Bankruptcy and Family Law – A Not So Happy Marriage?

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Bankruptcy

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Introduction and Scope

Unfortunately, the breakdown of a marriage is far too often accompanied by financial problems of one or both spouses. Sometimes these financial problems cause or contribute to the breakdown of the marriage, while in other cases the marriage breakdown causes or contributes to the eventual bankruptcy. There are of course also circumstances where the marriage breaks down for entirely unrelated reasons, but the situation will nonetheless be impacted where a bankruptcy intervenes in the process.

This paper explores how some of the most frequently asked about areas of family law (namely, support, matrimonial property, and dower rights) interact with a bankruptcy. While the basics are covered and some commentary is provided on some issues of interest, this paper is not intended to be an exhaustive review of this area of law. Therefore, readers are encouraged to take note of the "References and Further Reading" section at the end of this paper.

In addition, this paper is not intended to be relied upon as legal advice. Readers are advised to obtain legal counsel to explore their full range of options in light of their particular circumstances.

As one might observe during the course of reading this paper, the bankruptcy system does a fair job of contemplating and dealing with some areas of family law, but leads to serious conflicts in others. This conflict is most apparent in the treatment of matrimonial property.

The reader should be cautioned that matrimonial property regimes may differ significantly from province to province. This paper focuses solely on the law that is relevant in Alberta.

Throughout the paper, there is discussion about the solvent spouse, the insolvent spouse, and the trustee. For convenience, this paper presumes at times that the insolvent spouse is the husband, and reference is made to "him" or "he", and likewise for the gender of the trustee (most Trustees are actually corporate entities). Nothing is implied by this and it is not intended to give credence to any stereotypes; rather the aim is to assist with ease of phrasing and to avoid the reader having to put straight in his or her mind which spouse is the solvent one and which is the insolvent one.

Bankruptcy Basics

For those who practice primarily in the area of insolvency, this section of the paper may be elementary. However, it is common that some of the basic bankruptcy principles are quite foreign to those without significant practice in the insolvency area. This section will highlight a few of the basic principles to keep in mind as we explore more specific issues.

The following are some of the fundamental principles that will be most germane to the topics covered in this paper:

- The *Bankruptcy and Insolvency Act* ("BIA" or the "Act") is federal legislation. Where there is an operational conflict between the BIA and provincial statues, the BIA trumps provincial law.
- Bankruptcy triggers an automatic stay of proceedings against the bankrupt. There are a few exceptions here, with the ones relevant to the topics at hand discussed later.
- The bankrupt's "property" (which is broadly defined under the BIA – see section 2) vests in the Trustee upon bankruptcy (s.71). Accordingly, the trustee does not simply distribute the bankrupt's property – he becomes the owner of it. The trustee will generally proceed to liquidate the bankrupt's assets, and where sufficient funds are realized, pay a dividend to unsecured creditors (generally on a *pro rata* basis, although certain classes of unsecured creditors may have some priority over the general body – see s.136 of the BIA for the scheme of distribution).
- Upon the bankrupt's discharge, he is released from all debts and claims that are "provable" in the bankruptcy (with a few exceptions – see s.178), regardless of whether the creditor filed a proof of claim in the bankruptcy proceedings or even had notice of the proceedings (although there may be some remedies available for this latter situation). Provable claims are defined generally in s.121(1) of the Act as follows:

> All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be provable in proceedings under this Act.

Support

Claims for spousal and child support are specifically contemplated and addressed within the BIA, although the relevant provisions are somewhat scattered throughout the Act.

Actions for support by the solvent spouse are not stayed by a bankruptcy (s.69.41 of the BIA), which is an exception to the general principle mentioned in the "Bankruptcy Basics" section of this paper. This means an action for support can be commenced or continued in the ordinary course without regard to the bankruptcy. However, the solvent spouse cannot enforce her judgment or order against property that has vested in the trustee or against surplus income payments that the husband may have to pay into his estate as part of the bankruptcy process – see s.69.41(2) of the BIA.

The next question that may come to mind is whether a claim for support is a "provable" claim in the husband's bankruptcy. This can be important to the solvent spouse where the bankrupt had significant assets, as only proven creditors (i.e. those with "provable claims" who submit a proof of claim to the trustee) are entitled to share in any dividends that are paid.

Whether a support claim is provable is specifically dealt with by s.121(4) of the BIA. A solvent spouse has a provable claim if it is: