

## Chapter 6: The consequences of bankruptcy: Part 9

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### Summary

There are many different consequences of bankruptcy. Some of the concepts are quite complicated. It is important to have a broad understanding of the principles and to be familiar with problems that might arise so that you know what questions to ask the client and when to seek more advice on their behalf.

This section is broken up into segments. Parts 1 – 5 covers:

1. What happens to debts?
2. What property is protected?
3. What property will be taken by the Trustee?
4. Whether the client has to pay income contributions and how much.
5. What other consequences there might be.

Financial counsellors should be aware of the content of all these parts at least in broad terms as they are relevant to all clients.

Parts 6 – 9 need only be referred to if they are relevant to your client's individual circumstances. They cover in order:

6. Small Business
7. Family Law
8. Gambling and hazardous speculation
9. Death

## Introduction

Your client must understand the following potential impacts of bankruptcy before making an informed decision whether to go bankrupt:

- **Debts** – will they go away?
- **Assets** (past, present and future) – will the trustee in bankruptcy ('the Trustee') take them? Can the Trustee undo past transactions and get at assets now owned by others? What about assets your client may acquire in the future?
- **Income** – will the client have to pay a portion of their income towards their debts ('income contributions') and if so, approximately how much?
- What other limitations might there be on the client's life as a result of the bankruptcy?

These are all covered in this Chapter.

**Note:** The same consequences apply when the client has been made bankrupt on a Creditor's Petition, although in that case there is no decision for the client to make. You can refer to this Chapter to advise your client about what to expect during bankruptcy. You should also refer to the bankrupt's obligations in **Chapter 8**. If your client has very recently been made bankrupt and does not think this should have happened, refer to **Chapter 10** – A sequestration order has been made against my client – Is there anything he or she can do? Advise your client to seek urgent legal advice.

## Part 9: Death and bankruptcy

### Summary

The Bankruptcy Act provides for the administration of a bankrupt estate after the death of the bankrupt. This can be at the instigation of creditors or the executor of the estate (for example, as an alternative to the State based process in circumstances where there are more debts in the estate than assets and the executor would like to hand the administration over to a Trustee).

A common concern of relatives of a deceased debtor is that they may be liable for the debts. This is not the case, but there may be less money or property available (or none in the case of a bankrupt deceased estate) for distribution under a will because debts must be paid out of the estate prior to distribution.

Whether a deceased person's share of a jointly owned property is available for creditors (whether the deceased is bankrupt or not) will depend on whether the property is owned by the deceased and another person (or people) as joint tenants or as tenants in common.

## The administration of insolvent deceased estates

Part XI of the *Bankruptcy Act* allows for the administration of the estates of deceased persons who were either insolvent when they died or when a deceased estate becomes insolvent due to debts incurred by the legal personal representative of the deceased estate (for example, the executor) after death.

Creditors can also apply for an administration order to be made against the estate of a deceased debtor. There does not need to be an act of bankruptcy but there must be a debt or debts totalling \$10,000 as with any other Creditor's Petition (see **Chapter 10 – Help I'm being made bankrupt!**). A judgment debt or Bankruptcy Notice is not required.

Where there is an *insolvent deceased estate*, it can also be administered under the appropriate State and Territory laws. For example, the *Probate and Administration Act 1898* (NSW) or the *Administration and Probate Act 1958* (Vic), provide for the proportional division of the estate among creditors where there are insufficient funds to pay the debts in full. However, it will often be easier for the executor or administrator to apply to the court for an administration order under the Bankruptcy Act and allow the trustee to deal with the creditors and beneficiaries. Administration of a deceased estate under Part XI of the *Bankruptcy Act* also gives the Trustee the power to recover property that would not be available to creditors under State and Territory probate laws due to the antecedent transaction provisions of the *Bankruptcy Act* (such as undervalue transactions, preferential payments or transfers to defeat creditors). Once a State based estates administration process has already commenced, the matter can only be dealt with under the *Bankruptcy Act* with the leave of the court.

The [Official Receiver's Practice Statement 5 \(ORPS5\) – Administration of estates of deceased persons](#) which can be found on the AFSA website gives information on the process.

As a financial counsellor the most likely scenario is where the executor of a deceased estate decides to file for bankruptcy under Part XI of the Bankruptcy Act.

The connection with Australia rules apply with regard to the deceased at the time of death.

When an executor applies to make a deceased estate bankrupt, the petition must be presented to the court (not the Official Receiver) and must be accompanied by a Statement of the Deceased Person's Affairs. The required paperwork is detailed in the above Practice Statement. The regulations also require that the legal personal representative give the Official Receiver a copy of the petition within 2 working days after the court endorses it.

### **What happens if the bankrupt dies during the bankruptcy administration period?**

The administration of the bankrupt estate continues as far as practicable.

### **What if the debtor is served with a bankruptcy notice prior to death?**

If debtor dies before service of Creditor's Petition, the creditor is required to proceed and present a Creditor's Petition under Part XI of the Act.

### **What if the debtor dies after service of a Creditor's Petition?**

If the debtor dies after the Creditor's Petition has been presented but before it is served, the proceedings lapse, and the creditor must commence new proceedings under Part XI of the Act. If debtor dies after service of Creditor's Petition but before the sequestration hearing the court can:

- make order that estate be administered under Part XI
- make an order to dismiss Creditor's Petition (on the usual grounds – see **Chapter 10**).

### **Relatives and their liability for the debts of the deceased**

When a person dies with debts, the relatives can be confused about the extent to which they are liable for those debts. In some cases, creditors may even pressure the relatives for payment (or the relatives may perceive they are doing so because they are receiving phone calls or sorting through mail intended for the deceased).

The deceased person's estate is liable for the person's debts, but the relatives are not. This may impact on the relatives if they receive less by way of inheritance than they otherwise would, but it does not mean they are liable to pay the deceased person's debts from their own funds.

If there is another person who owns property with the deceased (for example, their children or their partner) what happens will depend on whether they own the property as joint tenants or tenants in common (see **Chapter 6 Part 3**). If they own the property as tenants in common, the deceased person's share of the property (e.g. 30% or 50%) may be available to creditors. The amount of the share should be clear from the title documents or a title search. If the property is owned jointly, then the full amount of the deceased person's share passes to the other joint owners as a result of the doctrine of survivorship and none of it is

available to creditors (unless the joint owner is also a joint debtor or guarantor). The existence of a joint tenancy will not necessarily protect the property entirely from a trustee. Section 249A enables a trustee to secure a charge to the value of any improvement, as defined in s 294 on the property, subject to some exceptions.

**See the checklist for this chapter in Chapter 13: Tools and Resources**