Federal Government's current proposals to reform Australian bankruptcy law.

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Notes

1. The authors wish to thank the statistics team at the Australian Financial Security Authority for their assistance in the provision of data for this project. The authors particularly wish to thank River Paul, who managed the process and was exceptionally patient with our questions and requests for additional data.
2. Debtors are entitled to retain ordinary household goods, items of sentimental value, tools of trade and other specified items (*Bankruptcy Act 1966* (Cth) s 116).
3. These studies have been undertaken in 1981 (Sullivan et al. 1999), 1991 (Sullivan et al. 2000), 2001 (Warren and Warren Tyagi 2003) and 2007 (Porter 2012).
4. The data spans the period from 1 July 2007 to 20 June 2016. 1 July 2007 was the date on which AFSA adopted its current data management and reporting system. The data file was produced on 20 June 2016 and includes all records entered up until that date.
5. All figures have been rounded to the nearest whole number.
6. Individuals in the sample were coded by AFSA as residing in a 'major city', 'inner regional', 'outer regional', 'remote' or 'very remote' area. This coding was based upon ABS classifications. See [ABS, Australian Statistical Geography Standard \(ASGS\) Remoteness Structure](#).
7. During the period under discussion, AFSA changed its reporting methods. It ceased reporting some bankruptcy statistics by calendar year and began to report them by financial year. Accordingly, this article cites some figures by calendar year and others by financial year.
8. AFSA, [Bankrupts](#) (31 January 2016).
9. In 2015, a further 19 bankrupt debtors did not state their gender: *ibid*.
10. For the purposes of statistical analysis, the 'remote' and 'very remote' categories have been combined.

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