

CONSUMERS INTERNATIONAL
Regional Office for Latin America and the Caribbean



**A MODEL LAW ON FAMILY
INSOLVENCY FOR LATIN AMERICA
AND THE CARIBBEAN**

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The need for a Model Law on Family Insolvency

This Model Law on Family Insolvency was developed with the aim of bringing fairness to a situation which is playing an increasingly large part in the lives of consumers: the problems caused by indebtedness. We say “fairness”, because this aim is consistent with the basic purpose of all consumer protection legislation, which is to provide tools that will enable the weaker party in the consumer relationship to deal with any problem that might arise with a supplier of goods and services.

Financial services form a very broad area of action in bringing these asymmetries into balance; in Latin America personal indebtedness and family insolvency are creating a problem whose consequences are being felt with ever greater force, especially among the medium and lower socio-economic groups.

Exposure to a battery of credit offerings, whether in the form of loans, cards or other types of facility, is a global phenomenon that has had consequences which can in some cases be described as seriously detrimental to the wellbeing of consumers and their families when borrowing leads to a degree of indebtedness that becomes unmanageable. It is also true that credit can help people to improve their quality of life and achieve social advancement, and it is precisely for this reason that credit should continue to be available to the greatest possible number of people. It is in the trade-off between these two variables that a balance needs to be struck: on the one hand, to protect those who for various reasons have fallen heavily into debt and to help them get out of it; and on the other, to find ways of ensuring that credit can continue to be a means for improving people’s quality of life.

For companies facing economic conditions that have caused them to suspend payments or to have difficulty in paying their debts, all countries have legislation that can help them to get out of debt, whether by means of creditors' meetings or by petitioning for bankruptcy. The main purpose of such solutions is to try to avoid consequences that could result in even worse problems. But if instead of companies we look at what happens to consumers in similar situations, the remedies are not the same and, worse still, are in most cases non-existent.

At present, a consumer who is having difficulty in honouring his debts or who is simply unable to do so has no mechanism available to him such as a creditor's meeting or a declaration of bankruptcy. It is true that some of the laws that apply in these situations do provide for meetings of creditors or bankruptcy proceedings for individuals, but the solutions offered do not have a social, but rather an economic purpose, having been designed for small business owners who get into difficulties in running their business or professional practice. And when one attempts to apply these solutions to situations such as family indebtedness, one finds that their internal logic is such that they are unable to respond to the implications that a position of severe indebtedness or inability to pay debts can have not only on people but on the wider community.

There is therefore a need for proposals to fill this legislative vacuum – which is also, to some extent, a policy vacuum. And the solution that looks most likely to succeed may be a law setting out a procedure whereby that consumer, or that family, can get out of the situation, and establishing safeguards both for the consumer or family and for their creditors.

This is the approach that has been taken with the Model Law on Family Insolvency and underlies the various solutions set out in the body of the text.

The Model Law is structured into four parts. The first explains the purpose of the Law and its scope of application, the types of person who may avail themselves of it, the definitions of the terms employed and the general principles on which it is based. The second part is concerned with the statutory body or agency that will apply the Law, and sets out its powers and responsibilities. The third part

describes the non-judicial procedure for reaching settlements with creditors, to be conducted under the authority of the statutory body; and the fourth part deals with the proceedings to be conducted in a court of law in the event that an out-of-court settlement is not achieved.

In drafting the Law care was taken at all times to ensure clarity, with priority being given to the swift processing of cases, economy in the use of resources, and fairness for both parties; given that the aim was to provide a Model Law to be used as a resource in the development of national laws, the utmost flexibility was built into the provisions dealing with powers and jurisdiction, time limits and requirements so that the Law could be adapted according to legal, social and political circumstances in different countries. Another characteristic that it was felt should be preserved was that the Law should be of a modular design, so that parts of it could be redrafted in a more concise form so as to include only some of the solutions being proposed.

The work of drawing up this Model Law benefited from contributions from the many people who gave of their time and their knowledge. We would like to thank Antonino Serra Cambaceres, who coordinated the project; Nayda Medrano, Giovanni Fletcher and Alejandro Pujá, who participated in the working group responsible for preparing the first draft of the text; and Claudia Lima Marques, Ester Reynoso, Jaime Lorenzini, Marcos Diegues, Gilles Paisant, Marcelo Sodr  and Jos  Luis Laquidara, who offered valuable comments and suggestions for improvement. We are also very grateful to the Fundaci n AVINA, which understood the need for a Model Law like the one we were proposing and provided us with human and financial support to realize this aim.

We hope that the result of these efforts will make a real contribution to making laws of this kind a reality in Latin America within the not too distant future.

Model Law on Family Insolvency

I. GENERAL PROVISIONS

Article 1 – The purpose of this Law is to establish an administrative and judicial procedure that will enable users of financial products and services who are in a position of insolvency to reach a settlement on payment with their creditors and thus discharge their outstanding financial obligations of a non-commercial nature.

It also aims to support the economic recovery of families or individuals, regularize their financial position and ensure that they are not subjected to any form of social exclusion or denied access to employment; it also seeks to foster the development of a culture of access to responsible credit through the provision of information and financial education.

Article 2 – This Law is applicable to all persons who are users of financial services and are resident in the national territory, and to all providers of the said products and services who are engaging in any commercial or financial activity within the country.

Nothing in this article shall prevent the procedure from being applicable to debts arising from the use of products or services of an international character such as credit facilities in foreign currency to be used in another country.

Article 3 – The procedure set out in this Law shall be applicable to any loans or other credit arrangements originating from a cause or title prior to the application being made.

Maintenance payments, proceedings to enforce maintenance payments and business debts shall be excluded from the scope of this Law.

Maintenance payments will, however, be taken into account in the setting of payments to be made by the debtor as part of the agreement with his creditors.

Article 4 – This Law will be based on the principles of good faith, simplicity, transparency and free access, and the conduct of proceedings will be governed by the principles of swiftness, economy, simplicity and orality.

Article 5 – For the purposes of this Law:

- a) **User of financial products and/or services** means any natural person who receives any credit, loan or other financing from a financial, banking or commercial entity supervised or controlled by a regulatory authority, and who uses the said credit, loan or financing for a non-business purpose.
- b) **Insolvency** means any situation in which a natural person or their family is placed when they have acquired debts which they cannot pay out of their income.
- c) **Passive over-indebtedness** means any position of indebtedness that results from unforeseen circumstances or circumstances which were foreseen but could not be prevented, and that restrict or impair the ability of a natural person or their family to pay their debts without risking insolvency.
- d) **Financial entity** means any legal person, whether private or public, whose normal business consists of acting as an intermediary between sellers and consumers of financial products and services.
- e) **Credit card** means a document issued by a financial or financial services institution authorized by the relevant or official agency or authority, enabling its holder or user, through a credit facility granted by the issuer, to purchase goods or services in authorized business establishments.
- f) **Commercial banks** means institutions that are operating as financial intermediaries and are able to carry out all lending, deposit-taking or service transactions that they are not prohibited from carrying out by laws regulating

the financial services market or by regulations imposed by the relevant authority in the exercise of its powers.

- g) **Commercial entity** means any natural person or corporate entity that sells goods or services and is able to grant loans, credit or financing of any other description to the public for the purchase of the said goods and services.
- h) **Precarious employment** means informal, unregistered employment in which social security contributions are not paid.

II. CAUSES OF OVER-INDEBTEDNESS

Article 6 – Any user of financial services may apply for the procedure established by this Law provided that they are financially insolvent and that their insolvency was caused by any of the following:

- a) Loss of employment as a result of direct and/or indirect dismissal;
- b) Precarious or unregistered employment;
- c) Temporary or permanent disability;
- d) Serious or chronic illness resulting in excessively high expenditure on treatment and/or medication;
- e) Separation, divorce or dissolution of a conjugal partnership;
- f) The death of a spouse or common-law spouse;
- g) The incurring of unforeseen expense due to special circumstances.

III. OBLIGATIONS OF FINANCIAL INSTITUTIONS, BANKS AND COMMERCIAL ENTITIES

Article 7 – Financial institutions offering loans shall provide to users of financial products and services, free of charge, detailed information about the product being

offered, in the manner and to the extent required by the law on consumer protection and other related or supplementary legal provisions.

Article 8 – Financial institutions shall inform users of financial services in writing, and in a clear and detailed way, of the total repayment amount of the debt at a specified date.

Article 9 – Financial institutions shall provide all users of financial services with a copy of the contract and any annexes thereto prior to the signature thereof.

IV. RELEVANT AUTHORITY

Article 10 – The authority charged with applying this Law will be the Over-indebtedness Conciliation Unit [*Unidad de Conciliaciones de Sobreendeudamiento*, “UCS”], which will be set up as a branch of the highest authority responsible for consumer protection and will be responsible for controlling, overseeing and administering the procedure in accordance with this Law and any regulatory provisions thereof.

Article 11 – The UCS will consist of a co-ordinator who will be responsible for administering the registry of conciliators, co-ordinating the team of expert case managers who will examine incoming applications, and for co-ordinating policy as appropriate.

Article 12 – Functions of the UCS:

- a) Ensuring that users of financial or credit products and services who are in a position of indebtedness have access to a procedure that is simple, short, confidential and free of charge.
- b) Drawing up plans for a return to economic health in each case.

- c) Setting up and maintaining a Register of Conciliators.
- d) Regulating, putting in place and developing the administrative procedure laid down by this Law.
- e) Setting judicial proceedings in motion by referring administrative cases where conciliation has failed.
- f) Giving permission for users of financial services making use of the procedure laid down by this Law to acquire further loans and credit, having regard to the circumstances of each case.
- g) Developing and drawing up education programmes on finance and personal financial management, including campaigns in a variety of communication media.

V. ADMINISTRATIVE PROCEDURE

Article 13 – The UCS will be responsible for ensuring that users of financial products and services have access to a procedure that is simple, short, free of charge and confidential.

Article 14 – Persons who are insolvent must present, either personally or through a consumer association, a written application for an administrative procedure to be conducted in accordance with this Law.

The application should:

- a) provide details of the applicant, the reasons for the application and an address for service of notices;
- b) provide clear and precise details of the income, assets and monthly outgoings for the applicant him/herself and for his/her family, if any;
- c) state the minimum amount needed to maintain the family group;

- d) give details of all loans or credit that have been taken out and any other necessary or relevant information that will make the applicant's financial situation clear;
- e) give details of the applicant's creditors and the amount or amounts owed to each one; and
- f) include documents to support the above information.

Once documentation has been received by the UCS it will be passed to the case management team, which will study the information and check it to make sure that sufficient information has been provided.

Article 15 - The UCS will notify the applicant's creditor or creditors that an application has been made, with a view to the creditor providing a written statement or reply within three days of the date of the notice.

Article 16 – On expiry of the period for providing the written statement or reply, the case management team will examine the case with a view to reaching a conclusion on the applicant's economic and financial position. During the evaluation period the parties may produce any evidence they consider appropriate or that is requested by the case management team.

The case management team will determine whether the application should be allowed or whether the case should be closed, and will give notice of its decision to the parties.

A decision to close the case must be accompanied by reasons.

Article 17 – An evaluation report declaring that the application should be allowed must include a plan for economic rehabilitation, to be presented to the parties at the conciliation hearing.

The economic rehabilitation plan should have the following objectives with respect to the indebted person:

- a) To enable the family economy to recover;
- b) To restore the debtor to financial health;
- c) To ensure that the debtor and any persons who are economically dependent on him/her are able to subsist, based on a minimum subsistence amount deducted from the family's income;
- d) To prevent any situation of social exclusion or psychological disturbance from arising.

Article 18 – Once the procedure has commenced, any court or out-of-court proceedings then in progress or follow-up action that could affect the assets of the debtor or any jointly liable co-debtors will be suspended.

In addition, once the procedure has started, the applicant shall not take on any further loans or accept any obligation whatsoever that could affect their financial position; failure to comply with this requirement will result in the immediate closure of the case except where the UCS has given its prior permission, which will be granted only if the applicant is able to give the UCS sound and valid reasons for taking such a step.

Credit reference agencies will be required to suspend access to, and the exchange of, all personal and credit information concerning the applicant immediately on receiving a notice from the UCS requiring them to do so.

Any credit reference agencies found to be in breach of the above requirement will be liable to a penalty.

Article 19 – The UCS co-ordinator will appoint a conciliator from the Register of Conciliators, who will preside over the hearing.

The evaluation report and any decision by the insolvency team must be supported by reasons or arguments.

Article 20 – The UCS will summon the applicant and the creditor or creditors to attend a conciliation hearing.

The hearing will take place with the parties in attendance and the evaluation report will be discussed. During the hearing the parties may provide such explanations or comments as they consider necessary and propose alternative solutions. The conciliator will try to bring about a rapprochement between the parties and to ensure at all times that the objectives of the economic rehabilitation plan can be achieved and that the minimum subsistence amount is assured.

If the hearing results in an agreement between the parties, a written record will be made, setting out the terms of the agreement that has been reached; this will then be signed by the parties attending the hearing and by the conciliator. The written agreement will subsequently be vetted and approved by the UCS co-ordinator.

A certificate of the written record, issued by the UCS and setting out the conciliation agreement, will have the effect of an out-of-court settlement and will be valid for enforcement purposes only if it is declared to be so by a judge.

Article 21 – Based on the evaluation report, the UCS will determine whether the debtor should be required to register for financial education programmes to be given by the UCS in offices provided for the purpose.

Article 22 – For the purpose of keeping documents and evidence of all actions and proceedings carried out in the course of the administrative insolvency procedure, a case file will be created and the said case file will be open to inspection by the parties and their authorized representatives.

VI. JUDICIAL PROCEEDINGS

Article 23 – If a conciliation agreement is not reached through the administrative procedure, or if conciliation has not been successful with respect to one or more creditors, the financial services user may demand that the case be tried by a judge of competent jurisdiction so that the judge can draw up a plan for the economic rehabilitation of the debtor.

Article 24 – The applicant must address his petition to the UCS, which will refer the administrative case file to the court of competent jurisdiction to which the case is assigned.

The State must guarantee to provide a system of free expert assistance to give support on accounting, legal and financial matters to debtors who require such assistance.

A court procedure under this Law is free of charge to the debtor and does not require the debtor to be represented by counsel.

Article 25 – On receiving the administrative case file, the judge with jurisdiction to try the case will summon the debtor to confirm the application. Such confirmation will have the value of a legal oath for all purposes.

Once an application to the court has been given admittance, all time periods that have commenced in any legal proceedings brought against the debtor will be suspended, as will the accrual of any statutory or default interest chargeable to the debtor; moreover, the debtor's assets will be declared to be immune from seizure.

Having given admittance to the claim, the Court will confirm the suspension of all access to, and exchange of, personal and credit information concerning the debtor by credit reference agencies.

Article 26 – The Court will order that notice of the claim be given to the creditor or creditors, who may provide statements of their case within any time period set by the Judge.

The Court will also arrange for a judicial notice or announcement, containing an extract of the order allowing the case to proceed and summoning all persons or institutions with an interest in the trial, to be displayed at the Court offices for five (5) days.

If the Court has a website it must place an announcement of the commencement of proceedings on the site, for the same purpose as the announcement to be made under the previous paragraph.

Article 27 – On expiry of the five-day period, the Judge shall set a day and time for a hearing, which the debtor and the creditor or creditors will be summoned to attend; the debtor and creditor(s) may, up to the time set for the hearing, provide to the Court any documents in their possession which they consider relevant to a ruling on the case.

Article 28 – The debtor may submit a payment proposal, which will be discussed at the hearing. At the hearing the parties may make such claims and put forward such arguments as they see fit. The Court may adjourn the hearing for periods of not more than two (2) hours to allow the creditor or creditors to make any technical verifications they consider expedient.

Article 29 – The Judge will be free to make any consultations he considers necessary for an agreement on the payment proposal to be reached between the

parties. The Judge's opinions at this stage of the proceedings shall not disqualify him from continuing to try the case.

Article 30 – If an agreement between the debtor and the creditor or creditors cannot be reached, the Court will declare the preliminary stage to be at an end and will immediately begin to hear arguments for or against a judicial restructuring of the insolvency or indebtedness.

Article 31 – The Court may obtain evidence of any description to arrive at the truth in relation to the material facts connected with the debtor's economic or financial position.

Article 32 – Having considered all aspects of the debtor's economic, legal, credit and financial position, the Court will give a judgment ordering:

- a) a debt restructuring plan to restore the debtor to financial health, allowing him/her to pay off his/her debts and simultaneously safeguarding the welfare of his/her family and the maintenance of a decent standard of living (minimum survival amount);
- b) the suspension or cessation of all legal proceedings then in progress;
- c) the suspension of any outstanding default interest;
- d) the entering of the resulting legal situation in the credit record provided or administered by credit reference agencies; and
- e) any other matter it considers relevant.

Article 33 – When giving a ruling the Judge will take account, inter alia, of the following circumstances in relation to the consumer/debtor:

- a) the commitment shown by the debtor to discharging his/her obligations;
- b) his/her credit history prior to becoming insolvent;
- c) the truth of his/her claims; and

d) clear evidence of responsible consumer behaviour.

Article 34 – The debt restructuring plan should not set any period longer than 5 (five) years for it to be carried out; the plan may include provisions for reaching an accommodation on, or a rescheduling or deferral of, debt repayments, or for the reduction or elimination of rates of interest, or for the consolidation of debt, or for the provision or replacement of guarantees and any other indispensable measures to adjust the debtor’s liability according to his/her ability to effectively discharge the debt.

The plan should take account of the minimum subsistence requirement to ensure that its implementation will not jeopardize the subsistence and basic economic survival of the consumer and his/her family or the payment of current outgoings necessary to ensure survival, including the supply of utility services to the home; no property, wage or salary income or other funds assigned to the debtor should be subject to seizure or attachment unless ordered by the Court.

The plan should make such measures conditional on the undertakings given by the debtor in such a way as to facilitate or ensure the payment of his/her debts or obligations. The Court will review all conditions, commitments, situations or other requirements imposed upon the debtor.

Article 35 – The Judge’s decision will be open to appeal.

Article 36 – The procedure shall be terminated:

- a) if the debtor fails, without good reason, to attend any hearing or stage of the trial;
- b) if the Court refuses to allow the case to proceed in accordance with this Law, on the grounds that it is out of order or lacking in substance, or that it

would not have the purpose or significance required for proceedings of this nature;

- c) where the debtor's conduct amounts to abuse of the legal process or shows a fraudulent intent that would clearly be to the detriment of one or more creditors;
- d) where conduct of the kind described above would, if confirmed, result in the imposition of fines or other penalties on the debtor.

Article 37 - A debtor will be prohibited from obtaining any of the legal benefits of a Court-sponsored debt restructuring under this Law if he/she has previously benefited from the effects of such restructuring within less than two (2) years of the conclusion of a similar procedure [sic].

The prohibition under the previous paragraph will not apply if the debtor's failure to pay or to fulfil any agreements or judgment reached in the context of this procedure is shown beyond doubt to have been due to unforeseen circumstances or *force majeure* and recognized as such by the Court.

Article 38 – Any misbehaviour by the debtor shall give rise to the acceleration of all debts covered by the agreement or by a final and binding judgment or debt restructuring plan.

Misbehaviour means any of the following:

- a) Making false statements or producing misleading documents with the intention of making use of the benefits of the procedure established by this Law;
- b) Concealing or diverting, or attempting to conceal or divert, all or any of his/her property, with a like intention;
- c) Aggravating his indebtedness by taking out additional loans or taking actions to dispose of his property which have not been judicially approved in

the course of the proceedings or as part of a plan or agreement resulting from conciliation.

Article 39 – A creditor will be deemed to have shown bad faith as a litigant if he makes false or exaggerated claims; or if he acts unreasonably by making repeated attempts to hold up the proceedings in such a way as to delay or prolong the process of reaching a final resolution in Court proceedings of this kind.

Such conduct shall, if confirmed by the Judge, result in the immediate imposition of penalties or fines on such creditor.

Article 40 - A National Insolvency Resolution Support Fund [*Fondo de Subsidio Estatal para Resolución de Insolvencias*] will be set up, and will be funded from civil and administrative fines imposed by Judges or Officials for abuses occurring in the course of the administrative or the Court proceedings.

VII. PREVENTION OF OVER-INDEBTEDNESS

Article 41 – The State shall promote the development of educational programmes to raise public awareness of aspects related to financial services. The said programmes will be implemented at the primary and secondary school levels. Financial education programmes will also be set up for consumers who voluntarily decide to improve their knowledge in this area, and such programmes will be obligatory for all persons who have applied for administrative or judicial intervention under this Law.