

KF
1526
S76
C.2

Economic and Social Factors Effecting the Increase In Bankruptcy Filings

Walter C. Stoertz, Jr.

Court Executive Development Program

National Center for State Courts

April 10, 1998

rec'd 10-12-98

Library
National Center for State Courts
300 Newport Ave.
Williamsburg, VA 23187-8798

ABSTRACT	3
ECONOMIC AND SOCIAL FACTORS EFFECTING THE INCREASE IN BANKRUPTCY FILINGS	4
THE UNITED STATES BANKRUPTCY CODE	4
RELIEF UNDER THE CODE	4
WHO MAY FILE	6
THE CHAPTER 7 PROCESS	7
THE CHAPTER 13 PROCESS	9
BANKRUPTCY FILINGS ON THE RISE	11
ECONOMIC FACTORS	13
CONSUMER CONFIDENCE IN A STRONG ECONOMY	13
THE CREDIT CARD INDUSTRY	14
UNEXPECTED CHANGE IN ECONOMIC STATUS	16
JOB LOSS/DIVORCE	17
SOCIAL FACTORS	19
LACK OF STIGMA	19
ATTORNEY ADVERTISING	21
REPEAT FILERS	22
LACK OF BASIC EDUCATION ON PERSONAL FINANCING	25
COSTS AND CONSEQUENCES OF FILING	26
COSTS TO THE DEBTOR	27
ATTORNEYS FEES	27
<u>PRO SE</u> FILERS	28
FILING FEES	29
CONSEQUENCES TO THE DEBTOR	30
EFFECT ON THE COURTS	31
EFFECTS ON THE FINANCIAL INDUSTRY	32
A CALL FOR CHANGE	33
BANKRUPTCY REFORM	33
CONSUMER EDUCATION	34
REFERENCES	37

Abstract

Although it is widely reported that the present economic condition in the United States is the strongest it has been in twenty years, the rate of personal bankruptcy filings¹ has risen to an all time high. It could be easily concluded that indiscriminate consumer spending is the catalyst for this trend. In fact, it would seem that there are several factors that exist which have caused changes in consumer behavior, leading an individual who has suffered a certain loss of control over personal financial management to file for protection under the United States Bankruptcy Code.² This paper will review certain economic and social factors which could be leading so many Americans to seek voluntary relief in the United States Bankruptcy Courts.

¹ Personal bankruptcy filings represent filings under chapter 7 and 13 of the United States Bankruptcy Code.

² U. S. Bankruptcy Code - "the law relating to bankruptcy is codified and enacted as a new Title 11 of the United States Code" - effective October 1, 1979.

Economic and Social Effecting the Increase in Bankruptcy Filings

The United States Bankruptcy Code

Title I of the Bankruptcy Reform Act of 1978 provided for the enactment of Title 11 of the United States Code, the Bankruptcy Code, which became effective on October 1, 1979. For consumer debtors, the Bankruptcy Code is the source of law which may allow them to absolve themselves from the burden of their debt so that they may have another chance at leading productive lives free of their past financial problems. For creditors, it is a means of achieving an equitable distribution of a debtor's assets to which they may be entitled.

Relief Under the Code

An individual debtor seeking voluntary relief³ under the United States Bankruptcy Code will usually file a petition under chapter 7 or chapter 13.⁴ The filing of a voluntary petition under either chapter with the clerk of the

³ The majority of consumer bankruptcy petitions are filed as voluntary petitions although the Bankruptcy Code does provide for involuntary petitions filed by creditors.

⁴ Although it is possible for an individual to file for relief under Chapter 11 (Reorganization), such filings are rare since the protections available are limited.

bankruptcy court⁵, and the tendering of required filing fees⁶, automatically constitutes an “order for relief under such chapter”⁷ and operates as a stay⁸ to stop all “collection efforts, harassments, and all foreclosure actions”⁹ on the part of any creditor. At the time of filing the voluntary petition, the debtor is required to file a schedule of all assets, liabilities and budget¹⁰ as of the date of filing. At the conclusion of the proceedings under each chapter, unless the petition is sooner dismissed, the debtor will receive a discharge which serves as an absolution of any further responsibility to pay those debts listed in the debtor’s schedules for which no successful objection has been obtained by a creditor.¹¹

⁵ The U. S. Bankruptcy Court is a unit of the U. S. District Court and all matters arising under Title 11 are referred by the district court to the bankruptcy court pursuant to 28 U.S.C. § 157. A bankruptcy petition should be properly filed in the bankruptcy court located within the district where the debtor resides or is domiciled or where the principle assets of the estate are located.

⁶ 28 U.S.C. § 1930 requires that a fee of \$130.00 be paid to the clerk of court for the filing of a chapter 7 or chapter 13 case plus an additional \$30.00 miscellaneous administrative fee under either chapter and a \$15.00 surcharge under chapter 7.

⁷ 11 U.S.C. § 301.

⁸ 11 U.S.C. § 362.

⁹ Notes of Committee on the Judiciary, Senate Report No. 95-989.

¹⁰ Federal Rule of Bankruptcy Procedure 1007(b).

¹¹ Objections to claims - Federal Rule of Bankruptcy Procedure 3007; Adversary proceedings objecting to discharge - Federal Rule of Bankruptcy Procedure 7001.

Who May File

Any individual may file a bankruptcy petition under chapter 7 or chapter 13 who “resides or has a domicile, a place of business, or property in the United States.”¹² Under each chapter, an individual is not eligible to file a petition if he or she has been a debtor in a bankruptcy case pending within the preceding 180 days and “(1) the case was dismissed by the court for willful failure of the debtor to abide by orders of the court, or to appear before the court in proper prosecution of the case; or (2) the debtor requested and obtained the voluntary dismissal of the case following the filing of a request for relief from the automatic stay provided in section 362.”¹³

The significant difference in the eligibility requirements under these chapters is that under chapter 13, “only an individual with regular income that owes, on the date of the filing of the petition, liquidated, unsecured debts of less than \$250,000 and non-contingent, liquidated, secured debts of less than \$750,000, or an individual with regular income and such individual’s spouse, except a stockbroker or a commodity broker, that owe, on the date of the filing of the petition, non-contingent, liquidated, unsecured debts that aggregate less than \$250,000 and non-contingent, unliquidated, secured debts of less than \$750,000

¹² 11 U.S.C. § 109(a).

¹³ 11 U.S.C. § 109(g).

may be a debtor.”¹⁴ These limitations would unlikely be a concern for debtors with a low income.

Under either chapter, it is not specifically required that the debtor be insolvent, and only a husband and wife may file as joint debtors. Although the majority of chapter 7 bankruptcy cases filed represent filings by individual nonbusiness debtors, a corporation or partnership may also seek relief under chapter 7. A corporation or partnership may not be a debtor under chapter 13.

The Chapter 7 Process

Chapter 7 of the United States Bankruptcy Code provides for liquidation of all of a debtor’s non-exempt assets.¹⁵ For a person filing under Chapter 7, there are usually no assets to distribute.

Immediately after the filing of the voluntary petition, an interim trustee

¹⁴ 11 U.S.C. § 109(e)

¹⁵ Exempt assets are defined under 11 U.S.C. § 522(d) as certain limited values of interest in personal or real property, a motor vehicle, certain household goods or furnishings, or personal jewelry; unmatured life insurance contracts; professionally prescribed health aids for debtor or debtor’s dependents; rights to receive social security, veteran’s or disability benefits; right to receive an award under a crime victim reparation law; wrongful death payment; payment under a life insurance contract; limited payment for bodily injury; payment in compensation for loss of future earnings.

is chosen from a panel established by the United States Trustee.¹⁶ A notice of the stay and a date and time for a first meeting of creditors¹⁷ is sent by the clerk of court to the debtor, debtor's counsel and all creditors. In all chapter 7 cases, creditors are allowed 60 days from the first date set for the first meeting of creditors within which to file a complaint objecting to the discharge or to the dischargeability of a particular debt. If there appear to be no assets in the estate, the court will notify creditors that no claims need be filed unless there is later notification that assets do exist. Any property claimed as exempt is retained by the debtor, unless there is an objection. At the expiration of the 60 day period, if no assets exist, the trustee¹⁸ will file a final report and the court will enter an order discharging the debtor of all dischargeable debts.

¹⁶ The Bankruptcy Judges, United States Trustees and Family Farmer Bankruptcy Act of 1986 instituted a United States Trustee program to handle many administrative functions previously handled by the court such as supervising trustees, convening the meeting of creditors and monitoring fees charged by attorneys. The United States Trustee may also move for dismissal of chapter 7 cases if it is determined that provisions of the Bankruptcy Code may have been violated.

¹⁷ 11 U.S.C. § 341 provides that within a reasonable time after the order for relief in a bankruptcy case, the trustee will convene and preside over a meeting of creditors. The meeting allows the various parties to examine the debtor regarding his or her status and allows the trustee to learn what will be necessary to carry out his or her duties.

¹⁸ The interim trustee becomes a permanent trustee after the creditors' meeting pursuant to 11 U.S.C. § 702(d) unless the creditors vote to elect a trustee, which is rare in a consumer case.

In cases where the debtor has assets in the estate, the property of the estate is administered by the trustee. If there are only nominal assets, the property may be abandoned. After the meeting of creditors, the trustee will take over all property of the estate that is not exempt or has not been abandoned.¹⁹ The trustee will provide all parties with 20 days notice of a private sale or public auction of the property. A notice setting a deadline of 90 days within which to file proofs of claim is mailed by the clerk of court to all creditors. After the deadline for filing claims has passed, the trustee will file an objection to any claim deemed improper and the court will determine whether or not the claim will be allowed. Once the status of each claim has been determined, a distribution of the assets remaining in the estate is made to the creditors based upon the priority status of each claim.²⁰ After the distribution, the trustee will submit a final report and accounting to the court and the case is closed.

The Chapter 13 Process

Chapter 13 of the United States Bankruptcy Code pertains only to wage

¹⁹ In a chapter 7 asset case, the debtor will likely be discharged 60 days after the meeting of creditors if no complaints objecting to the discharge have been filed, since the trustee has taken over the property of the estate.

²⁰ 11 U.S.C. § 507.

earners. Under this chapter, the debtor is required to submit a plan setting forth the creditors to be paid as well as when, how and how much they will be paid.

Immediately upon the filing of a chapter 13 petition and plan, the standing chapter 13 trustee for the federal judicial district in which the bankruptcy petition is filed, is appointed.²¹ The automatic stay effectuated by the filing of a chapter 13 case also stays actions against most co-debtors who would have an obligation to pay any claim against the debtor.²² Any entity holding property of the debtor that the trustee may use, sell or lease or that the debtor may exempt, must be turned over to the trustee for delivery to the debtor.²³ Within 30 days of the filing of the plan, the debtor is required to begin making plan payments to the standing trustee for distribution to creditors.

The standing trustee presides over a first meeting of creditors. A creditor seeking to be paid through the plan may file a claim within 120 days after the conclusion of the creditors' meeting. The trustee reviews each claim and determines if any objections will be filed. A hearing to confirm the plan is scheduled at a time shortly after the creditors' meeting, at which time, any objection by a creditor to the debtor's plan is heard. If the plan is confirmed, the

²¹ Most federal districts appoint a standing chapter 13 trustee to act as trustee in all chapter 13 cases filed in that district.

²² 11 U.S.C. § 1301.

²³ 11 U.S.C. §542 and 11 U.S.C. §543.

debtor and all creditors are bound to the provisions of the plan. Most chapter 13 plans are arranged to allow for payments by the debtor over a 36 month period. In the event that a debtor is unable to complete the payments under the plan, the plan may be modified, the case may be converted to a chapter 7, a hardship discharge²⁴ may be entered if appropriate, or the matter may be dismissed.

After completion of all payments under a confirmed plan, the trustee will file a final report and a notice of proposed discharge is mailed by the clerk of court to all creditors and parties in interest. If no objections to the discharge are filed, an order is issued by the court discharging the debtor of all debts provided for by the plan and the case is closed.

Bankruptcy Filings On The Rise

According to the Administrative Office of the United States Courts, for the 12 month period ending March 31, 1997, 1,247,065 bankruptcy cases were filed nationwide. This is a record breaking number showing a 27 percent increase over the 980,126 cases filed nationwide during the 12 month period ending March 31, 1996.

²⁴ 11 U.S.C. § 1328(b) provides that a hardship discharge may be granted to a debtor prior to the completion of the plan, due to circumstances beyond the control of the debtor, if unsecured creditors have received as much compensation as they would have received in a chapter 7 liquidation.

While these figures include business as well as nonbusiness consumer bankruptcy cases, the growth during this period resulted primarily from the increase in filings under chapters 7 and 13. Chapter 7 filings showed an increase of 30 percent and chapter 13 filings showed an increase of 24 percent. Overall, of the 1,247,065 cases filed, 1,193,057 were nonbusiness filings.

The following table shows the total number of bankruptcy cases filed under each chapter, together with the total number of business and nonbusiness filings for the reporting years ended March 31, 1993 through March 31, 1997.²⁵

BANKRUPTCY CASES FILED NATIONWIDE YEARS ENDED MARCH 31, 1993 THROUGH 1997								
		TOTALS BY CHAPTER						
YEAR	TOTAL	7	11	12	13	OTHER	BUSINESS	NON-BUSINESS
1993	939,935	656,625	21,451	1,542	260,287	30	68,016	871,919
1994	858,482	590,191	18,105	1,062	249,087	37	59,571	798,911
1995	838,959	568,565	14,055	916	255,382	41	51,668	787,291
1996	980,126	665,310	12,901	988	300,901	26	52,210	927,916
1997	1,247,065	862,136	11,472	1,050	372,369	38	54,008	1,193,057

Although these totals show a downward trend in filings during the years 1993 through 1995, the totals for 1996 and 1997 show the trend moving

²⁵ Filing totals pursuant to the Federal Judicial Caseload Statistics, March 31, 1997, Administrative Office of the United States Courts.

dramatically upward, particularly in filings under chapters 7 and 13. It is difficult to project whether this upward trend in filings will continue into the next several years. A recent forecast by Regional Financial Associates, Inc. based in West Chester, Pennsylvania, projects that more than 1.54 million individuals will file for bankruptcy in the year 2007.²⁶ This projection becoming a reality depends directly upon whether or not the present economic and social factors leading so many individuals to the bankruptcy courts will change over the upcoming years.

Economic Factors

Consumer Confidence in a Strong Economy

Consumer confidence regarding personal finances as well as confidence in the U. S. economy, is the highest it has been in recent years and most Americans expect economic expansion to continue into the foreseeable future.²⁷ This sense of confidence has led to a rise in indiscriminate consumer spending and suggests that such rise will continue. Although the economy is generally stronger when people spend more, as indiscriminate spending rises, so does individual debt.

²⁶ Denver Business Journal, Friday, April 11, 1997, "Denver Bucks Bankruptcy Trend," Sougata Mukherjee, Washington Bureau Chief.

²⁷ According to the Money/ABC News Consumer Comfort Index, in June, 1997, the comfort index climbed eight points, with two-thirds of the public expecting economic expansion to continue over the next twelve months or longer.

According to the findings of a USA Today/CNN/Gallup poll published in June, 1997²⁸, the typical bankruptcy filer was found to be a married homeowner with an annual household income of less than \$30,000.00. Fifty-five percent of the filers were women. The average debt of the individuals polled, all having filed for bankruptcy within the preceding 12 month period, was \$47,000.00 owed to creditors, not including mortgage lenders. Twenty-nine percent of those polled reported serious financial problems existed for them for less than a year before they filed for bankruptcy. Fifty-eight percent of the filers were employed full time compared to 22% who were unemployed. Twenty percent of the filers were either divorced or separated.

The Credit Card Industry

The credit card industry is a strong force influencing consumer spending habits, and as such, seems to be a primary factor in the increase in bankruptcy filings. Most people filing for bankruptcy blame credit cards as the cause of their financial hardships²⁹.

Last year, credit card companies issued 2.4 billion solicitations to

²⁸ USA Today, June 10, 1997, "Profile of a Bankruptcy Filer."

²⁹ See footnote number 28.

prospective constomers through direct mail marketing.³⁰ Through these solicitations, as well as telemarketing solicitations, many consumers receive multiple pre-approved credit card applications in the mail each week, being tempted with offers of low introductory interest rates, and the availability to use new cards to pay off existing card balances. The average consumer holds four or more credit cards with an average balance per card of \$2,000.00.³¹

The combination of easy credit and the rise in consumer confidence has tempted many individuals to overspend and overextend themselves. The decision to purchase big ticket items where available cash on hand might not be present is made easier with the prospect of paying by installment through the use of credit cards, as are purchases for everyday items such as groceries, gasoline and even some household utility bills. With the high interest rates usually associated with each credit card, people in this category are no longer spending their income, they are spending credit. Over a period of time, indiscriminate consumers possessing several credit cards may find themselves with card balances equal to or higher than their annual salaries. It can become harder to make substantial payments toward the principle balance due on each card, eventually resulting in the inability to meet monthly minimum payment requirements. When many such individuals

³⁰ USA Today, June 10, 1997, "How Bankruptcy Finds Fertile Ground."

³¹ Mortgage Banking, Copyright 1997, Mortgage Bankers Association of America, February 1, 1997, Vol. 57, No. 5, ISSN: 0730-0212.

can no longer sustain this debt load, they file for bankruptcy.

It would seem that credit card companies would be experiencing considerable losses as a result of the increase in bankruptcy filings. Since the national economy depends upon consumer spending, dramatic cutbacks in credit made available to consumers would have a negative impact on economic growth. To counter the effects of bankruptcy filings on the industry, credit card companies set higher interest rates. As a majority of consumers likely will not lose control over their budgetary restraint as a result of credit card debt, companies extending credit might cut their losses by determining stronger standards in developing their market. This can be accomplished by limiting solicitations to individuals who may be of a less credit risk as well as setting stricter standards for eligibility based upon an individual's income and credit history. Although changes in marketing strategies are unlikely to decrease the immediate growth in consumer bankruptcy filings, over time there could be an effect.

Unexpected Change In Economic Status

Job loss/Divorce

Loss of employment and divorce are the two most common factors resulting in an unexpected change in an individual's economic status, often resulting in a decision to file for bankruptcy. Although national jobless rates have

decreased and a majority of workers are feeling a sense of job security due to favorable economic forecasts,³² 50 % of the debtors surveyed in the USA Today/CNN/Gallup poll cited job loss or a pay cut as their primary reason for filing bankruptcy. Thirteen percent cited divorce or separation as their primary reason.

The unemployment rate gradually declined during the 1997 calendar year, ending at 4.7%³³, but the means by which the rate is determined may be misleading as it relates to predicting the impact on unemployed consumers filing bankruptcy. A great number of unemployed workers stop searching for jobs after becoming discouraged in their attempts at finding employment. This group is generally not counted among the statistics that determine the number of unemployed. Divorce statistics show that close to 1.2 million marriages end in divorce each year and it is predicted that half of all new marriages will result in legal separation and/or divorce.³⁴

In the present economy, the greater availability of consumer and home mortgage credit has helped consumers attain a higher standard of living. Banks

³² According to Money/ABC News Consumer Comfort Poll, 86% of those polled do not expect to lose their jobs over the next 12 month period, up from 78% in 1993.

³³ The Mortgage Mart - current data reported January 9, 1998.

³⁴ Los Angeles Times, 5/27/96, page A16.

and credit card companies apply less stringent standards in determining extension of credit. Families with two incomes incur debt based upon the assumption that both incomes will be available to pay for those debts. This assumption may be based upon their sense of employment security during a stable economy and their belief in the strength of a marital union. For families living on too much credit, a high debt load can put them in a position of living pay check to pay check, or with very little savings. An unexpected life change, due to the loss employment of one partner or the break up of a marriage, may put them over the edge financially.

For the homeowner who encounters sudden unemployment, the situation may result in the depletion of any available savings to finance living expenses, then charging up to the limits of available bank or credit cards before exhausting all available resources, possibly ending in mortgage default. Over time, unemployed workers who have not been successful in finding new employment may lose job skills, making it more difficult to find a job. Eventually, they may find themselves losing their desire to work or accepting employment with fewer benefits and lower pay.

For the recently divorced individual with a high debt load, the challenge of maintaining the high standard of living attained through the benefit of two incomes can become a struggle. Even if the responsibility to pay the debts remaining from the marital estate is divided pursuant to a divorce agreement, if

one party stops making payments, the other party is responsible if his or her name remains on the debt. If one former spouse files for bankruptcy, the other spouse may be required to assume the responsibility for such debts.

Social Factors

In addition to the economic factors influencing the present boom in bankruptcy filings, there are also social implications contributing to the increasing statistics. Among today's American consumers, there is less stigma associated with bankruptcy and a greater awareness of filing bankruptcy as a remedy to hold off the aggressive collection tactics of creditors.

Lack of Stigma

In general, society's view of individuals who file bankruptcy seems to be changing. There is a growing social acceptance of bankruptcy and the stigma once associated with the word "bankrupt" has lessened. Individuals who suffer financial hardship are no longer perceived as societal misfits.

In particular, a study by the WEFA Group³⁵, an economic consulting firm,

³⁵ Mortgage Banking, Saturday, February 1, 1997, "A Bankruptcy Wake Up Call."

suggests that as the share of the population aged 25 to 44 increases, so does the number of bankruptcy filings. This age group does not look upon bankruptcy with the same stigma as other generations before them, who were influenced by times of greater financial hardship, once did. Adults in this age group typically borrow and consume at a greater rate than other age groups, leaving them less likely to have adequate savings on hand at times of financial distress and may be more inclined to file for bankruptcy.

Social acceptability of filing bankruptcy may also be predicated upon an individual's association with others who have filed. Of the people surveyed in the USA/CNN/Gallup poll who filed for bankruptcy last year, 51% said that they had a close friend or relative who also went bankrupt. In another poll of the general public,³⁶ 39% reported that they had a friend or relative who filed for bankruptcy.

Media exposure has also helped to destigmatize bankruptcy protection. The increased attention to bankruptcy in news reporting on television, radio and in print has worked to familiarize the public as to its availability. A cable television show titled "Debt" currently airs nightly, affording financially distressed consumer contestants to compete in answering trivia questions for a monetary prize equal to the value of their debt.

The retail industry has also worked to lessen the stigma of bankruptcy

³⁶ USA Today, June 10, 1997, "How Bankruptcy Finds Fertile Ground."

through advertising the availability of credit to bankrupt debtors for the financing of big ticket purchases, likely at higher interest rates. Major car dealers, electronics dealers and even consumer finance companies regularly use television, radio and print advertising to lure debtors, and former debtors, into their market. Such advertising exposes potential bankruptcy filers to the perception that they will not be altogether excluded from the market if they do decide to file. At the same time, bankrupt debtors may represent a lesser risk to such retailers since they have cleared their existing credit card balances, compared to other consumers who are carrying balances and struggling to pay their bills.

Attorney Advertising

A few years ago, attorneys who practiced bankruptcy law represented a very small segment of the bar. Bankruptcy practice was considered a specialized field and remained a foreign area ignored by most attorney's who chose the more lucrative fields of civil and/or criminal law. With the rise of consumer debt over the years, more attorneys have realized the potential monetary rewards available in soliciting for the representation of consumer debtors. As a result, there has been a growth in lawyer advertising to promote the availability of filing for bankruptcy, and the ease with which individuals can unload their liabilities under the

Bankruptcy Code. This has helped to make consumers more aware of bankruptcy as an option.

Attorney advertising can be found on local television and radio stations, in print ads on subways and in the yellow pages, often suggesting that a debtor may be able to retain everything he or she owns and be required to pay back little in return. Although not all attorneys who advertise can be considered unethical, such aggressive advertising can bring an attorney's ethics into question as it encourages bankruptcy filing without warning the consumer of the possible ramifications. To ensure that their counsel will be acting in their best interests, consumers who are not educated about the alternatives to bankruptcy should be careful to select an attorney who has a proven track record of being knowledgeable and ethical.

Repeat Filers

A current factor to be reviewed for its possible effect on bankruptcy filing statistics is the alleged problem of repeat filers under Chapter 13. These individuals are often referred to as "serial filers" because they engage in the repetitious filing of new bankruptcy petitions in order to benefit from the automatic stay provisions which had been lifted in previous filings, in an attempt

to continually prevent foreclosure or eviction proceedings on the part of creditors.

Section 109(g) of the Bankruptcy Code precludes any individual from being eligible for relief who, within the previous 180 days, has (1) suffered dismissal of a case for willful failure to abide by orders of the court or to appear before the court or (2) requested and obtained voluntary dismissal following the filing of a request for relief from the section 362 stay. This, however, does not prejudice the debtor from filing a subsequent petition.

An example of a bad faith, repetitive filing might involve a debtor who has defaulted on a mortgage and is facing a scheduled Sheriff's sale of his or her property. The debtor files a chapter 13 bankruptcy petition prior to the time of the sale, providing immediate protection under the automatic stay provision of the Bankruptcy Code. The sale cannot proceed unless the lending creditor files, and is subsequently granted, a motion for relief from the automatic stay. The time between the filing of the motion and the date of hearing is usually between 20 and 30 days, to allow time for the creditor to serve the motion and for the debtor to file any response as required by the bankruptcy rules. If the debtor is strategic in filing the petition close enough to the time of the scheduled Sheriff sale, the creditor will unlikely be able to seek relief from the stay until after the debtor has presented the Sheriff with a stamped copy of the petition, and the debtor will have successfully stopped the sale of the property. If the court subsequently grants the

creditor's motion for relief from the automatic stay and dismisses the case, the debtor files another bankruptcy petition to repeat the process and once again delay the sale. Although the actions of the debtor are clearly an abuse of the Bankruptcy Code, the debtor's success is predicated upon the fact that the clerk of the bankruptcy court has no authority to refuse a bankruptcy filing, regardless of the status of the debtor.³⁷ Consequently, the court can invoke section 109(g) of the Bankruptcy Code and bar the debtor from filing any further bankruptcy petition for a period of 180 days, or bar the debtor from any future filing without first obtaining prior leave of the court.

Congress is currently considering proposals from the consumer credit industry to discourage the repeated filing of separate bankruptcy cases by individuals seeking to evade creditors, but the issue of serial filers as a factor in the increasing number of bankruptcy filings remains a controversy. A 1996 Visa survey³⁸ of 5,000 individuals who had filed bankruptcy during the previous 12 months found that the number of individuals who had filed before was a "significant minority." Eighty-six percent had never filed before, but two-thirds of the remaining respondents had filed twice before, and the rest more frequently. The preliminary findings of an as yet unpublished empirical study on chapter 13

³⁷ Federal Rule of Bankruptcy Procedure 5005(a).

³⁸ Mortgage Banking, Saturday, February 1, 1997, Vol. 57, No.5, ISSN. 0730-0212.

repeat filings conducted by Susan L. DeJarnett, Professor of Law at Temple University, suggest that claims 'that repeat filings to stop eviction are a big problem' are greatly exaggerated, as is the view that repeat filings should be viewed as abusive. Professor DeJarnett's findings were based on a survey of 62 chapter 13 trustees, 55 of which suggested that eviction prevention was rarely the goal of repeat filers. The study further suggests that there is no need to impose limits on a debtor's right to refile since the Bankruptcy Code "provides ample means to police abuse by repeat filers."

Lack of Basic Education on Personal Financial Planning

While there may be a greater awareness of bankruptcy as a remedy to financial distress, the increase in filings suggests a broad lack of education among consumers regarding the principles of personal budget planning. For these individuals, there is a belief that bankruptcy is their only alternative when they become overextended.

The 1996 survey conducted by Visa³⁹ found that only 49% of the respondents sought professional debt counseling prior to filing for bankruptcy. This would suggest that alternatives such as setting up a personal budget,

³⁹ See footnote 38.

discontinuing use of credit cards to pay for everyday purchases, negotiating extended payment schedules with creditors or selling off expensive possessions to gain cash to pay bills often may not be considered before declaring bankruptcy.

A 1991 Gallup Poll⁴⁰ of over 1000 heads of household confirmed a general lack of financial planning among consumers. Forty-eight percent of those surveyed admitted that they don't usually set a budget for household expenses. Only 40% balance their checkbook each time they write a check and 22% said that they ever think ahead about their financial goals.

Costs and Consequences of Filing

Costs to the Debtor

As the public becomes more aware of the availability of filing for bankruptcy to bring immediate relief from the collection efforts of creditors, there are also certain unavoidable costs associated with filing which must be considered.

⁴⁰ Findings of the Gallup Organization, Inc., published in Mortgage Banking, February 1, 1997, Vol. 57, No. 5, ISSN: 0730-0212.

Attorney's Fees

Attorney fees for debtor's counsel in consumer bankruptcies typically range between about \$300 and \$800 in chapter 7 cases and up to \$1,000 or more in chapter 13 cases, depending upon the anticipated complexity of the case. Unlike fees charged by attorneys who practice in other areas of the law, bankruptcy attorneys are required by statute to disclose to the court the amount of compensation paid, or to be paid, by the debtor for services rendered.⁴¹ A statement of disclosure of compensation paid or promised must be filed with the court within 15 days after the order for relief.⁴² Most bankruptcy courts have adopted a local rule requiring that any fee charged in excess of a certain amount, usually around \$500.00, must be reviewed and approved by the court.

Pro Se Filers

A number of chapter 7 filers have no available resources to pay the fees required for representation by counsel. Many counties have community legal service organizations to assist indigent filers through legal representation, but as

⁴¹ Title 11 U.S.C. § 329.

⁴² Federal Rule of Bankruptcy Procedure 2016(b).

government funding for these agencies has dwindled, they are becoming less available. As a result, there are a number of individuals filing for bankruptcy pro se.⁴³ Although chapter 7 no asset cases are usually routine, with the debtor never having to appear before a judicial officer prior to a discharge hearing, the challenge of representing one's self in a bankruptcy matter can prove frustrating. There are consumer assistance agencies available in many communities where a pro se filer can obtain procedural aid in preparing the bankruptcy petition and required forms, but these agencies are usually not staffed with licensed attorneys and are therefore barred from offering legal advice. The filer often turns to the court clerk's office for guidance, but the code of conduct for judicial employees bars any court employee from offering legal advice to any litigant.

It should be noted that not all pro se filers are indigent. Many debtors filing under chapter 7 or chapter 13 represent themselves by choice, usually because of personal bias towards, or mistrust of, attorneys.

Filing Fees

In addition to attorney's fees, there are also required filing fees under each chapter to be paid to the clerk of court at the time of filing the petition. The total

⁴³ Individual representing himself or herself without assistance of an attorney of record.

fee for filing a chapter 7 bankruptcy petition is currently \$175.00 and the fee for filing a chapter 13 petition is \$160.00.⁴⁴ As these fees may not be waived, they may present a practical problem for an indigent filer, but rarely are a deterrent from filing.

The court can accept a bankruptcy petition without the full payment of the required fee only if it is accompanied by an application to pay in installments.⁴⁵ An individual debtor is only eligible to pay in installments if he or she has not previously paid any fees to an attorney for services in connection with the case. The filing fee must be paid in full over a period of 120 days, or 180 days if an extension is approved by the court, pursuant to a court approved schedule of not more than four installments. If the debtor fails to make a timely installment payment pursuant to the schedule set, the case may be dismissed.

The Bankruptcy Code does not provide for in forma pauperis filings by indigents.⁴⁶ However, on October 27, 1993, Congress enacted legislation requiring the Judicial Conference of the United States to study the effect of

⁴⁴ Title 28 U.S.C. § 1930 requires a total filing fee of \$175 for a case commenced under chapter 7 of the Bankruptcy Code, including \$130 as a miscellaneous administrative fee and \$15 for a trustee surcharge; and a total fee of \$160 for a case commenced under chapter 13 of the Bankruptcy Code including \$130 for the petition and \$30 as a miscellaneous administrative fee.

⁴⁵ Federal Rule of Bankruptcy Procedure 1006.

⁴⁶ In United States v. Kras, the U.S. Supreme Court found that due process does not require a right to waiver of the bankruptcy filing fee for indigents.

waiving the filing fee in chapter 7 cases under the Bankruptcy Code for individual debtors who are unable to pay the fee in installments. Six federal judicial districts were selected to participate in the study which began on October 1, 1994 and ended on September 30, 1997. The Judicial Conference is to submit to Congress a report describing the costs and benefits of the program by March 31, 1998. Congress will thereafter consider whether the program will be implemented nationwide.

Consequences to the Debtor

In addition to the financial costs of filing for bankruptcy, there are consequences to be faced as a result of filing.

1. An individual is not eligible to file for chapter 7 again for a period of six years.
2. A number of filers will find it difficult to successfully reestablish credit. A chapter 13 can remain on an individual's credit report for up to six years, while a chapter 7 remains for ten years. Many creditors and credit bureaus are more lenient with people who file under chapter 13 rather than chapter 7 since they generally receive more money in a chapter 13.
3. It may be difficult to lease an apartment or obtain a mortgage.

Traditional mortgage lenders with strict lending policies are reluctant to extend loans to individuals with poor credit histories. More progressive lenders, such as consumer finance companies, generally charge additional fees and higher interest rates.

4. Although the Bankruptcy Code protects an individual against discriminatory treatment,⁴⁷ it may be difficult to find gainful employment.

Effect on the Courts

The number of bankruptcy filings has had a major impact on the workload of the federal bankruptcy courts, and with the increased caseload, the system can suffer. Cases take longer to resolve and the incidence of fraud can increase. The United States Judicial Conference has determined that the average U.S. Bankruptcy judge has an annual weighted caseload of 1,306 hours.⁴⁸ The increased workload can leave judges with less time to study the law and write opinions, and the burden on clerk's offices can cause delays in keeping timely court records.

⁴⁷ 11 U.S.C. § 525(b) provides that no private employer may terminate the employment of, or discriminate with respect to employment against, an individual who is, or who has been, a debtor.

⁴⁸ Washington Business, The Washington Post, April 21, 1997.

The Judiciary has been working to get Congress to approve additional bankruptcy judgeships to handle the increasing caseloads.⁴⁹ However, Senate approval for funding as well as the selection and placement of new judges are timely processes and are not offering immediate relief.

Effects on the Financial Industry

The extension of easy credit by banks and other lenders has contributed to the increase in the number of consumers in default, and the rise in bankruptcy filings is causing considerable losses to the credit industry. Visa and MasterCard have estimated that bankruptcies cost their member banks \$8 billion in 1996⁵⁰ and expected the figures for 1997 to exceed \$9 billion. But while the banks and the credit card companies are cutting their losses, there doesn't appear to be any significant reduction in the offer of credit cards or higher credit limits. It is apparent that the credit industry needs to tighten its lax lending methods by more adequately analyzing potential markets for credit card solicitations and setting stricter credit standards.

⁴⁹ The Bankruptcy Judgeship Act of 1997, H.R. 1596, has been passed to authorize a total of 18 Bankruptcy judgeships, seven new and 11 temporary, but funding for all these judgeships has not been provided.

⁵⁰ Puget Sound Business Journal - Seattle/Tacoma, Friday, April 18, 1997.

A Call For Change

There doesn't appear to be a specific standard by which it can be predicted whether or not the current upward trend in bankruptcy filings will continue. It is certain that the affects of uncontrollable or unexpected life events such as illness, personal injury, natural disasters, unemployment and divorce will continue to have an impact on the bankruptcy industry. However, it can be determined that the only significant changes in the current trend can come as a result of congressional efforts to reform the Bankruptcy Code as well as efforts to change some of the factors influencing indiscriminate spending habits through the availability of consumer education and credit counseling.

Bankruptcy Reform

Under the Bankruptcy Reform Act of 1994, Congress established a nine member Bankruptcy Review Commission to study the need for amendments to consumer bankruptcy laws. The Commission is currently considering the following proposals:

- 1) To make bankruptcy exemptions more uniform to reduce possible varying results between debtors of similar status in different states;

2) To simplify the chapter 13 process and make it more appealing to the debtor than a chapter 7 case, so creditors would benefit from a greater number of repayment plans;

3) To curb serial filings by limiting the availability of chapter 7 discharge to only once every ten years instead of the present six years and chapter 13 discharge to only once every five years;

4) To randomly audit debtors to see if they have understated their income and assets;

5) To promote debtor education. Before the bankruptcy petition is filed, it would be required that debtors be given a notice setting forth alternatives and listing names and addresses of available credit counseling services.

Consumer Education

Probably the most effective way to influence financial literacy is to implement state mandated educational programs in schools, starting as early as grade school and extending through the high school level. Programs teaching fundamental principles of personal budget planning as part of the required school curriculum would expose individuals at an early age to the expenses that they will face as productive members of society and provide a basic foundation for

practicing financial responsibility when they come of age.

The credit industry now targets low earning college students as an appealing market on the theory that an individual's first credit card is the one that is kept the longest. It is not unusual for many credit card companies to solicit on college campuses and extend credit to students who list no employment on their credit applications. American undergraduate college students carry an average credit card balance of \$2,200.00 in addition to the \$12,000.00 in student loans for which they will be liable after graduation. It is estimated that the average starting salary out of college is \$24,000.00 a year, yet a graduate will need to earn at least \$38,000.00 a year before taxes to cover anticipated living expenses including their minimum monthly credit card payment, rent, food, utilities, transportation and student loan payments.⁵¹

Early education in the following areas is essential for preparing individuals to be financially responsible adults:

- 1) Setting financial goals;
- 2) Preparing a personal budget plan;
- 3) Available savings and investment opportunities;
- 4) Balancing a check book;
- 5) Methods for avoiding debt or escaping debt before it becomes

⁵¹ USA Weekend, March 6 - 8, 1998, "So Young And So In Debt," Jean Sherman Chatzky.

uncontrollable such as:

- Avoiding only minimum credit card payments;
- First paying the debts which carry the highest interest rates;
- Keeping an emergency cushion in the bank;
- Consolidating high interest rate credit cards into a single low interest rate loan.

Although consumer education can be an effective resource for avoiding problems, it will not yield immediate results. As such, consumer counseling is the most effective way to deal with problems once they start. The National Foundation for Consumer Credit Counseling has several hundred counseling facilities in operation in the United States where consumers can seek assistance. However, most debtors preliminarily seek advice of a bankruptcy attorney and are unlikely to subsequently seek assistance from a consumer counseling service prior to filing for bankruptcy. In either instance, it is important that individuals are properly informed as to the consequences of filing a bankruptcy petition and the possible alternatives available to them.

References

Bankruptcy Code, Rules and Forms. West Publishing, 1997 Edition.

Federal Judicial Caseload Statistics, Administrative Office of the United States Courts, March 31, 1997.

Charles W. Price, Attorney at Law. "Life After Bankruptcy." Practical Publications, Inc., Tallahassee, Florida, 1993.

Henry J. Sommer, Esq. "Consumer Bankruptcy Law and Practice." National Consumer Law Center, 1998 Third Edition.