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WHY DO WE FORGIVE OUR DEBTORS?

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Regional

Why do we forgive our debtors?

In this article, Bob Wessels examines the Dutch debt discharge regime for natural persons and the tension it creates with the traditional principle that debts must be repaid. Drawing on the experience of the Netherlands, he explores the legal, social, and economic reasons for granting the honest but unfortunate debtor a fresh start.

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The editor of the Revista Concursal Latinoamericana invited me to contribute to the theme of this issue of the Revista: Discharge in insolvency law. I would like to provide my perspective on debt discharge given to natural persons (consumers, non-entrepreneurs).

The media in my country (the Netherlands) regularly focuses on the so-called debt problems of individuals: excessive credit, payment problems, evictions, food banks, thousands of homeless people, and debt restructuring. How does the Netherlands deal with this?

Since 1998, our country has had a debt rescheduling scheme for individuals under the Netherlands Bankruptcy Act. Debt rescheduling is, in short, a provision in this Act (containing over 80 articles!) that offers individuals who are heavily in debt the opportunity to put an end to their situation.

The court determines whether the scheme can be applied, and if so, an insolvency practitioner ('bewindvoerder') is appointed, a predetermined amount of income is protected, and the remaining income is made available to creditors. Debt rescheduling in the Netherlands usually lasts three years. However, since July 1, 2023, the general rule has been 18 months. During this period, the debtor is protected from claims by its unsecured (and preferred) creditors. These include the mail order company, the landlord, the health insurer, the mobile phone provider, the energy supplier, and so on. Incidentally, the arrangement does not infringe on the security rights of so-called separatists (usually mortgage-granting banks), nor does it affect certain fines and student loans, as these are entirely excluded from the arrangement. As a background: five years ago, the average discharge period in the EU Member States (which included pre-Brexit England & Wales, with discharges of just one year) was five years.

In the Netherlands, with a current population of around 18 million, tens of thousands have gone through this debt rescheduling scheme in the past 25 years or so. Why is the Dutch legislator doing this? The core objective of the law is to offer the 'unfortunate but honest' debtor the opportunity for a 'clean slate' ('schone lei') after a year and a half of forced savings has ended. The 'slate' ('lei') comes from the saying: 'start with a clean slate.' In the Netherlands, until the 1950s, shopkeepers used to write down their customer's debts on the slate ('lei', in Dutch a small blackboard) and erase them after payment. After the debt rescheduling procedure, a clean slate is obtained; the debtor's remaining obligations are converted into unenforceable obligations (so-called natural obligations).

Dutch law thus puts an end to the long-established legal and moral adage that a person must keep their promise; that a debtor must honor their word. That he must pay his debts and, if necessary, guarantee them for the rest of his life and with his entire fortune. This is a principle that has existed for two millennia: the Latin ‘redde quod debes’ (‘pay what you owe’ (Seneca, Liber II, Epistula XVIII.xiv)). Similar regulations exist in neighboring countries: Germany (‘Verbraucherinsolvenz’, ‘Restschuldbefreiung’) and Belgium (‘collective debt settlement’, ‘règlement collectif de dettes’). These countries also offer a legal route for individuals to a debt-free restart, but there are numerous differences in access, implementation, and duration.

Why is an exception being made to this age-old principle? In other words, why do we forgive our debtors?

Debt Forgiveness and Property Law

The concept of debt forgiveness falls on rather dry ground in general property law. The 1992 revision of the Netherlands Civil Code left the idea that in today’s society, everyone is free to obtain information about goods or services offered, to investigate, to test those goods, or to obtain information about them firmly intact. Everyone is free to enter into an agreement, and if concluded, they must honor that agreement: ‘Pacta sunt servanda.’ Concepts such as ‘an agreement is an agreement’ and ‘a man is a man, a word is a word’ express this idea. The consequences are clear. If you fail to fulfill an agreement, you are in breach of contract, and that breach obligates you to pay damages. This is, of course, different in the event of force majeure, but some causes of such force majeure are the debtor’s own risk. The general view is that a debtor’s financial inability does not justify an appeal to force majeure, even if the debtor found themselves in that situation through no fault of their own and even if the situation could not have been foreseen at the time. The majority view is that a debtor who commits himself is obligated to guarantee that his financial situation will enable him to fulfill his obligations: the creditor may rely on this. Any other solution would be unacceptable in economic life. This is, of course, strong language. In everyday practice, all this means that in the event of non-payment, a creditor can threaten bankruptcy and, if payment is not forthcoming, bankruptcy follows, which has a clearly punitive character. It is the expression of the Calvinist view ‘whoever is in debt is guilty and must pay.’

Nearly 30 years ago, the law significantly infringed on this age-old and widely accepted principle. The basic philosophy behind the law is that it is socially undesirable for citizens who find themselves in financial difficulties through no fault of their own to be pursued by their creditors indefinitely. The

law then introduced the 'finitude of debt,' giving bona fide debtors a new chance to build an economic life.

Debt Forgiveness and Insolvency Law

Even in light of the developments of insolvency law, the idea of debt forgiveness is far removed from its historical context. Until the Middle Ages, trade had barely developed in this country. There was little need for something like bankruptcy law at that time. But when (retail) trade emerged, initially, as in other parts of Europe, provisions regarding defaulters were primarily criminal in nature. In 1501, the city of Leiden (where my university is located) obtained from the Count of Holland the privilege of subjecting the bankrupt to a three-day mocking exhibition, even after he had relinquished his entire estate. In the edicts of Emperor Charles V (concerning the police) ('rakende de policie') of October 7, 1531, and October 4, 1540, defaulters were threatened with severe penalties flogging, 'gheesselinghe' and hanging with a rope ('ter doot met der coorde'). Only since the sixteenth century has bankruptcy law focused its sanctions on assets rather than on persons, individuals themselves. However, the harshness remained. This was true for centuries. Until the end of the last century, a debtor was required to continue paying, even after bankruptcy. They could—so it was said—be held liable for those debts for life.

Now back to the question. Tens of thousands in the Netherlands have been given a clean slate: why do we actually forgive our debtors? What principle, or even legal principle, underlies this?

Ethical-moral basis?

First of all, the idea itself isn't new. When I told some people I was thinking about the concept of debt forgiveness, they quickly said: yes, it's in the Bible. Indeed, there are several passages in the Bible that indicate that a person will not be haunted by debt for the rest of their lives. See, for example, Deuteronomy 15 (The Sabbath Year), the so-called forgiveness laws: 'At the end of seven years you shall grant forgiveness,' after which the methods of forgiveness are explained. And 15:7-8: 'If there is a poor among you ... you shall not harden your heart nor shut your hand against your brother in need, but you shall open your hand wide to him and lend him enough for his need.' From these and other passages it can be deduced that this is not a loan but a forgiveness every seven years (2 Kings 4:1-7 (The Widow's Oil) and Leviticus 25 (Sabbath and Jubilee Years)). The prayer well-known to many, The Lord's Prayer, also places forgiveness of sins at its heart: Give us this day our daily bread; and forgive us our debts, as we forgive our debtors.

So, does the Netherlands Bankruptcy Act embody what I now call an ethical-moral principle, grounded in the Christian faith? Perhaps in 1998, but that seems significantly less so now. For context, thirty years ago, the Netherlands had 21 percent Protestants and 33 percent Roman Catholics. That has now dropped to 14 percent and 17 percent, respectively.

American literature does refer to this biblical inspiration for the principle of 'debt forgiveness,' which it also applies. In this view, debt forgiveness is the expression of a form of Christian (or more broadly: religiously oriented) charity, which aims to bring about greater humanity in society. People are rescued from a quagmire of debt. An American view is that rehabilitation of debtors is part of the responsibility to treat members of society humanely. It promotes values of human dignity and respect. That sounds nice, but this principle does not offer a clear explanation, because it is clear that the Bible has in mind the truly poor and needy and not what we now call calculating citizens, who get into financial trouble through strategic actions, for example by working and not declaring income to the tax authorities, by abusing social security or by putting a house or a car in someone else's name.

Social basis?

A second explanation has a social dimension. For many decades, Dutch law has offered protection to the economically vulnerable, such as rent and dismissal protection and our social security system (sickness and unemployment benefits), although this has gradually become less extensive. A social-legal infrastructure of this nature, which offers a degree of protection, has also gradually become recognizable in property law since 1992, as stipulated in the Civil Code. I would like to mention the court's authority to mitigate a debtor's obligation to pay damages, where one of the factors to be considered is the parties' 'ability to pay' or the court's ability to mitigate an agreed contractual penalty, '... if fairness clearly requires it.'

Insolvency law also contains exceptions that offer the bankrupt some safeguards. For example, items that the debtor cannot reasonably afford to lose are excluded from the bankrupt estate. The law includes, among other things, the bed and bedding of the debtor and the resident members of his family, as well as their clothing, tools for the craftsman, and the household's supply of 'food and drink, serving the household's needs, for one month.' This provision, incidentally, has remained unchanged for three decades. And upon the final liquidation of the bankrupt's assets, the bankruptcy judge may leave 'some household goods' to the bankrupt. In this second perspective, the 'clean slate' is therefore one of the many measures a welfare state implements for its citizens. From this perspective, debt forgiveness is a measure of socio-economic policy.

A legal-political basis?

Or is the idea behind the principle of debt forgiveness not ethically and morally inspired, nor a socially embedded right to protection, but rather an appeal to citizens to reclaim their own independent place in the world? Obtaining a clean slate appeals precisely to the active side of the consumer, from the passive deviant debtor in the debt collection process to an active citizen claiming their right to participate as a full citizen again. The clean slate expresses human freedom of action in a world where money is becoming increasingly important. This perspective could be called a legal-political one, based on an ideal of active citizenship.

A land of three rivers?

I estimate that all three fundamental ideas resonate in the legal form of the Dutch debt rescheduling scheme. Does one of the three considerations perhaps prevail? The ethical-moral, religiously inspired view must be placed in its proper context. The debt forgiveness laws of two thousand years ago functioned in Israel at that time in what we would now call a social context, with a heavy tax burden to finance the urbanization process, a civil service, and a professional army. And the charity rule (the debt forgiveness law of that time is not law, because, in my opinion, a sanction is lacking) functions as a kind of collective hardship clause to rectify what has become socially distorted in seven years. The idea of leveling what has become distorted can also be used to support this view. In literature from the late 20th century, the position of the ordinary debtor was compared to that of the defaulting legal entity, with the position of the ordinary debtor being considered far inferior. Dutch law then functioned as a collective hardship clause to level out distorted relationships.

I myself have emphasized the social dimension as the underlying principle behind the legislator's chosen approach. The statutory regulation is based on further legal development of an interest worthy of legal protection from a social perspective. In the twentieth century, the position of a natural person has gradually been legally strengthened in those aspects of life essential for a general level of living and well-being: income generation (employment law), residential enjoyment (tenancy law), income expenditure (regulations on general terms and conditions; consumer purchases; travel agreements and financial products), product quality and safety (product liability). The debt rescheduling offers a protective instrument for those who, for whatever reason, succumb to the advantages or temptations of relatively easy access to credit.

This third view, that of active citizenship, is not without optimism. The image of the supposedly active citizen ('citoyen') is unrealistic, for example, when considering the many homeless people or groups close to the 'fatal circle.' They often incur debt, but they don't seem to fit the image of the

active citizen. Another objection is also obvious. If the clean slate essentially offers a limitation of liability for debts, the active citizen, especially the citizen who is well-versed in their own interests, is, as it were, challenged to obtain that slate. In this view, I miss the social necessity to prevent this calculating citizen from reaching his goal.

The downside of this ideal of active citizenship must also be mentioned: to remain a 'State' for everyone, the State (out of well-understood self-interest) needs citizens who contribute and can continue to contribute. After all, the ongoing execution of debts deprives the debtor of virtually all means of subsistence, and productive people contribute to prosperity and taxes. From this perspective, 'debt forgiveness' is a political mechanism to keep the State running and thus to recycle the over-indebted consumer so they can resume their place in society. Debt forgiveness is then a form of reintegration into (working) society. In the individual case, it concerns a situation perceived as so pressing that there is no prospect of debt satisfaction, and where the constant threat of enforcement disrupts, or even prevents, the social functioning of those involved.

Future perspective

With these modest reflections on justice—fairness, if you will—in Dutch insolvency law, I wanted to highlight the questions facing lawyers. The new generation of lawyers, in particular, should be challenged to test these possible explanations. And if one or a combination (or perhaps another) of these proves decisive, rest assured that other questions of fairness will arise. Is it fair to leave creditors with an unpaid claim? Shouldn't resolving a citizen's financial predicament also be the responsibility of all creditors, and therefore also the responsibility of secured creditors, such as the mortgage bank? And if the idea expressed in Europe in 2007 that 'financial rehabilitation of over-indebted individuals and families and their reintegration into society' is so important, shouldn't the bill be passed on to the community, ie that society? And if the principle of equality prevails, of leveling the playing field, is that principle limited to the Netherlands? Why do large differences exist in Europe (and perhaps beyond) in the treatment and settlement of debts?

If the reader of this Revista thinks independently and critically along the lines presented, difficult dilemmas will be exposed. The reader will then search for the underlying principles for legal rules. He or she will then not only apply the law but also contribute to its development.