Senate Banking, Housing and Urban Affairs Committee

Subcommittee on Financial Institutions & Regulatory Relief

Hearing on Bankruptcy Reform

Prepared Testimony of Ms. Dorinda Simpson
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10:00 a.m., Wednesday, February 11, 1998

Good morning. I am Dorinda Simpson, CEO of American Partners Federal Credit Union in Reidsville, North Carolina, and I appreciate the opportunity to be here to tell you about our concerns with the increasing number of bankruptcies and how this is impacting credit unions -and my credit union in particular. I am speaking on behalf of the Credit Union National Association (CUNA), which represents over 11,000 state and federal credit unions nationwide. We are very pleased that this subcommittee is holding hearings today on the important issue of bankruptcy and recognizes the fact that "consumers who pay their debts in full are bearing the burden of the high cost of bankruptcies."

American Partners is a $32 million federally-insured credit union with 9,000 members that work in local industry in the north Piedmont area of North Carolina. Our members have invested their savings with us, and in turn, we offer a range of credit to our members --currently a bit over $8 million in car loans, almost $9 million in home-secured loans, and over $5 million in personal loans. In addition, we have issued 3,000 credit cards for an additional $2 million plus.

Everyone is aware of the incredible increase in consumer bankruptcy filings --which topped 1.3 million in 1997 and is expected to exceed that in 1998. Chairman Faircloth, you may be interested in the bankruptcy situation in North Carolina, where it appears that consumer bankruptcies have been increasing at a faster pace than elsewhere. In 1995 the nationwide increase in such filings was 12.1 %, in North Carolina the increase was 20.7%. In 1996 the nationwide increase was 28.6%, but 41.3% in North Carolina.

We are quite concerned at our credit union about the steady increase in bankruptcy filings nationwide in the last few years because we have seen that same increase in the number of our credit union members who file. In 1994 we had only 6 members who filed for bankruptcy; in 1995 there were 17; in 1996 that number rose significantly to 37; and in 1997 to 41 --an increase since 1994 of over 500%! And already in 1998 two credit union members have filed for chapter 13. A significant number of our bankruptcies are chapter 7, which cause the greatest loss. As the number of member bankruptcies has increased, so too have the losses to the credit union. In 1997 alone the actual bankruptcy losses were $119,550, up from 1996's $92,781. This information is attached to my testimony and shows the outstanding balance of loans subject to bankruptcy at the time of the filing. CUNA estimates that more than half of all credit union losses in 1996 were bankruptcy-related and that those credit union bankruptcy losses in 1997 will exceed $700 million.

American Partners is a careful lender. We cannot afford to be otherwise. We do a good job with scrutinizing loan applications and carefully determining that the applicant is creditworthy before extending credit. We examine credit reports, verify income, and see that a reasonable debt-to- income ratio is maintained by the borrower. We even look at the applicant's disposable ificome to determine that the applicant can make the payments.

We also try to educate our members about alternatives to bankruptcy. We offer credit counseling to all our members at any time and encourage them to come to the credit union for help if they are experiencing financial difficulties. We tell the members about this service in our newsletter and in statement stuffers, and examples of these are attached to my testimony. My staff has told me that after such a mailing typically five to six members respond seeking help. However, even with financial counseling we certainly recognize that there are instances in which bankruptcy may be the only alternative for members and the way for them to get a needed "fresh start." Credit unions clearly recognize the value of financial counseling for their members. According to a recent CUNA bankruptcy survey, 70% of credit unions counsel financially troubled members at the credit union. A similar percentage of credit unions may also refer members to an outside financial counseling organization, such as the Consumer Credit Counseling Service, and many do both.

Because we are a not-for profit cooperative financial institution, losses to the credit union have a direct impact on the entire membership due to a potential increase to loan rates or decrease in interest on savings accounts. Therefore, we have a policy that if a member causes a loss to the credit union, services to that member, aside from maintaining a share account, will be withheld. And our members take it seriously because they do not want to cause a loss to the credit union. For example, several years ago a member filed chapter 13 bankruptcy and for months thereafter avoided the credit union. Obviously, she was embarrassed. Then the company she worked for was sold, and when she received her profit sharing check, she brought it in and paid everything we had discharged from her bankruptcy filing. She did not want the credit union to lose any money. And, we were able to offer her a checking account and credit card with a reasonable interest rate --something she might not have been able to obtain elsewhere.

We try to attend every 341 hearing, where creditors are permitted to question the debtor. I have noticed that so many of the debtors are young (25 years old or less) and do not seem to know why they are there or what bankruptcy means. Sometimes they do not attend the hearing. A number of our members, who file for chapter 13 and agree to a plan, fail to make their first payment into the plan, and their plan is dismissed. We then repossess their car. A second bankruptcy is filed, we return the car, and again they fail to make their first payment -- it goes on. Sometimes members who are under a chapter 13 plan even come back to us and try to borrow money from the credit union!

The National Bankruptcy Review Commission filed its report with Congress on October 20, 1997, and credit unions were very actively involved during the commission's review of the bankruptcy system --as can be seen from the references to them in that report. Credit unions were in attendance at almost all of the commission's public meetings, participated as panelists at many of the meetings, and wrote over 120 letters to the commission. A credit union person also testified before the commission in December 1996 as CUNA's representative of the National Consumer Bankruptcy Coalition. In general, CLTNA was disappointed in the consumer bankruptcy recommendations adopted by the commission in a 5-4 vote. In particular, we believe the commission erred in not adopting a needs-based bankruptcy recommendation that a debtor who can repay at least part of his/her debts should be required to do so. However, we were pleased that several commissioners did urge such a recommendation in a minority r6port. Credit unions were also disappointed that the commission recommended eliminating the reaffirmation of unsecured debt and greatly limited the possibility of reaffirming secured debt after credit unions had been especially vocal about the benefit of reafffirmations both to the credit union and to the members who can thus continue to obtain reasonable credit.

Again, let me say that I am pleased you are holding this hearing today. Credit unions are very anxious to see Congress enact meaningful bankruptcy reform and believe that "needs-based bankruptcy" presents the best opportunity to achieve this important public policy goal. Happily, there are bills in both the Senate and the House that offer a needs-based approach, and we encourage you to push for passage of such bills before Congress' fall recess. CUNA has endorsed the needs-based approach of a House bill, H.R. 2500, and is pleased that the Grassley- Durbin bill, S. 1301, contains a needs-based provision. However, we prefer H.R. 2500 as a fairer, more certain, less litigious alternative. On the House side, H.R. 3150, another needsbased reform bill, was just introduced by Rep. Gekas (R-PA), together with Reps. Moran (DVA), McCollum (R-FL), and Boucher (D-VA) last week. CUNA also supports this bill, which mirrors H.R. 2500's needs-based provision. The bill permits a debtor with an annual income of less than 75% of the national median income to automatically be allowed to choose whether to file a chapter 7 or a chapter 13. CUNA urges a change to this needs-based formula's 75% threshold to a test more relevant to rural or regional conditions that might substantially differ from the national average. We are pleased that the Gekas bill also contains a "Debtor's Bill of Rights" and a pilot program for consumer education. This bill attempts to strike a balance between making bankruptcy laws fairer and helping consumers avoid or better manage their debt. This is consistent with the primary concerns of credit union members. CLTNA hopes to embark on a nationwide consumer education campaign in the future to help consumers avoid the pitfalls of bankruptcy altogether.

Thank you. I will be happy to answer any questions.
