

BANKRUPTCY AND FAMILY LAW

1 October 2020

With COVID-19, financial pressures are increasing. When financial pressures are serious that can sometimes lead to bankruptcy. Declaring bankruptcy is a major financial step to take but what impact can it have in a divorce?

What is bankruptcy?

When a person is declared bankrupt, their assets are immediately put under the control of a Trustee. This means the bankrupt person does not have any control or possession of their assets and can no longer transfer property.

In Family Court proceedings

A person who is bankrupt, or becomes bankrupt, and is a party to Family Court proceedings must notify the court at the start of the proceedings or as soon as they become bankrupt.

A bankrupt person is not entitled to make submissions to the court in relation to property that is currently being looked after by the Trustee, but they do have a right to make submissions in relation to property owned by their non-bankrupt spouse.

Where there is one party to a property settlement who is bankrupt and the other party is not, the non-bankrupt person may make an application to the Family Court for an injunction.

The purpose of the injunction is to stop the Trustee from distributing any assets or property amongst the bankrupt party's creditors before the property settlement matter is resolved.

The court can order that property, otherwise available for distribution to creditors, be transferred to the non-bankrupt spouse.

Types of debts:

In cases of bankruptcy, it's important to note the difference between secured and unsecured liabilities.

Secured liabilities are "secured" by a tangible asset such as a house or car – the asset serves as collateral for the debt. Lenders have a right to seize the asset to cover the debt. A mortgage and car loan are the most common examples of secured debt.

With unsecured liabilities, lenders do not have the rights to any collateral for the debt. If you fall behind on your payments, they generally cannot claim your assets for the debt. Credit card debt is the most widely held unsecured liability.

What about child support?

Even when a person has been declared bankrupt, child support or spousal maintenance orders can be made against them.

A person who is bankrupt is not released from all provable debts – they're still liable, for example, for debts incurred by fraud such as Centrelink debts and debts incurred under a maintenance order or child support assessment.

In fact, when an order is made for child support or spousal or child maintenance, the payments are taken to the debts of the bankrupt party. The non-bankrupt person can then choose to enforce those debts via court proceedings. The funds can be recovered either by voluntary payments, by deductions from the bankrupt person's wages or by intercepting and applying taxation refunds.