

BANKRUPTCY BY THE NUMBERS

CONSUMER FILINGS IN A COMPLEX ECONOMY

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In this month's article we continue our effort to characterize the current status of consumer bankruptcy and the contexts in which it arises.

One of the striking aspects of the bankruptcy landscape is that consumer filings have climbed to new highs while many other features of the economy have shown sustained positive growth. This apparent anomaly is frequently noted in political discussions about consumer bankruptcy reform, including the conclusion that "the bankruptcy crisis is not due to recession, depression, inflation or high unemployment."² Moreover, chapter 11 filings have been falling during this time period, lending apparent support to the view that current economic conditions should result in reduced consumer rates as well.³ Unless, of course, there are serious flaws in the consumer bankruptcy system that present inappropriate temptations to prospective filers. Whether there are such serious flaws is an issue at the core of the debate about proposed legislative changes pending in H.R. 833 and S. 625.⁴

Recent improvements in measures of income are widespread. Thus the Census Bureau reported that 1998 was the fourth year in a row in which real median income increased for U.S. households, arriving in 1998 at a value of \$38,885.⁵ Between 1997 and 1998, growth occurred in

¹All views expressed in this article are those of the authors and do not necessarily represent the views of the Executive Office for U.S. Trustees.

² S. Report No. 49, 106th Cong., 1st Sess. 2 (1999). Subsequent examples of this conclusion may be found at Congressional Record, September 21, 1999, S11091 (comments of Senator Sessions); and Letter of Professors Zywicki and White to Senators Hatch and Leahy, September 16, 1999, www.abiworld.org/legis/bills/106anal/gmulaw.html.

³Comments of Senator Sessions, Congressional Record, *supra* n.2.

⁴ "It is the strong view of the [Senate Judiciary] Committee that the bankruptcy code's generous, no-questions asked policy of providing complete debt forgiveness under chapter 7 without serious consideration of a bankrupt's ability to repay is deeply flawed and encourages a lack of personal responsibility." S. Report No. 49, *supra* n. 2, at 3.

⁵ U.S. Census Bureau, Current Population Reports, P60-206, *Money Income in the United States: 1998*. U.S. Govt. Printing Office, Washington, D.C., 1999. At v.

both family households and households comprising unrelated individuals, in households headed by women with no husband in the home, and in households headed by men with no wife in the home.

Other economic good news is also easy to find. The Bureau of Labor Statistics “Economy at a Glance” Report shows the civilian labor force growing from 138.1 million in September 1998 to 139.4 million in September 1999. The unemployment rate fell from 4.5% to 4.2% during the same period, while the Consumer Price Index rose very slightly each month if at all.⁶ The “Beige Book,” an economic overview published by the Federal Reserve several times during the year, has painted generally positive pictures of the economy in each of its recent reports.⁷ And there is the stock market. The Dow Jones Industrial average, the benchmark many people rely on, was at approximately 7500 sometime in September 1998 and is at about 10,600 on this day in early November, 1999; and the Nasdaq Consolidated Index has climbed past 3000, an historic high mark..⁸

How should we think about consumer bankruptcy filings in the face of all this good news about the economy? Perhaps the following observations create a useful perspective:

- In respect to median income, though there has been four-year rise, 1998 was the first year that real income was greater than it had been in 1989. For all classes of households (both family and non-family), 1998 real median income was no more than slightly greater than 1989 income. The values reported in 1989 preceded the recession that lasted from July, 1990 through March, 1991. Real median incomes have been playing catch-up since then.⁹ We noted in an earlier article that most 1998 chapter 7 bankrupts in our study sample filed at a time when their incomes had been rising—but from low baselines.¹⁰
- In respect to the broad front of advance in economic measures, there are, nevertheless, sectors that are in trouble, including agriculture in particular.¹¹ If family farmers are in crisis, then those who depend on those farmers in the economy, including their employees, business creditors,

⁶ <http://stats.bls.gov/eag.html>

⁷ www.bog.frb.fed.us/FOMC/BeigeBook/1999

⁸ See www.dowjones.com

⁹ *Money Income in the United States: 1998*, supra n. 4, at viii and B-1.

¹⁰ Bermant, Gordon, and Flynn, Ed, *Income Trajectories, Debts and Expenses of Some Chapter 7 Debtors, 1996-1998*. *Amer. Bnkry. Inst. J.*, October 1999, 16.

¹¹ The fact of distress in the agricultural sector is beyond argument, and was acknowledged on October 9, 1999 when the President signed into law a 9-month extension of Chapter 12.

and trade merchants, will feel the pain as well, and many of these may find chapter 7 bankruptcy their most rational option.

- There are sound data to support the argument that the benefits of growth have not accrued equally between men and women. On the bankruptcy side, this topic is now subject of lively discussion¹²
- The benefits of recent real income increases have not accrued equally to all racial and ethnic groups. For example, only non-Hispanic white households showed a significant increase in income from 1997 to 1998.¹³ A full account of income differences across these groups, as the Census organizes them,¹⁴ requires great care in order to capture fairly the human realities behind the aggregate statistics. Household income reports, for example, need to be corrected for whatever differences may exist between groups in the average numbers of persons per household. Across the four groups defined by the current Census (Asian and Pacific Islanders, Black, Hispanic, and non-Hispanic White), the ratio of the highest median household income to the lowest in 1998 was 1.84 (\$46,637 for Asian and Pacific Islander households; \$25,351 for Black households). When these numbers were recalculated based on considerations of household size, the ordering and ratio changed. The ratio of highest to lowest income per household member was 2.04 (\$22,633 for non-Hispanic White households, \$11,071 for Hispanic households).¹⁵ The two sets of calculations provide different pictures of incomes and their distribution in the population. Which is the better number for purposes of understanding the determinants of a decision to file consumer bankruptcy?

Income Inequalities

¹² Pollack, Oliver G., Letter to the Editor, *Amer. Bnkry.. Inst. J.*, October 1999, at 24; Sullivan, Teresa, and Warren, Elizabeth, More Women in Bankruptcy. www.abiworld.org/research/morewomen.html; Ernst & Young Study Disputes Data on Women Filing for Bankruptcy. www.abiworld.org/release/99july20.html.

¹³ *Money Income in the United States: 1998*, supra n. 4, at ix.

¹⁴ The Census Bureau emphasizes that its racial and ethnic categories require great care in interpretation. The categories of “Asian and Pacific Islander” and “Hispanic” are particularly diverse across many important dimensions. *Money Income in the United States: 1998*, supra n. 4, at vii, notes 11 and 12.

¹⁵ *Id.* at ix.

Economists and others have emphasized the growth of income and wealth disparities within the United States over the past several decades.¹⁶ Relationships between such disparities, their growth, and debtors' propensities to file for bankruptcy have not been documented or developed theoretically.¹⁷ The significance of being near the bottom of the income distribution in America today is in dispute: while some commentators express concern about the great spread in income and wealth, others argue that most households in the bottom twenty percent of the income distribution are pretty well off already, and are unlikely to stay near the bottom of the distribution, no matter how distant they are in material well-being from those in the top twenty percent.¹⁸

However one interprets the facts about income and wealth inequalities, the fact remains that chapter 7 petitioners during the past few years come overwhelmingly from the lower portions of the income distribution. For example, using the same sample of 845 filers from 1998 that we have reported on earlier, we found that 80% of the debtors were in the lower half of the general population income distribution (i.e. below the median), 88% of the debtors were in the lower 60% of the population distribution, and 98% were in the lower 80%.¹⁹

Real insight into the determinants of the decision to file for chapter 7 may require a better understanding of how individuals and families in the lower rungs of a society with increasing spreads of income and wealth come to perceive their positions with respect to their creditors and other groups around them.

¹⁶ Frank, Robert H. and Cook, Philip J., *The Winner-Take-All Society*. Penguin Books, 1996. Schor, Juliet B., *The Overspent American*. Basic Books, 1998. Wolff, Edward N., Recent Trends in the Size Distribution of Household Wealth. *J. Econ. Perspectives*, 1998, 12, 131-150.

¹⁷ In addition, both demographic trends and official measurement changes have reduced the usefulness of comparisons going back more than about 7 years. There are now relatively more households headed by single parents or comprising unrelated persons, and the Census changed its data gathering method in 1993 in a way that increases traditional measures of inequality. Comparing apples to apples has become more difficult. *Money Income in the United States: 1998*, supra n. 4, at xv, note 29.

¹⁸ For one side, see citations supra n. 16; for the other, see Sowell, Thomas, *The Quest for Cosmic Justice* (1999); Rector, Robert, The Myth of Widespread American Poverty, *The Heritage Foundation Backgrounder*, No.1221, September 18, 1998.

¹⁹ Bermant and Flynn, supra n.10. This sample may overestimate debtors' incomes because it used only those debtors who also reported incomes for 1997 and 1996. Chapter 7 filers often do not show earlier years' incomes, either because they neglect the forms or because they didn't have the income. Nor do the numbers as shown correct for size of household/family.

