

THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT

The number of personal bankruptcies has nearly doubled in the past ten years: it rose from roughly 700,000 in 1990 to more than 1.2 million in 2000, passing through a peak of nearly 1.4 million in 1998.¹ Despite the prosperity of the 1990s, roughly one percent of American households declared bankruptcy each year.² In response to these figures, and to aggressive lobbying by banks and consumer lenders,³ broad bipartisan majorities in both the House and Senate passed the Bankruptcy Abuse Prevention and Consumer Protection Act (“Bankruptcy Reform Act”) early in the 107th Congress.⁴ President Bush has indicated he will sign the bill,⁵ which is virtually identical to legislation that President Clinton killed by pocket-veto in the 106th Congress.⁶

Proponents describe the Bankruptcy Reform Act as an effort to restore an ethic of personal responsibility among borrowers by forcing them to repay what debts they can.⁷ At a time of impending recession, they argue, the bill will deter reckless borrowing, generating savings for lenders that will be passed on to consumers in the form of lower interest rates.⁸ As prominent academics, congressional Democrats, and consumer

¹ See American Bankruptcy Institute, *U.S. Bankruptcy Filings 1980–2000 (Business, Non-Business, Total)*, available at <http://www.abiworld.org/stats/1980annual.html> (last visited Oct. 26, 2001).

² See Michelle J. White, *Why Don't More Households File for Bankruptcy?*, 14 J.L. ECON. & ORG. 205 (1998).

³ See 145 CONG. REC. S14,067 (daily ed. Nov. 5, 1999) (statement of Sen. Feingold (D-Wis.) (indicating that “[a] very wealthy and powerful industry has pushed and pushed for this bill,” and that “the members of the National Consumer Bankruptcy Coalition, an industry lobbying group made up of the major credit card companies such as Visa and MasterCard and associations representing the Nation’s big banks and retailers, gave nearly \$4.5 million in contributions to parties and candidates” during the 1998 election cycle); see also Kathleen Day, *House Passes Bankruptcy Limits: Measure Would Make it Harder for Consumers to Wipe Out All Debts*, WASH. POST, Mar. 2, 2001, at A1 (“Contributions to federal candidates and the political parties from finance and credit card companies during the 2000 campaign totaled \$9.2 million Commercial banks’ political contributions [totaled] \$28.5 million.”).

⁴ H.R. 333, 107th Cong. (2001); S. 420, 107th Cong. (2001). The House Bill passed on March 1, 2001 by a margin of 306 to 108, receiving 93 Democratic votes in favor and no Republican “nay” votes. See CONG. REC. H600–01 (daily ed. Mar. 2, 2001). The Senate then passed the bill with minor amendments on July 17, 2001 by a margin of eighty-two to sixteen. See 147 CONG. REC. S7742 (daily ed. July 18, 2001).

⁵ See Day, *supra* note 3, at A1.

⁶ See HOUSE COMM. ON THE JUDICIARY, BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2001, H.R. REP. NO. 107-3, at 3 (2001) [hereinafter HOUSE JUDICIARY COMMITTEE REPORT].

⁷ See, e.g., *id.* at 2 (“The purpose of the bill is to improve bankruptcy law and practice by restoring personal responsibility and integrity in the bankruptcy system”); 147 CONG. REC. H518 (daily ed. Mar. 1, 2001) (statement of Rep. Armev (R-Tex.), House Majority Leader) (“This bill is about the character of a Nation and [whether] the Nation’s laws have a character of the Nation’s people.”).

⁸ See, e.g., 147 CONG. REC. S1807 (daily ed. Mar. 5, 2001) (statement of Sen. Grassley (R-Iowa)) (“With the possibility of the economy slowing right now, we need to at this time

advocates have noted, however, the bill carries a strong pro-creditor bias that threatens to undermine its purported objectives.⁹ Since the bill does little to curb the lending practices that have made possible Americans' extraordinary debts, there is reason to believe it will succeed neither in reducing bankruptcies nor lowering interest rates.¹⁰

The main thrust of the reform bill is to provide less generous options to debtors who file for bankruptcy. Under current law, debtors may choose between two personal bankruptcy options: asset liquidation under Chapter Seven¹¹ of the bankruptcy portion of the United States Code, and debt readjustment under Chapter Thirteen.¹² Any debtor may seek the protection of either chapter, regardless of whether the debtor is insolvent.¹³ Chapter Seven permits the filer to discharge all debts, with certain exceptions such as mortgages, student loans, fraudulently incurred debts, and some child support and alimony obligations.¹⁴ In return for the discharge, however, the debtor must accept the liquidation of all assets, excepting certain exempt property such as the debtor's homestead.¹⁵ By

fix a bankruptcy system that inflates interest rates and threatens to make the slowdown even worse.").

⁹ See Kathleen Day, *Foes of Bankruptcy Bill Point Finger at Credit Card Issuers*, WASH. POST, Feb. 28, 2001, at E1; see also HOUSE COMM. ON THE JUDICIARY, BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2001: DISSIDENTING VIEWS, H.R. REP. NO. 107-3, at 455 (2001) [hereinafter JUDICIARY COMMITTEE DISSIDENTING VIEWS] ("We oppose the bill because it is likely to harm low income consumers, women and children reliant on alimony and child support, and employees of troubled businesses, among other vulnerable groups."); 147 CONG. REC. H518 (daily ed. Mar. 1, 2001) (statement of Rep. Conyers (D-Mich.), Ranking Member, House Judiciary Comm.) (calling House Bill 333 "a bill that massively tilts the playing field in favor of creditors and against the interests of ordinary consumers and workers.").

¹⁰ See, e.g., JUDICIARY COMMITTEE DISSIDENTING VIEWS, *supra* note 9, at 478 (criticizing the Bankruptcy Reform Act for "ignor[ing] the transgressions of the credit industry," and noting that "the overwhelming weight of authority establishes that it is the massive increase in consumer debt . . . which has brought about the increases in consumer filings."); *infra* text accompanying notes 57-88.

¹¹ 11 U.S.C. §§ 701-766 (1994 & Supp. V 1999).

¹² *Id.* §§ 1301-1330.

¹³ See *id.* § 707(b) (stating that a court may deny access to Chapter Seven only if it finds that "the granting of relief would be a substantial abuse of the provisions of this chapter."). Commentators have disputed the extent to which this provision protects creditors from bankruptcies by debtors who could afford to pay their debts. Compare SENATE JUDICIARY COMMITTEE, BANKRUPTCY REFORM ACT OF 1999, S. REP. NO. 106-49, at 6 (1999) (indicating that, since the statute provided no definition of "substantial abuse," courts have generally held excess income is only one factor to be considered) with Carl Felsenfeld, *Denial of Discharge for Substantial Abuse: Refining—Not Changing—Bankruptcy Law*, 67 FORDHAM L. REV. 1369 (1999) (noting a split in Circuits between two tests for "substantial abuse," the "excess income" test and the "totality of the circumstances" test, but arguing that in practice "courts routinely apply only an excess income test"). A finding of "substantial abuse" is possible only upon motion of the court or of the United States Trustee, a Department of Justice official who manages the liquidation of the debtor's assets; creditors and interested parties may not request such a finding. See 11 U.S.C. at § 707(b) (Supp. V 1999).

¹⁴ See 11 U.S.C. §§ 523, 727 (1994 & Supp. V 1999).

¹⁵ See *id.* § 522. The debtor may choose between exemptions provided by federal or state law. See *id.* § 522(b). This exemption system is controversial. See *infra* note 46.

contrast, debtors who file under Chapter Thirteen may retain most assets, but must develop a plan to commit their disposable income to repayment of debts over a three to five year period,¹⁶ at the end of which the court discharges any remaining debt.¹⁷

The Bankruptcy Reform Act would abolish the debtor's voluntary choice of chapter, replacing it with a means test designed "to ensure that debtors repay creditors the maximum they can afford."¹⁸ The bill would require all bankruptcy filers to complete the test, though in general only those with a family income above the state median would be denied access to Chapter Seven.¹⁹ Under the bill's test, the debtor's monthly income (defined as the monthly average of all income received during the previous six months)²⁰ multiplied by 60 (the number of months in five years, the length of a typical Chapter Thirteen repayment plan under the bill)²¹ is compared to the sum of the following five figures: (1) total "priority" debts, such as family support obligations; (2) scheduled payments on secured debts over the next five years; (3) arrears on secured debts; (4) monthly living expenses calculated on the basis of Internal Revenue Service guidelines, multiplied by 60; and (5) an allowance for the administrative costs of a Chapter Thirteen plan.²² If the debtor's income exceeds this sum by either (1) an amount equal to twenty-five percent of remaining unsecured debts (unless the debtor could pay no more than \$100 a month toward these debts) or (2) \$10,000, whichever is lower, then the debtor faces a presumption of abuse which he or she may rebut only by establishing that, due to "special circumstances," there is "no reasonable alternative" to an adjustment in the debtor's income or expenditure.²³

While the means test is the Bankruptcy Reform Act's centerpiece,²⁴ it is not the only new restriction the bill would impose on bankruptcy filing. The bill would also, for one, require debtors to obtain "credit

¹⁶ See 11 U.S.C. § 1322 (1994).

¹⁷ See *id.* § 1328 (1994 & Supp. V 1999).

¹⁸ HOUSE JUDICIARY COMMITTEE REPORT, *supra* note 6, at 2.

¹⁹ See H.R. 333, § 102(a).

²⁰ See H.R. 333, § 102(b). The calculation of monthly income excludes Social Security benefits and reparation payments for victims of war crimes and crimes against humanity; however, it includes all other sources of income whether or not they are taxable. See *id.*

²¹ See 511 U.S.C. § 1322 (1994). Whereas three years is the length of the typical Chapter Thirteen plan under current law, the Bankruptcy Reform Act would make five years the norm in an increased number of cases. See H.R. 333, § 318.

²² See H.R. 333, § 102(a).

²³ See *id.* Chapter Seven access would be presumptively denied to a debtor with above-average income who could pay all scheduled payments and arrears on priority obligations plus at least \$6,001 (more than \$100 per month over five years) towards a \$24,000 credit card debt (four times the minimum payable amount). Chapter Seven would also be unavailable to a debtor who could pay all priority obligations plus \$10,000 of a \$10,001 credit card debt.

²⁴ See HOUSE JUDICIARY COMMITTEE REPORT, *supra* note 6, at 2 (calling the means test the bill's "heart").

counseling” before filing.²⁵ Under this provision, debtors could receive bankruptcy relief only upon completion of “an instructional course concerning personal financial management” given by an approved non-profit counseling agency.²⁶ For another, the bill would toughen the presumptions against discharge of debt obtained shortly before filing. Current law permits creditors to challenge the discharge of any debt of \$1,150 or more for “luxury goods and services” that the debtor obtained from a single creditor within sixty days of filing.²⁷ The Bankruptcy Reform Act would reduce the amount for such presumptively non-dischargeable debts to \$250, while increasing the relevant time-span from sixty to ninety days before bankruptcy.²⁸ Similarly, whereas current law prevents the discharge of debts from cash advances amounting to more than \$1,150 if they are incurred within sixty days of filing,²⁹ the Bankruptcy Reform Act would lower that minimum amount to \$750, while also shortening the relevant time-period to seventy days.³⁰ In addition, the bill would restrict debtors’ rights to stay debt payment by declaring bankruptcy.³¹ There is evidence that some debtors make strategic use of the automatic stay afforded to filers under current law;³² some debtors apparently file successive Chapter Thirteen motions with no intention of completing a plan and obtaining a discharge.³³ The Bankruptcy Reform Act would curtail such “abusive serial filing” by requiring a showing of good faith before granting a stay of more than thirty days to debtors who had filed and had their case dismissed within the previous year.³⁴

Because such changes to the mechanics of bankruptcy under the Bankruptcy Reform Act could alter the relative advantages for competing creditor groups, the bill would adjust the treatment of certain types of debts in bankruptcy. Under current law, Chapter Seven filings are generally more advantageous for creditors holding secured debt. Chapter

²⁵ H.R. 333, § 106. For critical analysis of the view that a credit counseling requirement would benefit debtors, see Howard B. Hoffman, *Consumer Bankruptcy Filers and Pre-Petition Consumer Credit Counseling: Is Congress Trying to Place the Fox in Charge of the Henhouse?*, 54 BUS. LAW. 1629, 1632 (1999) (indicating that, because existing credit counseling agencies are funded by “voluntary contributions” from creditors, such agencies may encourage debtors to undertake burdensome repayment budgets).

²⁶ H.R. 333, § 106(b)(3) (adding the counseling requirement to Chapter Seven); *id.* § 106(c) (adding the requirement to Chapter Thirteen).

²⁷ 11 U.S.C. § 523(a)(2)(C) (LEXIS through 2001 legislation).

²⁸ See H.R. 333, § 310.

²⁹ See 11 U.S.C. § 523(a)(2)(C) (LEXIS through 2001 legislation).

³⁰ See H.R. 333, § 310.

³¹ *Id.* § 302.

³² See 11 U.S.C. § 362 (1994 & Supp. V 1999).

³³ See Elizabeth Warren, *A Principled Approach to Consumer Bankruptcy*, 71 AM. BANKR. L.J. 483, 502–03 (1997).

³⁴ H.R. 333, § 302. Debtors who file more than twice within a year would have to show good faith by clear and convincing evidence. See *id.* See generally Scott F. Norberg, *Consumer Bankruptcy’s New Clothes: An Empirical Study of Discharge and Debt Collection in Chapter 13*, 7 AM. BANKR. INST. L. REV. 415, 427 (1999) (describing the abusive serial filing provisions).

Seven debtors often agree to reaffirm secured debts so as to keep the underlying collateral, such as an automobile or appliance being purchased in installments. Many even accept agreements that require them to pay an outstanding balance that exceeds the value of the collateral property.³⁵ Meanwhile, unsecured lenders, such as credit card issuers, tend to lose out when assets are liquidated under Chapter Seven because unsecured debt is generally a low priority for repayment.³⁶

By contrast, Chapter Thirteen is more advantageous to unsecured lenders. As an incentive for debtors to file under Chapter Thirteen rather than Seven, secured debts on assets other than the debtor's home may be "stripped down" from the amount of the outstanding balance to the replacement value of the property.³⁷ Thus, whereas secured creditors may often obtain reaffirmation of the full value of their lien against a Chapter Seven debtor, the value of secured debts may be substantially reduced if the debtor files under Chapter Thirteen. Meanwhile, both secured and unsecured debt are included in the repayment plan, so unsecured lenders may receive repayment of debts that would have been discharged under Chapter Seven.³⁸

³⁵ See Warren, *supra* note 33, at 499 (noting that "more than forty percent of the debtors have been willing to sign on [to reaffirmation agreements]" even though those agreements typically require them to repay not only the secured portion of the debt, but also the unsecured portion, that is, the portion in excess of the value of the collateral). Reaffirmation agreements are permitted by 11 U.S.C. § 524(c) (1994 & Supp. V 1999). In an empirical study, Marianne Culhane and Michaela White found that twenty-eight percent of Chapter Seven debtors had "one or more reaffirmation agreements in the court file." Marianne B. Culhane & Michaela M. White, *Debt after Discharge: An Empirical Study of Reaffirmation*, 73 AM. BANKR. L.J. 709, 720 (1999). These figures might understate the level of reaffirmation, since there is evidence that many creditors obtained illegal "rogue reaffirmations" requiring debtors to repay loans without reporting the agreement to the court. *Id.* at 717-18. Many debtors in their sample also appeared to have retained assets through "ride-through" arrangements that permitted them to continue payments on items purchased on credit with the creditor retaining a right to repossess the item. *Id.* at 713. Culhane and White conclude that many Chapter Seven filers reaffirmed more debt than they could afford to pay; moreover, many reaffirmed debts on household items that were "unsecured for all practical purposes" since "the collateral was unlikely to be repossessed." *Id.* at 764.

³⁶ See 11 U.S.C. §§ 507, 726 (1994 & Supp. V 1999). Unsecured lenders have sometimes succeeded in obtaining reaffirmations of debt in return for promises of credit following bankruptcy. See Culhane and White, *supra* note 35, at 730; see also Scott F. Norberg, *supra* note 34, at 421 ("While unsecured creditors rarely realize any payment through liquidation of unencumbered, non-exempt property, they routinely receive at least some repayment through reaffirmations and non-dischargeability determinations.").

³⁷ See 11 U.S.C. § 1322(b)(2) (1994) (permitting the court to "modify the rights of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence"). Courts have interpreted this provision in conjunction with § 506(a), which provides that debt in excess of the value of the collateral may be treated as unsecured debt if another provision of the code permits modification of the lien. See, e.g., *In re Byington*, 197 B.R. 130, 133 (Bankr. D. Kan. 1996); see also Corinne Ball & Jacqueline B. Stuart, *The Battle Over Bankruptcy Law for the New Millennium*, 55 BUS. LAW. 1487, 1496-97 (2000).

³⁸ See generally Norberg, *supra* note 34, at 424-26.

Forcing debtors to file under Chapter Thirteen could disadvantage secured creditors if it eliminated reaffirmation opportunities that would have arisen under Chapter Seven. The Bankruptcy Reform Act compensates for this effect by restricting the debtor's opportunity to strip down undersecured debts in Chapter Thirteen. For automobile purchase loans made within five years of bankruptcy or for other personal property purchased within one year, debtors would no longer be permitted to bifurcate the replacement value from the remaining unsecured portion of the loan; the bill would instead require debtors to include the full value of such creditor liens in their repayment plan.³⁹ Further, the bill would require reaffirmation agreements to include extensive information about the debtor's rights,⁴⁰ and would instruct United States Attorneys and the Federal Bureau of Investigation to take responsibility for enforcing laws against abusive reaffirmation practices.⁴¹

Finally, the Bankruptcy Reform Act would amend the Truth-in-Lending Act ("TILA")⁴² to require new disclosures from creditors. In particular, it would require credit card billing statements to disclose information on the amount of time required to pay off a hypothetical balance by making minimum monthly payments.⁴³ Card issuers would be required to provide a toll-free telephone number from which card-holders could obtain information on the amount of time required to pay off their own account balance with minimum payments.⁴⁴ Additionally, credit card solicitations and applications would be required to include information "clearly and conspicuously" on the mechanics and duration of introductory "teaser" interest rates.⁴⁵

In sum, the Bankruptcy Reform Act would restrict access to Chapter Seven, limit the debt discharge, impose new burdens on bankruptcy filers, and eliminate strip-down, while offering consumers the benefit of additional disclosures from consumer creditors.⁴⁶ With the exception of the

³⁹ See H.R. 333, § 306. House Bill 333, section 304 also bars debtors and creditors from agreeing to let secured claims "ride-through" bankruptcy, as they may under current law. See Culhane & White, *supra* note 35, at 718–20 (describing "ride-through" options under current law).

⁴⁰ See H.R. 333, § 203(a).

⁴¹ See *id.* § 203(b); See also Culhane & White, *supra* note 35, at 717–18 (describing abusive reaffirmation practices by creditors).

⁴² 15 U.S.C. § 1637 (1994).

⁴³ See H.R. 333, § 1301(a). Credit card lending arrangements often involve "negative amortization"; that is to say, credit card lenders often set minimum monthly payments below interest charges, with the result that a debtor's total outstanding debt may increase while the debtor makes the minimum payments. TERESA A. SULLIVAN, ELIZABETH WARREN, & JAY LAWRENCE WESTBROOK, *THE FRAGILE MIDDLE CLASS: AMERICANS IN DEBT* 247–48 (2000).

⁴⁴ See H.R. 333, § 1301(a).

⁴⁵ *Id.* § 1303.

⁴⁶ The Bankruptcy Reform Act is a complex and detailed piece of legislation. This Essay discusses only the most significant and controversial changes the bill would make to current bankruptcy law. See generally Ball & Stuart, *supra* note 37. One controversial fea-

TILA amendments, all of these changes “move in the same direction”: they strengthen the position of creditors while weakening that of debtors.⁴⁷

The rationale for this package of reforms is twofold. First, proponents of the bill attribute the explosive increase in bankruptcy filing to abuse of current law by unscrupulous debtors.⁴⁸ Easy access to Chapter Seven, the argument goes, has eroded the “stigma” traditionally associated with bankruptcy, leading to the use of the bankruptcy system as a tool of financial planning, rather than as a last resort.⁴⁹ Bankruptcy laws, it follows, must be toughened to curb this practice.⁵⁰ Second, proponents argue that reform will have beneficial effects for responsible borrowers

ture of current law that the bill may *not* change significantly bears mention. Under current law, debtors may exempt assets from the bankruptcy estate according to either federal or state law. *See* 11 U.S.C. § 522 (1994 & Supp. V 1999). Some wealthy debtors have used this feature of bankruptcy law strategically, changing their state of residence before bankruptcy so as to gain a more generous exemption. *See* G. Marcus Cole, *The Federalist Cost of Bankruptcy Exemption Reform*, 74 AM. BANKR. L.J. 227, 229 (2000) (referring to “‘high profile’ cases in which wealthy individuals move to states with generous exemption regimes in order to obtain a discharge while shielding vast portions of their assets from creditors.”). For instance, a debtor who moves from New Jersey, which provides no state-law homestead exemption, to Florida, which provides an unlimited homestead exemption, may shield substantial assets from creditors by purchasing an expensive home. *See* Ball & Stuart, *supra* note 37, at 1499–1500. Critics argue that this opportunity for pre-bankruptcy planning by the wealthy undermines public confidence in the fairness and legitimacy of the system. *See, e.g.*, Elizabeth Warren, *supra* note 33, at 493–94. While the Senate version of the Bankruptcy Reform Act would impose a cap of \$125,000 on homestead exemptions, *see* Senate Bill 420 § 308, the House bill would make no such change, and President Bush has indicated that he opposes the Senate language. *See Senate Votes to Invoke Cloture on Motion to Proceed to Bankruptcy*, CONG. DAILY, July 12, 2001, available at 2001 WL 24848595.

⁴⁷ *Bankruptcy Reform: Joint Hearing Before the Subcomm. on Commercial and Administrative Law of the House Comm. on the Judiciary and the Subcomm. on Administrative Oversight and the Courts of the Senate Comm. on the Judiciary*, 106th Cong. 103 (1999) [hereinafter *Bankruptcy Reform Hearing*] (statement of Elizabeth Warren, Professor, Harvard Law School).

⁴⁸ *See, e.g., id.* (statement of Todd Zywicki, Professor, George Mason University School of Law) (“Bankruptcy is a moral as well as an economic act. There is a conscious decision not to keep one’s promises. It is a decision not to reciprocate a benefit received, a good deed done on the promise that you will reciprocate. Promise-keeping and reciprocity are the foundation of an economy and healthy civil society.”), *quoted in* HOUSE JUDICIARY COMMITTEE REPORT, *supra* note 6, at 6.

⁴⁹ S. REP. NO. 106-49, at 2–3 (“A decreased moral stigma associated with bankruptcy means that filing for bankruptcy is not viewed as a last resort for financially troubled Americans who need debt forgiveness Individuals who would have struggled to meet their financial obligations in the past are filing bankruptcy today in record numbers.”) (footnotes omitted); *see also* 146 CONG. REC. S50 (daily ed. Jan. 26, 2000) (statement of Sen. Hatch (R-Utah)) (“Not long ago in our Nation’s past, there was an expectation that people should repay what they have borrowed. Hand in hand with this expectation was a stigma that attached to those who filed bankruptcy Our current system, I am sorry to say, allows some people who are able to repay their debts to avoid doing so.”). *See generally supra* note 7.

⁵⁰ *See, e.g.*, Press Release, Sen. Chuck Grassley, Memorandum Re: S. 420, The Bankruptcy Reform Bill (Mar. 14 2001) (“There’s plenty of blame to go around for the 100 percent increase in the number of bankruptcy filings in the last ten years. Part of the problem is bankruptcy laws that are too lax.”), at <http://www.senate.gov/~grassley/releases/2001/p01r3-14d.htm>.

who pay back their loans. Under current law, responsible borrowers pay high interest rates to subsidize losses from the discharged debt of their less responsible peers.⁵¹ A reform that limits access to debt discharge should lower interest rates, reformers argue, since it would prevent reckless borrowers from shifting the costs of their activity onto other borrowers.⁵² Lower interest rates, in turn, would benefit the economy by facilitating responsible spending and investment.⁵³

Opponents of the Bankruptcy Reform Act contest both rationales given in support of the reform bill. They argue, first, that lenders, not borrowers, are to blame for bankruptcy increases, since their lending practices have fostered the indebtedness that places households at risk of bankruptcy.⁵⁴ Opponents also question whether bankruptcy reform will lower interest rates for responsible borrowers.⁵⁵ They suggest, rather, that commercial lenders will be the principal beneficiaries of the bill, since it will afford them increased opportunities for debt collection.⁵⁶

The first ground for disagreement relates to the causes of bankruptcy. On that count, one fact is clear: Americans have taken on unmanageable levels of debt in recent years. Indeed, the data on this point are overwhelming: total household debt in the United States increased from sixty-five percent of total income to eighty-one percent between 1980 and 1994.⁵⁷ During roughly the same period, households increased their total home mortgage and consumer installment debts by more than 400

⁵¹ See, e.g., HOUSE JUDICIARY COMMITTEE REPORT, *supra* note 6, at 5 (indicating that “financial losses attributable to bankruptcy filings in 1997 exceeded \$44 billion”); 147 CONG. REC. H134 (daily ed. Jan. 31, 2001) (statement of Rep. Gekas (R-Pa.)) (indicating the \$44 billion in losses from bankruptcy “equal[s] more than \$400 per household”); 147 CONG. REC. S1811 (daily ed. Mar. 5, 2001) (statement of Sen. Sessions (R-Ala.)) (“When somebody fails to pay what they owe, . . . what happens? It drives up the cost of . . . people’s business. They have to raise the charges on the honest people who pay them.”).

⁵² See, e.g., 147 CONG. REC. S1807 (daily ed. Mar. 5, 2001) (Statement of Sen. Grassley (R-Iowa)) (“The result of the bankruptcy crisis is that hard-working, law-abiding Americans have to pay higher prices for goods and services. [The Bankruptcy Reform Act] makes it harder for individuals who can repay their debts to file for bankruptcy under chapter 7 where their debts are wiped away. This would lessen the upward pressure on interest rates and higher prices.”).

⁵³ See, e.g., *id.* (“Bankruptcy reform will help our economy through lower interest rates.”)

⁵⁴ See, e.g., 147 CONG. REC. S2028 (daily ed. Mar. 8, 2001) (statement of Sen. Durbin (D-Ill.)) (“[Proponents of the Bankruptcy Reform Act] argued that the people who were filing for bankruptcy had forgotten the moral stigma of declaring bankruptcy in America Shouldn’t the moral stigma be on the conscience of these lenders who have dragged these poor unsuspecting people into a situation where they have no hope and nowhere else to turn?”).

⁵⁵ See, e.g., JUDICIARY COMMITTEE DISSENTING VIEWS, *supra* note 9, at 458 (“[W]e have never received any evidence that the credit card industry likely would pass on any of the ‘savings’ from bankruptcy law changes to individual consumers.”).

⁵⁶ See, e.g., *id.* at 460 (“[The Bankruptcy Reform Act] would institute a number of major changes to consumer bankruptcy . . . that are designed to increase pay-outs to non-priority unsecured creditors, particularly credit card companies, as well as certain secured lenders, especially those extending credit for automobile loans.”).

⁵⁷ SULLIVAN ET AL., *supra* note 43, at 18

percent.⁵⁸ Thus, “real consumer debt has risen dramatically over a long period during which real incomes for many people have stayed the same or declined.”⁵⁹ In addition, according to one survey, bankruptcy filers in 1997 had an average debt-to-income ratio of 2.76, with the average burden of non-mortgage debt totaling 1.87 times annual income.⁶⁰ During 2000, the American savings rate was negative for the first time since the Great Depression.⁶¹

The explanation for these trends is not obvious, however. On the one hand, some research supports the reformers’ claim that a shift in borrowers’ attitudes is to blame. For instance, one recent study concludes that “the explosion in bankruptcy filings is in substantial part attributable to a shift in social norms,” not legal and economic variables.⁶² In the authors’ view the most plausible explanation for increasing debt is “a decline in social sanctions”—that is, in stigma associated with bankruptcy.⁶³ Media reports of debtors filing for bankruptcy without compunction also suggest that social attitudes toward bankruptcy have changed.⁶⁴ Moreover, other research shows that increases in the rate of bankruptcy filing have correlated strongly with increased expenditures on legal advertising following a 1977 Supreme Court decision⁶⁵ that struck down restrictions on such advertising on free speech grounds.⁶⁶ While “it is difficult to establish a causal relationship,”⁶⁷ lawyer advertisements for bankruptcy services may have contributed to a decline in social stigma by presenting bankruptcy filing in a more positive light.⁶⁸

On the other hand, declining stigma does not appear to be a complete explanation. Some research indicates that about fifteen times as many American households could benefit from bankruptcy as actually file.⁶⁹ Socio-cultural deterrents may afford at least a partial explanation

⁵⁸ *Id.*

⁵⁹ *Id.*

⁶⁰ *Id.* at 70–71 tbl.2.5.

⁶¹ See Dolores Kong, *Many Seen at Risk in a Downturn: Personal Debt Soars While Savings Plunge*, BOSTON GLOBE, Mar. 20, 2001, at A1.

⁶² F.H. Buckley & Margaret F. Brinig, *The Bankruptcy Puzzle*, 27 J. LEGAL STUD. 187, 188 (1998).

⁶³ *Id.* at 206.

⁶⁴ See, e.g., Kim Clark, *Why So Many Americans Are Going Bankrupt?*, FORTUNE, Aug. 4, 1997, at 24; see also Judge Edith H. Jones & Todd J. Zywicki, *It’s Time for Means-Testing*, 1999 BYU L. REV. 177, 215–21 (1999) (quoting in part Clark, *supra*, at 24–25). But see SULLIVAN ET AL., *supra* note 43, at 32 (“Arguments that the stigma attached to bankruptcy has declined are typically made by journalists who are unable to find any bankruptcy debtors willing to be interviewed for the record and by prosperous economists who see bankruptcy as a great bargain.”) (footnote omitted).

⁶⁵ *Bates v. State Bar of Arizona*, 433 U.S. 350 (1977).

⁶⁶ See Diane Ellis, *The Influence of Legal Factors on Personal Bankruptcy Filings*, BANK TRENDS 98–103 (FDIC, Division of Insurance), Feb. 1998, available at <http://www.fdic.gov/bank/analytical/bank>.

⁶⁷ *Id.* at 9.

⁶⁸ See *id.* at 2.

⁶⁹ See White, *supra* note 2, at 205.

for this anomaly.⁷⁰ Indeed, some commentators doubt whether the stigma of bankruptcy has declined significantly.⁷¹ Furthermore, changes in the culture and regulation of consumer lending appear to have played some role in bankruptcy increases. Bankruptcy levels have closely tracked overall levels of consumer debt,⁷² which have risen rapidly with the burgeoning of the consumer credit industry beginning in 1978.⁷³ In that year, the Supreme Court made possible the modern credit card industry by permitting lenders to charge the highest interest rate available in any state to credit card borrowers throughout the country.⁷⁴ Credit was once all but unavailable for consumers who were too risky for loans within the regulated interest rate of their state.⁷⁵ Today, however, lenders bombard consumers across the United States with some three billion credit card solicitations annually—forty-one per household—spending roughly \$100 in solicitation costs for each new card-holder.⁷⁶ Unlike traditional lenders, credit card companies do not base lending decisions on a careful analysis of the borrower's creditworthiness; rather, they extend credit on an "actuarial basis," targeting entire demographic groups and charging interest rates as high as twenty-four percent to cover the risk that some borrowers

⁷⁰ Cf. SULLIVAN ET AL., *supra* note 43, at 32 ("Discharging debts that were honestly incurred seems the antithesis of middle-class morality. Public identification as a bankrupt debtor is embarrassing at best, devastating at worst. Bankrupt debtors have told us of their efforts to conceal their bankruptcy."). *But see* White, *supra* note 2, at 229 (postulating that debtors do not file "because they obtain the benefits of bankruptcy without bearing the costs of filings, since creditors do not attempt to collect.").

⁷¹ See, e.g., SULLIVAN ET AL., *supra* note 43, at 32.

⁷² See JUDICIARY COMMITTEE DISSENTING VIEWS, *supra* note 9, at 478 (noting that "there is an almost perfect correlation between the increasing amount of consumer debt and the number of consumer bankruptcy filings"); see also SULLIVAN ET AL., *supra* note 43, at 129 ("Bankruptcy filing rates and consumer debt to income ratios rise and fall together over time."); Paul C. Bishop, *A Time Series Model of the U.S. Personal Bankruptcy Rate*, BANK TRENDS 98–101, (FDIC, Division of Insurance), Feb. 1998 (estimating the influence of consumer indebtedness and business cycle activity on the bankruptcy rate and concluding that "approximately two-thirds of the increase in bankruptcies can be explained by these two factors alone"), available at http://www.fdic.gov/bank/analytical/bank/bt_9801.pdf (last visited Jan. 1, 2002).

⁷³ See JUDICIARY COMMITTEE DISSENTING VIEWS, *supra* note 8, at 478 (chart shows rapid increase in consumer debt levels from the 1970s to the present).

⁷⁴ *Marquette Nat. Bank of Minneapolis v. First Omaha Serv. Corp.*, 439 U.S. 299 (1978) (holding that usury laws regulating interstate lending are a policy matter for Congress to decide). See generally Dianne Ellis, *The Effect of Consumer Interest Rate Deregulation on Credit Card Volumes, Charge-Offs, and the Personal Bankruptcy Rate*, BANK TRENDS 98–105 (FDIC, Division of Insurance), Mar. 1998 (arguing that *Marquette* "fundamentally altered the market for credit card loans in a way that significantly expanded the availability of credit and increased the average risk profile of borrowers," leading to "a substantial expansion in credit card availability, a reduction in average credit quality, and a secular increase in personal bankruptcies."), available at http://www.fdic.gov/bank/analytical/bank/bt_9805.html (last visited Jan. 1, 2002).

⁷⁵ See Ellis, *supra* note 74, at 4 ("[I]n a regime of restrictive usury ceilings, where lenders' income potential was limited, lenders extended credit only to higher-quality borrowers, and poorer quality borrowers were shut out of the market.").

⁷⁶ See SULLIVAN ET AL., *supra* note 43, at 135.

in the group will be unable to pay.⁷⁷ Thus, credit is widely and easily available to consumers, regardless of creditworthiness. What is more, consumers may incur debts incrementally by charging purchases to their card without ever having to apply deliberately for a loan.⁷⁸ The result is that consumers have taken on more debt than ever before, with personal bankruptcy rates rising proportionally.⁷⁹ Aggressive efforts by lenders to extend credit card usage to new demographic groups, including low-income borrowers in the “subprime” market,⁸⁰ suggest that the rise in consumer indebtedness will be an ongoing trend.⁸¹

In addition to the increasing availability of credit, structural economic changes may be inducing households to take on more debt and increase their risk of bankruptcy. Increasing income inequality has produced a situation in which more families must borrow in order to maintain a “middle-class” lifestyle.⁸² The ill effects of this trend are compounded by the fact that rising divorce rates and decreasing job security have increased the risk that families will undergo financial shocks that cause them to fall behind in debt payments.⁸³ Meanwhile, the combination of consumer advertising pressures with a deeply ingrained culture of “rising expectations”—the presumption that household welfare will improve as careers advance—makes it difficult for many Americans to save funds. Their lack of savings, in turn, leaves Americans ill-prepared for future calamities, let alone the belt-tightening that may be required in the case of more mundane problems such as diminished salary, layoff, temporary unemployment, or divorce.⁸⁴ Thus, the consumer credit industry has come to function as a form of private wage insurance which provides emergency funds to households in distress.⁸⁵ In this capacity, the industry finances the losses of families who go bankrupt by charging high interest

⁷⁷ *Id.* at 246–47. Eighteen percent is the average interest rate, but credit card issuers often raise the rate to twenty-four percent or higher for borrowers who fall behind in payments. *Id.* at 18–19.

⁷⁸ *See id.* at 130.

⁷⁹ A comparison between Canada and the United States suggests that credit-card lending has played a substantial role in consumer debt and bankruptcy increases. Modern credit cards were introduced in the mid-1960s in both the United States and Canada, but states regulated interest rates in the United States until the 1978 *Marquette* decision, whereas Canadian interest rates have been deregulated since at least 1886. *See Ellis, supra* note 74, at 9. The Canadian and American personal bankruptcy rates have both risen dramatically in the past twenty years, yet the Canadian rate rose immediately following the introduction of credit cards—rising by 340% between 1966 and 1976—while the American rate took off only after the *Marquette* decision made widespread marketing of credit cards profitable in the United States. *See id.* at 9–10; *see also* JUDICIARY COMMITTEE DISSENTING VIEWS, *supra* note 9, at 479.

⁸⁰ Timothy L. O’Brien, *Lowering the Credit Fence: Big Players are Jumping Into the Risky Loan Business*, N.Y. TIMES, Dec. 13, 1997, at D1.

⁸¹ *See Ellis, supra* note 74, at 10.

⁸² *See SULLIVAN ET AL., supra* note 43, at 28–33.

⁸³ *See id.* at 75–107, 172–98.

⁸⁴ *See id.* at 22–26.

⁸⁵ *See id.* at 138.

rates to those who manage to recover and repay some or all of their debts.⁸⁶

In the view of critics of the Bankruptcy Reform Act, the role of structural economic trends and creditor behavior in the recent bankruptcy boom argues against the bill's focus on discouraging bankruptcy by strengthening creditor protections. The dissenters on the House Judiciary Committee contend that "the vast weight of the data and studies contradict [sic] the proponents' rationales and instead shows that non bankruptcy law factors are the root cause of increased bankruptcy law filings."⁸⁷

Reforms to benefit creditors are inappropriate, critics argue, for they benefit credit card lenders and other creditors who have helped create the bankruptcy crisis while burdening "vulnerable groups" that find themselves in debt as a result of financial and economic forces beyond their control.⁸⁸

Most Senators and Representatives, however, appear to have been more persuaded by the contrary view that deterrents should be directed at borrowers, not lenders, notwithstanding any role lenders have played in fostering current bankruptcy levels. It may be that structural economic changes are the causes of bankruptcy. Nevertheless, the argument goes, if consumers are using the bankruptcy system to avoid the consequences of irresponsible purchases or to support unrealistic financial expectations, then it is appropriate for Congress to encourage saving and restraint by sending a "moral signal" that debts must be repaid.⁸⁹ For many reformers, the prospect of an economic recession adds force to this view since the risk of bankruptcy will likely increase for many households during hard times.⁹⁰ As for the concerns about vulnerable groups, the bill's means test purports to address them by ensuring that the bill adversely affects only those debtors who fail the means test and do not "need" Chapter Seven relief.⁹¹ Thus, proponents have been able to present the bill as "balanced," notwithstanding critics' concerns about its generosity to creditors.⁹²

⁸⁶ *See id.*

⁸⁷ JUDICIARY COMMITTEE DISSENTING VIEWS, *supra* note 9, at 457.

⁸⁸ *Id.* at 455.

⁸⁹ Jones & Zywicki, *supra* note 64, at 191.

⁹⁰ *See, e.g.*, 147 CONG. REC. S1806 (daily ed. Mar. 5, 2001) (statement of Sen. Grassley (R-Iowa)) ("If we hit a recession without fixing the bankruptcy system, we could face a situation where bankruptcies spiral out of control even beyond what they were in the good times of 1998, 1997, and 1996.").

⁹¹ *See, e.g.*, 147 CONG. REC. H133 (daily ed. Jan. 31, 2001) (statement of Rep. Gekas (R-Pa.)) ("[House Bill 333] is tailored to make certain that anyone who is so overwhelmed by debt, so swamped by the inability to pay one's [sic] obligations . . . [is entitled] to be discharged in bankruptcy, to be free from the debts that so overwhelmed him."); Jones & Zywicki, *supra* note 64, at 207 ("Apocalyptic rhetoric to the contrary, the reality of means-testing is that it will apply only to bankruptcy filers with above median incomes, sufficient disposable income to fund a plan, the ability to repay a substantial portion of their unsecured debt, and no other overriding hardship.").

⁹² *See, e.g.*, 147 CONG. REC. S1807-08 (daily ed. Mar. 5, 2001) (statement of Sen. Grassley (R-Iowa)) ("[C]laims that this bill is unbalanced for the creditor and against the

The Bankruptcy Reform Act's likely effects are no less contested than the explanations for current bankruptcy trends. Reformers claim that the Bankruptcy Reform Act will be beneficial to consumers because toughened debt collection will lead to lower borrowing costs. There is some doubt, however, as to whether credit card interest rates are sufficiently competitive to respond to bankruptcy reforms. Despite deep market penetration and intense competition for new customers,⁹³ credit card issuers generally compete by offering perks such as purchasing discounts and frequent flier miles, not by offering lower interest rates.⁹⁴ Thus, while bank borrowing rates fell from 13.4% to 3.5% between 1980 and 1992, the average credit card interest rate rose from 17.3% to 17.8%.⁹⁵ In an influential article, economist Lawrence Ausubel has speculated that this "stickiness" occurs because many consumers deceive themselves about the likelihood they will carry a balance on their credit cards: they fail to seek out lower rates though it would be in their interest to do so.⁹⁶ Other commentators have suggested that interest rates remain high because the consumers who carry credit card balances are not savvy enough to appreciate the importance of the interest rate, while more sophisticated cardholders generally use cards only for convenience and do not carry account balances.⁹⁷

The disclosure requirements included in the Bankruptcy Reform Act could mitigate such problems by exposing credit cards' use of low minimum payments and high interest rates to keep consumers in debt.⁹⁸ It is doubtful, however, whether the inclusion of further fine-print disclosures on credit card materials would have any significant impact on consumer behavior.⁹⁹ Moreover, if Ausubel is correct about borrower self-deception, then it is likely that consumers would persist in ignoring interest rate information, permitting card issuers to continue to charge uncompetitive rates.

On the other hand, some reform proponents have argued that the low transaction costs of credit card borrowing justify the high interest rates.¹⁰⁰ There is also evidence that consumers have begun to take note of interest rates, shifting balances between cards to exploit introductory "teaser" rates and reduce monthly payments.¹⁰¹ If credit card interest rates are

debtor are wrong. There are enhanced consumer protection and information and education provisions . . .").

⁹³ See *supra* text accompanying note 76.

⁹⁴ See SULLIVAN ET AL., *supra* note 43, at 254.

⁹⁵ *Id.* at 255 (quoting JAMES MEDOFF & ANDREW HARLESS, *THE INDEBTED SOCIETY: ANATOMY OF AN ONGOING DISASTER* 12 (1996)).

⁹⁶ Lawrence Ausubel, *The Failure of Competition in the Credit Card Market*, AM. ECON. REV. Vol. 81, No. 1, at 50, 70-71 (Mar. 1991).

⁹⁷ See SULLIVAN ET AL., *supra* note 43, at 255.

⁹⁸ See *id.* at 247-48.

⁹⁹ See Ball & Stuart, *supra* note 37, at 1503-04.

¹⁰⁰ See, e.g., Jones & Zywicki, *supra* note 64, at 228-31.

¹⁰¹ See Jeff Bailey & Scott Kilman, *Taking Credit: Here's What's Driving Some Lend-*

economically reasonable, or are becoming so, then responsible borrowers might reap benefits from toughened bankruptcy laws. Still, the remarkable profitability of consumer lending¹⁰² and the prevalence of high interest rates have led some members of Congress to doubt whether “the credit card industry likely would pass on any of the ‘savings’ from bankruptcy law changes to individual consumers.”¹⁰³

There is also debate as to whether the Bankruptcy Reform Act would produce significant benefits for creditors. As Professor Elizabeth Warren has observed:

Bankruptcy is the ultimate zero-sum system. Creditors compete for the limited dollars of the people who have declared themselves bankrupt. More to one creditor is necessarily less for another.¹⁰⁴

Yet the Bankruptcy Reform Act avoids choosing between creditors; to the contrary, it flattens distinctions between them by toughening presumptions against dischargeability and blocking the bifurcation of undersecured debts. The result, in the words of Senator Feingold (D-Wis.), “is a bill at war with itself”—more creditors competing for the same funds.¹⁰⁵ This competition could mean that creditors end up collecting little more than they would under current law. One analyst has concluded that increasing secured creditors’ claims under Chapter Thirteen by preventing strip-down would “reduce distributions to unsecured creditors in Chapter 13, eliminating them in many cases.”¹⁰⁶ This possibility raises further doubts about the effect on interest rates: if unsecured lenders do not benefit from the bill, there will be no cost savings for them to pass on to consumers. On the other hand, if unsecured creditors receive more, secured creditors might receive less than they would have through Chapter Seven reaffirmation agreements, with the result that the costs of secured borrowing—for instance, automobile financing—could rise.

Critics are particularly concerned about the bill’s implications for priority creditors such as former spouses and local tax authorities.¹⁰⁷ The

ers Crazy: Borrowers Who Think Working Class Is Getting Hip to Lower Interest Rates; Card Surfing Is the Rage, WALL ST. J., Feb. 20, 1998, at A1.

¹⁰² See Lawrence Ausubel, *Credit Card Defaults, Credit Card Profits, and Bankruptcy*, 71 AM. BANKR. L.J. 249, 258–59 (1997). In part because of the high interest rates charged, financial institutions earn higher profits from credit cards than any other lending activity. See *id.*

¹⁰³ JUDICIARY COMMITTEE DISSENTING VIEWS, *supra* note 9, at 458.

¹⁰⁴ *Bankruptcy Reform Hearing*, *supra* note 47 (statement of Elizabeth Warren).

¹⁰⁵ 145 CONG. REC. S14,067 (daily ed. Nov. 5, 1999) (statement of Sen. Feingold (D-Wis.)) (commenting on an earlier version of the bill in the 106th Congress).

¹⁰⁶ Norberg, *supra* note 34, at 462.

¹⁰⁷ See, e.g., 145 CONG. REC. S14,067 (daily ed. Nov. 5, 1999) (statement of Sen. Feingold (D-Wis.)) (“In too many cases, I am afraid, [the bill] will hinder families’ ability to meet other obligations, particularly their obligations to their own children and to local

House Judiciary Committee Report stresses that “[d]omestic support claimants receive a broad spectrum of special protections” under the Bankruptcy Reform Act.¹⁰⁸ Like current law, the bill assigns priority status to family support obligations¹⁰⁹ and taxes,¹¹⁰ rendering them non-dischargeable along with certain other debts such as educational loans.¹¹¹ Critics worry, however, that since the bill expands the definition of non-dischargeable cash advances and consumer loans, it may place “the single mother seeking money for food into direct competition with credit card debt.”¹¹² Furthermore, by pushing debtors into Chapter Thirteen while restricting their right to re-file if their plans fail, the Bankruptcy Reform Act may make it more difficult for priority creditors to collect what they are owed. Roughly two-thirds of Chapter Thirteen plans fail under current law;¹¹³ analysts predict the success rate would remain low under the reform bill.¹¹⁴ When a debtor’s Chapter Thirteen plan fails, creditors may resume efforts to collect outstanding debts, deploying tactics ranging from letters, phone calls, and visits by collection agents to state law collection procedures, such as wage garnishment and asset foreclosure.¹¹⁵ In such circumstances, families and other priority creditors may lose out in the competition with more assertive and experienced debt collection professionals.¹¹⁶ Some debtors who might meet their priority obligations following a Chapter Seven discharge may instead end up paying their limited funds to non-priority creditors who are more assertive following the failure of a Chapter Thirteen plan.

A final important argument concerning the likely effects of the Bankruptcy Reform Act pertains to the costs of the bill for litigants and for the bankruptcy system. Since Chapter Thirteen plans require ongoing court supervision, Chapter Thirteen cases generally involve higher lawyer fees and court costs than Chapter Seven cases.¹¹⁷ Thus, an increase in

taxing authorities.”).

¹⁰⁸ HOUSE JUDICIARY COMMITTEE REPORT, *supra* note 6, at 11.

¹⁰⁹ See H.R. 333, §§ 211–15.

¹¹⁰ See *id.* § 705.

¹¹¹ See *id.* § 220.

¹¹² JUDICIARY COMMITTEE DISSENTING VIEWS, *supra* note 9, at 475.

¹¹³ See Norberg, *supra* note 34, at 439; see also SULLIVAN ET AL., *supra* note 43, at 14.

¹¹⁴ See Norberg, *supra* note 34, at 450–51. While the Bankruptcy Reform Act’s means-test might be expected to improve the success rate by pushing higher-income debtors into Chapter Thirteen, Norberg’s empirical examination of Chapter Thirteen cases found no correlation between income and plan completion. See *id.* Norberg goes on to say conclude that “[t]he essential unpredictability of success in chapter 13 undermines the case for means-testing.” See *id.*; see also Jean Braucher, *Increasing Uniformity in Consumer Bankruptcy: Means Testing as a Distraction and the National Bankruptcy Review Commission’s Proposals as a Starting Point*, 6 AM. BANKR. INST. L. REV. 1, 11 (1998) (“The impact of stricter means testing would likely include a higher failure rate [for Chapter Thirteen cases].”).

¹¹⁵ See White, *supra* note 2, at 211–12 (describing creditors’ legal remedies against debtors who default).

¹¹⁶ See JUDICIARY COMMITTEE DISSENTING VIEWS, *supra* note 9, at 472–75.

¹¹⁷ See Norberg, *supra* note 34, at 436.

Chapter Thirteen filings may impose higher costs on the bankruptcy system, while also increasing the proportion of debtors' assets that go to lawyers rather than creditors. Additionally, the Bankruptcy Reform Act's means test may be expensive to administer. One study based on an earlier version of the Bankruptcy Reform Act¹¹⁸ found that only 3.6% of Chapter Seven debtors would pass the means test and qualify as "can-pays" who should instead have been in Chapter Thirteen.¹¹⁹ If the Bankruptcy Reform Act's means test would filter out only a small proportion of Chapter Seven debtors, then, in the view of some critics, the costs of administering the test may outweigh the benefits.¹²⁰

Whether the means test is worthwhile despite its costs may depend on a value judgment. In the Committee Report on the Bankruptcy Reform Act, both the majority and the dissenters cite the 3.6% figure to support their views; this suggests the two sides assign different values to the social importance of pushing a small proportion of "can-pays" out of Chapter Seven.¹²¹ At a time when many households are taking on unmanageable levels of debt, it may be important for the bankruptcy system to send a strong signal that debtors who can pay must do so.¹²² Furthermore, one scholar has suggested that many courts already apply an *ad hoc* income test in making determinations of Chapter Seven abuse. If that is the case, then the universal application of a "mechanical test" could enhance the bankruptcy system's clarity and efficiency.¹²³

The administrative hurdle of a means test could possibly lead debtors outside of the 3.6% to file under Chapter Thirteen even though they could qualify for Chapter Seven. As one commentator predicts, "[s]ome

¹¹⁸ H.R. 3150, 105th Cong. (1998).

¹¹⁹ Marianne B. Culhane & Michaela M. White, *Taking the New Consumer Bankruptcy Model for a Test Drive: Means-Testing Real Chapter 7 Debtors*, 7 AM. BANKR. INST. L. REV. 27, 31 (1999). While research funded by the credit card industry has suggested that more than ten percent of Chapter Seven debtors would qualify as "can-pays," independent academics, as well as the General Accounting Office have criticized these results. *See id.* at 28–31 (describing industry-funded research and the debate over the results). *But see* Jones & Zywicki, *supra* note 64, at 186–200 (criticizing the Culhane & White study and arguing for the industry-funded research).

¹²⁰ *See, e.g., Bankruptcy Reform Hearing, supra* note 47, at 1 (statement of Prof. Warren) ("A good example of the failure of cost-benefit analysis is evident in the proposed means test.")

¹²¹ *See* HOUSE JUDICIARY COMMITTEE REPORT, *supra* note 6, at 5–6 n.18 (quoting the Culhane & White study to support the proposition that "debtors can, in fact, repay a significant portion of their debts"); *see also* JUDICIARY COMMITTEE DISSENTING VIEWS, *supra* note 9, at 458 (referring to the figure as "a mere 3.6%").

¹²² *See* Jones & Zywicki, *supra* note 64, at 191–92 ("[T]o the extent that there are doubts about the administrative savings that would result from a bright-line statutory means-testing requirement or about the number of individuals who would qualify under means-testing, this moral message [that debts must be repaid] must also be put on the scale in favor of means-testing.")

¹²³ Felsenfeld, *supra* note 13, at 1402; *see also* Jones & Zywicki, *supra* note 64, at 205 ("[S]tatutory-based means testing would substitute a bright-line rule for the current murky standard. In general, bright-line rules tend to reduce administrative costs relative to standards and increase the predictability of their application.") (footnotes omitted).

lawyers would avoid the expense of dealing with abuse or eligibility challenges by putting nearly all clients in chapter 13.”¹²⁴ Lawyers working for low-income clients on a fixed fee might have little incentive to complete the work required to establish Chapter Thirteen eligibility; meanwhile, debtors filing without representation might find the paperwork discouraging or impossible. As a result, debtors who could qualify for Chapter Seven may end up filing under Chapter Thirteen instead. Given the poor success rate of Chapter Thirteen plans, such debtors might spend years cycling in and out of repayment plans, struggling to pay debts that should have been discharged under Chapter Seven.¹²⁵

This possibility indicates what may be at stake in Congress’ efforts to overhaul the American bankruptcy system. The United States is unique among modern western states in offering its citizens the right to clear their debts and start over.¹²⁶ This “fresh start” policy has traditionally been seen as a component of America’s entrepreneurial, free-market culture: bankruptcy discharge promotes risk-taking by protecting failures; it ensures that no individual’s productivity is dampened by the prospect of earning income only to pay off old debts.¹²⁷ Western European countries have generally opted instead to compensate for economic risks by providing a generous social safety net.¹²⁸ A bankruptcy reform that pushes more debtors into unsuccessful Chapter Thirteen plans would place the United States in the novel position of offering its citizens neither the social protections of European states, nor the power to borrow during emergencies and clear debts through bankruptcy.¹²⁹

¹²⁴ Braucher, *supra* note 114, at 11.

¹²⁵ *See id.*; *see also* SULLIVAN ET AL., *supra* note 43, at 253–54 (describing proposals to push debtors out of Chapter Seven as “a social experiment that could get very ugly”). The possibility that many Chapter Seven debtors may end up filing unsuccessful Chapter Thirteen plans may explain why the credit card industry has lobbied so aggressively for a means test. *See* Warren, *supra* note 33, at 503–06 (indicating that the credit card industry advocated means-testing even before specific means test proposals were developed). Some research suggests unsecured creditors would get little more under Chapter Thirteen plans than they do now in Chapter Seven cases. *See supra* text accompanying note 106. Since most Chapter Thirteen plans fail, however, the displacement of Chapter Seven filers into Chapter Thirteen would mean in practice that credit card lenders could at least pursue debtors out of court, where their experience and sophistication may give them an advantage over other creditors. *See supra* text accompanying notes 115–116; *see also* Jones & Zywicki, *supra* note 64, at 191 (“If there really were no benefit to unsecured creditors from channeling more debtors into Chapter 13 payment plans, the credit industry would not be advocating means-testing.”) (footnotes omitted).

¹²⁶ *See* SULLIVAN ET AL., *supra* note 43, at 257–59.

¹²⁷ *See id.* at 258; *see also* Thomas H. Jackson, *The Fresh-Start Policy in Bankruptcy Law*, 98 HARV. L. REV. 1393 (1985) (arguing that the fresh start policy is justified by psychological tendencies to underestimate the social costs of risky decisions and to trade future costs for present benefits); John M. Czarnetsky, *The Individual and Failure: A Theory of Bankruptcy Discharge*, 32 ARIZ. ST. L.J. 393 (2000) (arguing that debt discharge by the bankruptcy system protects entrepreneurship, creating net benefits for society).

¹²⁸ *See* SULLIVAN ET AL., *supra* note 43, at 257.

¹²⁹ *Cf. id.* at 257–59 (comparing the European and American models and concluding “the need for a more protective consumer bankruptcy law is directly proportional to the

Given that debtor abuse may not be the sole explanation for high bankruptcy levels, and that interest rate reductions may not be the principle effect of restrictions on debt discharge, the Bankruptcy Reform Act shortchanges the complexity of the issues facing the American bankruptcy system. Toughened bankruptcy laws may deter some borrowing, but for any debtors who continue to accumulate unmanageable debts, the bankruptcy system will face the same choice it has faced throughout American history: it can demand that debtors repay what they can, or it can permit them to clear some debts and make a fresh start. Credit card companies and other lenders have earned healthy profits in a system that reflects the latter choice. Indeed, it is unclear creditors could earn much more in a system that restricts debt discharge; after all, debtors' resources are limited, however large their debts.¹³⁰ The question the Bankruptcy Reform Act raises is whether such marginal benefits to lenders are worth the cost of preventing millions of families from putting their financial misfortunes behind them.

—Zachary Price

size of the social safety net and the availability of consumer credit.”).

¹³⁰ *See id.* at 255 (“[M]uch of the debt discharged in bankruptcy had already been written off by the issuer as ‘uncollectible’ because the issuer had determined that the debtor was so unlikely ever to have the resources to repay that spending another dollar on debt collection was throwing good money after bad.”).