Senate Banking, Housing and Urban Affairs Committee

Subcommittee on Financial Institutions & Regulatory Relief

Hearing on Bankruptcy Reform

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INTRODUCTION

Mr. Chairman and Members of the Subcommittee, on behalf of our low-income clients, the National Consumer Law Center thanks you for inviting us to testify today regarding consumer bankruptcies and their impact on the banking system.

There is a great deal of misinformation circulating about the increase in bankruptcy filings and purported abuses in the system. The reality is that more debtors use the bankruptcy system because more debtors are having serious financial problems. American families increasingly face foreclosure, repossession, utility shut-off, wage garnishment and extensive collection activity on unsecured credit card debt. In short, more American families are using the bankruptcy system, because more American families are having trouble paying their debts.

My testimony will focus on four questions:

- Why more filings?
- Can the system efficiently capture more money for creditors?
- Are substantial costs of bankruptcy passed on to consumers?
- What reforms to the system are necessary?

I. WHAT HAS CAUSED THE INCREASE IN FILINGS?

The fact that more bankruptcies are being filed is not evidence, in itself, that debtors are abusing the system. The reality is that more cases are filed, because more American families are faced with crushing debt. There is much more consumer credit outstanding than ever before. With the additional extension of credit, comes additional risk. (See the Case Study in the Appendix for a typical example of an American family forced to file bankruptcy because of the convergence of consumer debt, job loss and divorce.)

The increase in bankruptcy filings is an unfortunate consequence of several significant structural changes in the American economy. These changes have combined to create a rise not only in bankruptcy, but also in foreclosures [2], repossessions, utility disconnections [3], credit card defaults [4] and visits to consumer credit counseling agencies. [5] Nevertheless banks continue to record profits, fueled in large part by credit card income.[6]

These are the factors which have contributed to the increase in filings:

- **Downsizing, economic dislocation, income disruptions and underemployment.** Families are increasingly impacted by instability in employment income, particularly at the lower end of the wage spectrum. [7] Although unemployment remains low, many workers file bankruptcy after being forced to shift to lower paying jobs. [8]

- **Rising debt to income ratios.** More families have more debt. Part of the reason for this is that the lending community has aggressively marketed credit card debt, [9] because it profits from the very high interest rates. Another factor is the unprecedented increase in the cost of education and the corresponding increase in student loan debt. [10] One family in six below $25,000 in annual income, spends more than 40% of its income on debt service.[11]

- **Reliance on two wage earners to make ends meet.** This change in a fundamental condition of the economy means that every family has double the risk. With two wage earners vulnerable to income instability, any change for either one creates enormous pressure on the family budget. Child-bearing and time off to raise children means that a family which was getting by on two incomes is forced to rely on only one.

- **Rising divorce rates.** A corollary of the latter factor is that when a family splits up, the pressure of running a household with less total income is impossible. Bankruptcy debtors are disproportionately single parents. [12]

- Uninsured medical debt. At a time when a two day stay in the hospital to deliver a baby can cost as much as $20,000, the uninsured have virtually no options to manage medical debts.[13] Bankruptcy has played an increasing role as the only way out. [14]

- **Aggressive Creditor Collection Action.** Wage garnishments, debt collection by aggressive telephone calling, and pursuit of legal remedies push many families int bankruptcy.[15] Few debtors can afford to pay an attorney to defend against a debt collection or wage garnishment action even when they have valid legal defenses. [16] Many bankruptcy filers report that their attempts at non-bankruptcy payment arrangements were rebuffed.

- **Deregulation.** As rates and terms of credit have been deregulated, an increasing number of American families have gotten credit on bad terms. [17] High rate home equity loans, credit card interest rates exceeding 18%, and consumer fraud tied to credit are frequent contributing causes of bankruptcy. [18] As some borrowers are increasingly pushed into "sub-prime" loans at high rates, the bankruptcy system is at the fulcrum of a "chicken and egg" problem. Are high risks justifying high rates, or are the high rates causing defaults which generate risk?

- **More Credit Means More Bankruptcy.** The clearest correlation of bankruptcy cause and effect is between the increase in the amount of credit outstanding and the number of filings. The number of bankruptcies and the total amount of consumer debt in our society have moved upward together in lockstep. [19] it is not surprising that as more Americans borrow more money, more families have financial troubles.

These reasons for the increase in bankruptcy filings are complex. Although banks and other lenders are correct in pointing out that they are not entirely to blame, it is disingenuous of them to assert that they should not bear sorne responsibility, at least to the extent of their own conduct.

Credit solicitations and other forms of marketing are designed to encourage consumers to rely on credit. Much of the marketing is done to people who once would have been considered high risk. Due to high interest rates, the lending community has discovered that it profits when people get in over their heads so that they cannot pay their balance in full each month.[20] This generates remarkable profits for banks. However, it also makes consumers vulnerable even to small life problems which can put them over the edge.

Appropriate consumer protections designed to address the lending community's responsibility to make good lending decisions might include:

- enhanced disclosure to consumers about the consequences of making minimum payments,[21]
- enhanced disclosures concerning teaser rates of interest, [22]
- protections against unilateral interest rate increases which are unrelated to a change in the lender's cost of funds,[23]
- prohibition of unilateral credit limit increases,[24]
- prohibition of security interests based in credit card agreements,[25]
- protection against so called "cashed check loans",[26]
- prohibition of credit card cash advance machines in casinos, [27]
- prohibition against making credit cards available to persons such as students who have no present ability to make more than nominal payments,[28] and
- reregulation of interest rates. [29]

Some of these provisions are in a bill which has been filed in the House of Representatives. [30] If lenders choose not to address these problems themselves, they ought not to complain about the bankruptcies which are the inevitable result.

II - IF WE CAN'T STOP AMERICAN FAMILIES FROM FILING BANKRUPTCY, CAN WE REDESIGN THE SYSTEM TO MAKE THEM PAY?

Nobody likes to be owed a debt which is not paid back. Yet our society has a system of debt forgiveness which has roots in the Bible. [31] Forgiveness and a fresh start have always been a part of that system. [32]

A family's ability to repay its debts is limited by its income. Data shows that Americans in bankruptcy are far poorer than their non-bankrupt counterparts. The median income of a family in chapter 7 bankruptcy is approximately half the national median. [33]

The credit industry has focused substantial resources on showing that despite this relative poverty, there are many families who are obtaining a bankruptcy fresh start even though they can afford to pay. Based on this assumption, they would set up a system in which debtors are forced into payment plans. [34]

However, if such plans are not entered voluntarily by the debtor, they have little chance of success, absent extensive and impracticable coercive mechanisms. For this reason, forced participation in payment plans has consistently been rejected by Congress and the two most recent goverment sponsored commissions which have studied bankruptcy. [35]

Apart from this procedural difficulty, there is no empirical evidence which shows that debtors can afford to pay. In 1989, Professors Sullivan, Warren and Westbrook published the results of an evaluation of a substantial statistical database and concluded:

> The overwhelming majority of Chapter 7 debtors -90% by any measure-- could not pay their debts in Chapter 13 and maintain even the barest standard of living. ... A new bankruptcy regime that invested more time to find and to investigate the potential can-pay debtors would prompt only a small amount of new repayment. This is the

classic case in -which a policy maker asks if the game is worth the candle. [36]

The creditor industry's own study released last year, [37] purporting to show the opposite, has been severely criticized by the General Accounting Office. [38] Once the credit industry study's results are adjusted to take account of the GAO critique, it shows that only about 5 % of debts could be repaid by debtors -- *if they undergo five year repayment plans.* [39] This means that the creditor's own study ultimately shows that bankruptcy debtors can afford to pay about a penny on the dollar per year.

Outside bankruptcy, no reasonable creditor would spend more than a penny to collect a penny. Proposals to require five year payment plans for many more debtors have a heavy price tag, including costs of administration and monitoring, costs to resolve disputes about capacity to repay, and costs of collecting and distributing payments.

Either the taxpayer would have to fund these costs, or if they are debtor funded, they will reduce the receipts available to creditors in a repayment plan. If taxpayer funded, every American would be helping banks and other creditors collect their one cent per dollar per year. If debtor funded, the one cent per dollar per year repayment capacity of debtors is even further reduced.

Finally, requiring five year repayment plans would have enormous social and human costs. People use the bankruptcy system for many legitimate reasons. If navigating the system is made more difficult, and if a meaningful fresh start is denied when some cases inevitably fail, [40] more debtors would be left with the burden of unmanageable debts.[41] Loss of homes, repossessions, wage garnishments, utility shut-off and family stress associated with unmanageable debts would be the inevitable result. While these social and human costs of denying chapter 7 relief to debtors may be difficult to quantify, they nevertheless remain an important part of the relevant equation.

III - ARE CONSUMERS PAYING THE COST OF THE CURRENT BANKRUPTCY SYSTEM?

The banking industry has claimed that it is losing 40 billion dollars each year to the bankruptcy system and that it is passing those costs on to consumers at the rate of $400 per family. *These numbers are utter nonsense.* Families may be discharging debt in bankruptcy, but the creditor's own study, discussed above, shows that these are not debts which consumers can afford to pay.

In reality, the lending community is scapegoating the bankruptcy system for losses associated with bad loans. The vast majority of debts which are discharged in bankruptcy would have been written off if no bankruptcy had intervened. The only impact of the bankruptcy case is that it gives debtors a legally enforceable fresh start -- the same second chance which has been guaranteed since Biblical times.

Equally important, there is no evidence that lenders would reduce rates on unsecured consumer lending if they could avoid bankruptcy losses. Between 1980 and 1992, the federal funds rate at which banks borrow fell from 13.4% to 3.5%. Nevertheless credit card interest rates actually rose. [42] How likely is it that other types of savings, if any could be realized, would be passed on to consumers?

To a large extent, the bankruptcy "problem" is nothing but a "bad loan" problem. It could be fixed if lenders were more closely attentive to underwriting. For the most part, the lending community has chosen not to take this step. The present interest rate environment has taught lenders that substantial profits can be made from extending credit to risky borrowers, such as, college students. However, in exchange, the banking community must accept that it is reaching some borrowers who cannot afford to pay.

IV - WHAT SHOULD BE DONE?

The bankruptcy system established in 1978 has been remarkably efficient. It provides critical relief to financially troubled American families at a low cost to taxpayers. Over the years, many open issues under the bankruptcy law have been resolved by court decisions and carefully crafted Congressional amendments.

To the extent the increase in the number of bankruptcies suggests that there are problems in the consumer lending system, responsibility for fixing those problems must be shared between consumers and lenders. Congressional reforin, if any,_should be balanced and narrowly targeted at abuses by both debtors and creditors.

It would be a mistake to enact reforms without addressing reckless lender conduct which pushes people into bankruptcy. Offering additional credit, for example, to families already struggling to pay their debts hurts not only borrowers, but also the borrowers' honest creditors if the new credit pushes the family over the edge" Similarly, failure by one creditor to seriously consider payment arrangements outside bankruptcy for families facing hardship may lead to a bankruptcy filing which affects all creditors.

Although we do not agree in many respects with the Report of the National Bankruptcy Review Commission, that commission did important work, at Congressional behest, which should be treated seriously by Congress. The Bankruptcy Review Commission heard from hundreds of witnesses on consumer bankruptcy over the course of its work. [43] Most of the neutral witnesses, judges, law professors, economists, and bankruptcy trustees have recommended and continue to support balanced reforms rather than enactment of a creditor's wish list. The majority report of the Review Commission is reasonably balanced and a good start for Congressional consideration.

To the extent there has been a focus on debtor misconduct, the burden of proof remains on the credit industry. To date it has not been met. Simply saying that more people are using the system, is not proof that people are misusing the system.

Some observers ignore the fact that the present system already has a variety of protections which are designed to effectively root out abuses by debtors. These include: Rule 9011,[44] objections to discharge, [45] complaints to determine dischargeability, [46] good faith requirements, [47] Rule 2004 examinations, [48] creditor's meetings, [49] dismissals for substantial abuse, [50] and criminal sanctions. [51] indeed, it is unclear why the creditor community does not believe that the small number of cases where significant repayment appears possible are not resolvable under the "substantial abuse" test of 11 U.S.C. 707(b). [52] Most of the anecdotal evidence of abuse which exists arises not because the system is broken, but rather because these provisions have been effective in bringing the abuse to light.

An additional set of balanced reforms may be appropriate as long as they do no harm to the majority of honest debtors who urgently need help. Provisions should be narrowly targeted to address debtors who truly are abusing the system without affecting lower income debtors who would be hurt by having to litigate additional issues [53]

Appropriate reforms would also do more to create incentives for debtors to use a repayment plan option in bankruptcy in order to repay their debts. Significant actions could be taken to make the costs of those plans more manageable and to enhance outcomes for debtors who complete plans. [54]

Additionally, the system should penalize dishonest creditors whose actions push people into bankruptcy. Honest creditors should be preferred to abusive debt collectors, lenders that encourage gambling in casinos, high rate mortgage lenders, and lenders who are unreasonable in refusing to accept non-bankruptcy payment plans. Lenders whose actions violate the bankruptcy laws should be subjected to meaningful and straightforward penalties.

CONCLUSION

The lending community should not be allowed to scapegoat the bankruptcy system for lending decisions which result in bad debt. The right to participate in the bankruptcy system should require honesty not just on the part of debtors, but also by creditors.

Radical change has the potential to undermine the economy by changing the fundamental balance between debtors and creditors. Concerns about the health of the banking system are unwarranted during this period of record bank profits. No legislative action should ignore the significant hardships of the millions of American families who are overwhelmed by debt.

Appendix

Case Study

Mrs. M is a 39 year old mother of three children, two of whom are living at home. Her financial problems started in 1994 when her husband lost his job in construction. Since that time, he has been under-employed; his earnings have declined from an average of $52,000 annually between 1990 and 1993 to an average of $26,000 between 1994 and 1997. Starting in 1994, the family's primary income has been $30,000 which Mrs. M earns as an administrative assistant at an insurance company. Mr. and Mrs. M have struggled successfully to maintain payments on a home they bought in 1987 since their financial problems began in 1994.

Mr. and Mrs. M have also had significant credit card bills since the late 1980's. Despite their financial problems, they avoided default on those debts by making minimum payments between 1994 and 1997. However, the total amount of their credit card debts increased from about $11,000 in 1994 to about $29,000 in 1997, largely due to the accumulation of interest at an average annual rate of 17.5%.

In 1997, Mrs. M's financial problems worsened, because Mr. M moved out of the family home. An additional strain was created because Mrs. M attempted to provide financial help to her oldest daughter who began her first year of college. In family counseling, Mr. and Mrs. M acknowledged that their marriage was breaking up largely because of the constant pressure of financial problems and Mr. M's continuing inability to find steady work.

Mrs. M attempted to make payment arrangements with her credit card lenders so that she could focus on her mortgage obligation. She was told that no payment arrangements were possible and that she should "borrow money to pay off the debts". Mrs. M went to consumer credit counseling where she was advised that her budget did not support any payments on credit cards. She was advised to consider chapter 7 bankruptcy in order to eliminate the credit card debts so that she could maintain her payments on the mortgage.

In September, 1997, Mrs. M obtained advice from a bankruptcy lawyer and reluctantly filed bankruptcy. She will discharge approximately $35,000 in unsecured debts. She will reaffirm and continue to make payments on her mortgage and car loan -- totalling $1,320 monthly.

Notes:

[1]The National Consumer Law Center is a nonprofit organization specializing in consumer credit issues on behalf of low-income people. We work with thousands of legal services, government and private attorneys around the country, representing low-income and elderly individuals, who request our assistance with the analysis of credit transactions. The National Consumer Law Center also serves as an advocate for low-income consumers on consumer lending and bankruptcy. NCLC publishes materials for lawyers and consumers, including the nationally acclaimed book Surviving Debt: A Guide for Consumers. NCLC has trained lawyers and counselors nationwide on consumer protection issues relevant to low-income consumers. My own experience includes 12 years as an attorney representing clients in bankruptcy, as an advocate for consumers on bankruptcy issues, as a teacher and trainer of other lawyers, and as an author of books on bankruptcy and consumer debt. My work also focuses on helping homeowners with financial problems avoid foreclosure. The bankruptcy system has always provided an important means to that end.

[2] Foreclosures have more than tripled since 1980. There were approximately half a million foreclosures in 1996.

[3] See National Consumer Law Center, "The Energy Affordabilty Crisis of Older Americans " p. 23 (August, 1995).

[4] Ausubel, "Credit Card Defaults, Credit Card Profits and Bankruptcy", 71 Am. Banker. L.J. 250 (1997).

[5]The number of consumers who have visited consumer credit counseling for help in the last 20 years has increased at a faster rate than bankruptcy filings. More than two million families sought such help in 1997.

[6]Commercial banks earned 14.8 billion in the third quarter of 1997, the third consecutive quarter of record profits and the 19th consecutive quarter involving profits of more than 10 billion. See Ausubel, Credit Card Defaults, Credit Card Profits and Bankruptcy, 71 Am. Banker. L.J. 250 (1997) for a discussion of the role of credit card profits in the current boom in banking.

[7]Even Mastercard recognizes this trend. In its recent report on debt and bankruptcy, its economist states: "Stagnation in real wages during the last 20 years and the growing disparity in income and wealth, ... have almost certainly contributed to the rise in personal bankruptcies. Declines in income caused by job loss make it that more difficult for those affected to service previously accumulated debt." Chimerine, "Americans in Debt: The Reality", p. 24 (MasterCard International 1997).

[8] Sullivan, Warren, and Westbrook, As We Forgive Our Debtors, pp. 91-102 (Oxford University Press, 1989). See Generally Medoff and Harless, The Indebted Society pp. 103-119 (Little Brown & Co. 1996) (in the last two decades real wages of the newly hired have fallen faster than those of longer tenured employees).

[9] More than two billion credit came solicitations were sent out in 1997. See Hays, "Banks Marketing Blitz Yields Rash of Defaults " Wall Street Journal, p. B1 (September 25, 1996). MBNA, one of the largest issuers, claims 30 million credit card solicitations each month in 1997 together with 6 million phone solicitations. Hansell, "A Banking Powerhouse of Cards ", N. Y Times, p. CI (October 22, 1997).

[10] See Chacon, "Debt Burden Soaring for U.S. Students " Boston Globe, p. 1 (October 23, 1997). According to the Nellie Mae study on which the article is based, an average student's debt increased from $8,200 in 1991 to $18,800 in 1997

[11] Family Finances in the United States: Recent Evidence from the Survey of Consumer Finances" Federal Reserve Bulletin, p. 1, 21 at Table 14 (January, 1997). Overall, the rate is one family in nine.

[12] See Sullivan, Warren, and Westbrook, As We Forgive Our Debtors, pp. 147-165 (Oxford University Press, 1989).

[13] See Hildebrandt and Thomas, "The Rising Cost of Medical Care and Its Effect on Inflation ", Federal Reserve Bank of Kansas City, Econ. Rev. p. 47 (Sept.1Oct. 1991).

[14] Doinowitz & Sartrain, Determinants of the Consumer Bankruptcy Decision, p. 25 (1997).

[15]See Dugas, "Special Report: Going Broke, Wage Garnishments a Key Factor" USA Today, p. 1A (June 10, 1997); Hansell, "We Like You. We Care About You. Now Pay Up. Debt Collecting Gets a Perky Face and Longer Arms ", NY Times, F. 1 (Jan. 26, 1997).

[16] Sterling & Shrag, Default Judgments Against Consumers: Has the System Failed?" 67 Denv. U.L.R. 357, 384 (1990).

[17] See, e.g., Adding Insult to Injury: Credit on the Fringe, Hearing before the Subcommittee on Consumer Credit and Insurance of the House Committee on Banking, 103rd Cong., 1st Sess. (1993). Rehm, In a First, FDIC Warns Banks About Dangers of Sub-Prime Lending, 162 Ain. Banker 2 (May 13, 1997).

[18]See Forrester, "Mortgaging the American Dream: A Critical Evaluation of the Federal Government's Promotion of Home Equity Financing " 69 Tul. L. Rev. 373 (1994).

[19]Three neutral academic studies show this remarkable correlation. Ausubel, Credit Card Defaults, Credit Card Profits and Bankruptcy, 71 Am. Bankr. L.J. 250 (1997); Bhandari & Weiss, The Increasing Bankruptcy Filing Rate: An Historical Analysis, 67Am. Bankr. L.J. 1 (1993); Statement of Kim Kowaleivski, Chief, Financial and General Macroeconomic Analysis Unit, Congressional Budget Office, before the Subcommittee on Administrative Oversight and the Courts, Committee on the Judiciary, United States Courts, (April 11, 1997). See Commission Report at pp. 84-86. These studies stand is sharp contrast to credit industry funded studies which purport to show othervise.

[20] Borrowers who maintain balances pay interest at rates which typically range from 14.5 to 19.8%.

[21] Minimum payments on many credit cards will not amortize the loan, thus sucking people in over their heads. If minimum payment terms are offered which won't amortize the debt in two years, consumers should be told, in clear and conspicuous language, what they need to pay, if they make no further charges, in order to pay off the loan over a two year period.

[22] Low initial rates are designed to encourage consumers to use credit in the first months after credit is granted. Many consumers do not understand what the permanent rate will be or the impact of the rate change on a large unpaid balance.

[23] Some lenders raise rates arbitrarily after consumer balances reach a certain level.. -Interest rate changes should be tied to an actual change in the interest rate environment so that consumers are not caught unawares.

[24] When a lender extends a consumer's credit limit unilaterally, in some cases after a consumer is already struggling with the existing balance, the message is that the lender believes that the consumer can afford to take on more credit. Consumers would not be hurt by having to ask for more credit, rather than having it offered unilaterally. Such a request should trigger at least minimal underwriting requirements.

[25] These hidden security interests in items of property which have no resale value to the creditor provide inappropriate leverage to lenders in the collection process even though there is no potential that the lender could make money in the event of repossession.

[26] Consumers receive checks from several major lenders in the mail for as much as $5,000. Not everyone understands that cashing these checks can lead to acceptance of high rate credit terms, In addition, providing preapproved credit through cashed checks eliminates the cooling off period which more common credit application processes provide.

[27] With credit card cash advance machines prevalent in casinos, is it surprising that some gamblers get overextended on credit and file bankruptcy based on those credit card debts?

[28] Offering credit aggressively to college students who cannot afford to pay off their debts until they join the workforce some years later is prevalent because interest mounts until the debt is paid. By lending aggressively to college students, at a time in life when money is scarce, our society runs the risk of saddling people early in life with an unmanageable problem which will later preclude more important uses of credit such as purchase of a home and car.

[29] Competition in the market has not worked to keep rates at reasonable levels. On a procedural level, the Supreme Court has held that credit card lenders can rely on the law in the state where they are incorporated in setting the interest rate and many of the other terms of credit for consumers nationwide. This has led to a "race to the bottom ". States deregulate in order to create the best possible environment to encourage a credit card company to locate there in order to export terms of credit across the country. This helps certain states create jobs. However, it means that those other states that do want to regulatefor the benefit of their citizens can no longer do so. Either states should be freed to create and enforce meaningful regulations or th e federal government should step in with consumerprotections.

[30] H.R. 1975, 105th Cong., Ist Sess. (1997) "Credit Card Consumer Protection Act of 1997". See also H.R. 3146, 105th Cong., 2d Sess. (February 3, 1998) "Consumers and Lenders Bankruptcy Accountability Act of 1997" for an

approach to addressing these problems by changes to the bankruptcy system.

[31] Deuteronomy 15:1-2 ("At the end of every seven years thou shalt make a release. And this is the manner of the release: every creditor shall release that which he has lent unto his neighbor and his brother, because the Lord's release hath been proclaimed".)

[32] Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934). See Gross, Failure and Forgiveness, ch. 6 (Yale University Press 1997).

[33] Sullivan, Warren and Westbrook, "Consumer Debtors Ten Years Later: A Financial Comparison of Consumer Bankrupts 1981-1991 ", 68 Am Bankr. L. J. p. 121, 128 (1994).

[34] Proposed legislation favored by the credit industry includes: S. 1301, 105th Cong., 1st Sess. 102 (1997); H.R. 2500, 105th Cong., Ist Sess. 101, 102 (1997); H.R. 3150, 105th Cong., 2d Sess. 101 (1998). Consumer groups including the National Consumer Law Center, the Consumer Federation of America, the National Association of Consumer Bankruptcy Attorneys and the United Auto Workers are opposed.

[35] See Report of the Commission on the Bankruptcy Laws of the United States, Part I at 159 (1973); H.R. Rep. No. 595, 95th Cong., 1st. Sess. 120-121 (1977); Report of the National Bankruptcy Review Commission, Vol. 1, at pp. 89-91 (October 20, 1997) [hereinafter "Commission Report"].

[36] Teresa A. Sullivan, Elizabeth Warren, and Jay Lawrence Westbrook, As We Forgive Our Debtors, pp. 205-206 (Oxford University Press, 1989). This seminal book and the empirical work which underlies it remains the single most authoritative published source for studying bankruptcy demographics. it has been updated more recently in an article by the same authors which concludes that debtors are now even poorer and less able to pay their debts than they were when the initial study was done. "Consumer Debtors Ten Years Later: A Financial Comparison of Consumer Bankrupts 1981-1991", 68 Am Bankr. L. J. 121 (1994).

[37] Barron and Staten, "Personal Bankruptcy: A Report on Petitioners' Ability to Pay ", Monograph 33, Georgetown U. Credit Research Center (19 7). is report is reprinte as Appen G-2. b to e National Bankruptcy Review Commission Report.

[38] GAO Draft Report at p. 8. The final report is due out on February 8, 1997 (requested by Senators Charles E. Grassley and Richard J. Durbin). The GAO concluded that the study's "fundamental assumptions were not validated". In addition, the GAO review concluded that the credit industry's study: failed to assess the accuracy of the data collected; failed to account for major expenses which bankruptcy debtors have afterfiling including payments on non-housing secured debt and reaffirmed or non-discharged non-priority debts; failed to evaluate potential differences among the sites chosen for the study; and failed to use statistically valid research techniques.

[39] Without allowing for the GAO's criticisms, the creditor's study concludes that debtors could pay 13.7% of their debts over five years. The GAO report points out that this conclusion must be modified because the creditors did not account for 1.) repayment plan failures (approximately 67% under current law), 2.) debts which must be paid back despite bankruptcy including car loans, student loans, reaffirmed debts and interest on those debts (payment obligations on these debts represent approximately 46 % of total debts and thereby reduce a family's ability to pay other debts) and administrative costs of payment plans (10 % of plan payments under current law). When these deductions from payment capacity are taken into account, what is left is the ability to pay about 5 % of total debts over a five year period.

[40] 67% of repayment plan cases fail under current law. There is evey reason to think that if economically marginal debtors are forced into involuntary repayment plans, the failure rate would be higher.

[41] See D. Caplovitz, Consumers In Trouble: A Story of Debtors in Default pp. 280-285 (Free Press, 1974).

[42] Medoff and Harless, The Indebted Society, at pp. 12-13 (Little, Brown & Co. 1996).

[43] Report of the National Bankruptcy Review Commission, Vol. 1, at p. ix (October 20, 1997) [Hereinafter "Commission Report"].

[44] Fed. R. Bankr. P. 9011.

[45] See 11 U.S.C 727.

[46] See II U.S. C. 523 (a).

[47] See, e.g., In re Barrett, 964 F. 2d 588 (6th Cir. 1992) (finding that debtor's second chapter 13 filing, when he had insufficient incoine to support plan, was in bad faith but that third chapter 13 case, after circumstances had changed was not in bad faith); In re Love, 95 7 F. 2d 1350 (7th Cir. 1992).

[48] Fed. R. Bankr. P. 2004. It is hard to see why creditors concerned about abuses can't utilize the examination process to uncover them. If it is not financially feasible for a creditor to pursue an examination, why should taxpayers instead bear that burden for the creditor's benefit.

[49] 11 U.S. C. 341. Fed. R. Bankr. P. 2003.

[50] 11 U. S. C 707(b).

[51] 18 U.S. C. 151-157. Bankruptcy fraud is punishable by fine and imprisonment for up to five years. 18 U.S. C 15 7.

[52] That is the provision which Congress added to the Code in 1984 and which has functioned to root out debtors who can afford to pay their creditors. See, eg., In re Kelly, 841 B. R. 908 (9th Cir. 1988); In re Krohn, 886 F. 3rd 123 (6th Cir. 1989) (substantial abuse found where debtors could pay back their debts with "good, old-fashioned belt tightening ").

[53] See, e.g., H.R.3146, 105th Cong., 2d Sess. 8 (February 3, 1998). Creditors should not be allowed to obtain leverage by forcing new litigation on consumers who cannot afford to pay.

[54] For example, efforts should be made to provide improved credit reporting for people who complete chapter 13 payment plans. In addition, the discharge available in chapter 13 should be as broad as possible in order to serve as incentive to choose that chapter. Costs can be lowered by encouraging secured lenders to accept modifications to their mortgages in exchange for more favorable treatment.