

## BANKRUPTCY BY THE NUMBERS

### **A Small New Window on Chapter 13**

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Last March in this column we called for new studies of chapter 13 cases that would provide factual information vitally relevant to the policy debates surrounding proposed consumer bankruptcy reforms.<sup>2</sup> Some relevant information has since been published by Professor Scott Norberg of Mississippi College School of Law.<sup>3</sup> Norberg's analytic framework and approach to the data are salutary. His conclusions are strong and immediately relevant to current consumer bankruptcy issues - but his data are too few to support the conclusions as other than tentative. The conclusions must be tested across a wide range of bankruptcy districts. Here we briefly review Norberg's work and re-emphasize the importance of collecting and cumulating such data at a national level.

#### **The Analytic Framework**

Norberg framed his study to respond directly to the question of chapter choice: what are the consequences for debtor and their creditors arising from choices between chapter 13 and chapter 7? The analysis emphasizes the distinct interests of secured vs. unsecured creditors: under the present Code secured creditors appear to be better off with a chapter 7 filing while unsecured creditors should benefit more from [a successful] chapter 13 plan. Which

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<sup>1</sup> All 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.

<sup>2</sup> Bermant, Gordon, One Hand Clapping: What We Know, and Still Need to Know, About Consumer Cases. *Amer. Bnkry. Inst. J.*, 1999 (March), 16-17.

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Norberg, Scott F., Consumer Bankruptcy's New Clothes: An Empirical Study of Discharge and Debt Collection in Chapter 13. *7 Amer. Bnkry. Inst. L. Rev.*415 (1999).

chapter works better for a particular debtor depends on the distribution of the debt: debtors with relatively high secured or priority debts fare better in chapter 13, all else equal, while debtors with little or no secured debt should be better off in chapter 7.

There is thus a three-way tension built into the chapter choice decision that is now determined almost entirely by the debtor:<sup>4</sup> a tension between the debtor and each of the two major creditor classes, and a tension between secured and unsecured creditors themselves. In the current debates about changing the rules for chapter choice through means-testing, the tension between secured and unsecured creditors has not been nearly so visible publicly as that between the unsecured creditors and debtor community representatives. As Norberg observes, some recent statutory proposals and the Supreme Court's ruling in *Associates Commercial v. Rash*<sup>5</sup> provide new protections to secured creditors in chapter 13.<sup>6</sup>

We do not have a clear public national view of how debtors progress through chapter 13 and how well their creditors do in terms of eventual payout.<sup>7</sup> One approach to

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<sup>4</sup> Of course we recognize that the debtor's counsel and the local legal culture have a significant influence on a debtor's chapter choice. See Braucher, Jean, *Lawyers and Consumer Bankruptcy: One Code, Many Cultures*, 67 Am. Bankr. L.J. (Fall 1993)

<sup>5</sup>520 U.S. 953 (1997)

<sup>6</sup> Norberg, *supra* n.3, at 426.

<sup>7</sup> The Executive Office for U.S. Trustees maintains careful records of amounts disbursed annually to different creditor classes in chapter 13. Over the past several years, payments to secureds have been 2.5 to 3 times greater than payments to general unsecureds. The policy significance of this ratio, and the dollar amounts behind them, are difficult to discern without additional information about the details of the plans within which the disbursements were made: their duration, percentages of debt totals owed at the time of filing, extent of secured debt cram down, amounts paid outside of the plans, and so on. See Norberg, *supra* n.3, at 434. There are two numerical errors in the table as published: the "other"

gaining that view is to go district by district to gain the relevant longitudinal perspective. Norberg provided that perspective for the Southern District of Mississippi, circa 1998.

### **The Data**

The data comprised 71 chapter 13 cases filed in Mississippi Southern between 1992 and 1998; all were closed between January and June of 1998.<sup>8</sup> By beginning with the standing trustee's closing report and working back to the schedules and plan, Norberg could show the progress, or lack of it, of these filings to a successful completion and discharge. Comparing schedules to plans<sup>9</sup> was also a critical part of the analysis. Only with that comparison can we understand how chapter 13 operated in fact to regulate the extent of creditor disbursements and to aid or thwart the debtor's progress through to a chapter 13 discharge.

In a series of 26 tables Norberg wrings the useful information out of the data from the 71 cases. We will not summarize the findings here except as they bear on the significant conclusions described in the next section.

### **The Conclusions**

Consistent with earlier reports from other districts, approximately one-third of the Mississippi Southern debtors (23 out of 71) completed their chapter 13 plans and received

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payments have not been included in the total for 1998, and the total reported for 1994 should be corrected to read \$1,844,750,141.

<sup>8</sup> Every 19<sup>th</sup> cased closed was selected. This was a 5.2% sample of the 1,371 chapter 13 cases closed in the district during the period. Norberg, *supra* n. 3, at 427.

<sup>9</sup> Norberg does not report on the prevalence of amended schedules and how the research accounted for them. We are told by knowledgeable people that amendments are frequent in the early stages of chapter 13, and that relying on the first filed schedules will produce a misleading picture of the debtor's financial affairs.

discharges.<sup>10</sup> Of the two-thirds whose cases were dismissed from chapter 13 before completion, more than 70% (35 out of 48) were dismissed after plan confirmation. This suggests that initial appearances of feasibility do not accurately predict successful completion.

In particular, debtor income was not a predictor of chapter 13 success in Mississippi Southern.<sup>11</sup> Norberg argues, with minor qualification, that these findings "undercut" the case for means-testing to limit participation in chapter 7.<sup>12</sup> Why should we expect that debtors whose bankruptcy choice is limited to chapter 13 will be more likely to succeed than these debtors, who entered the chapter voluntarily? But he further notes that the policy intent of means testing may be to exclude relative high-income people from chapter 7 without concern for the probability of their success in chapter 13.<sup>13</sup>

Unexpectedly, there was no statistically significant relationship between the percentage payback proposed and the probability of completing a plan. Nor was there a significant relationship between the proposed durations of the plans and the likelihood of successful completion.<sup>14</sup> On the other hand, the data did allow the conclusion that debtors who had filed one earlier chapter 13 case were more likely than other debtors to complete the plan successfully.

Overall, the most compelling findings in the data were these:

- debtors who successfully completed their plans had significantly higher secured debt at the time of filing than did debtors whose cases were eventually dismissed. The higher debt likely relates to more assets. In a nutshell then, debtors for whom chapter 13 provides the best chance to keep their major possessions are more likely to make the plan work for them. From a debtor's

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<sup>10</sup> Norberg, *supra* n.3, at 440.

<sup>11</sup> *Id.*, at 442.

<sup>12</sup> *Id.*, at 441.

<sup>13</sup> *Id.*, at 442.

<sup>14</sup> *Id.*, at 447, table 15.

perspective, this seems to be what chapter 13 is about.<sup>15</sup>

- The distributions proposed for unsecured creditors in the 71 cases ranged from 0% to 100%. While almost one-third of the debtors proposed 100% repayment, almost one-half proposed to repay no more than 15%.<sup>16</sup> Only about one-third of all the scheduled debt was unsecured (including priority and general).<sup>17</sup> Norberg concludes that "debtors pay precious little unsecured debt in chapter 13."<sup>18</sup>

### **The Weaknesses**

Norberg's analysis of the current Code and case law, and the implications of legislative proposals, are commendable. Also to be commended is the effort to illustrate how chapter 13 works in fact. The weaknesses arise from the small sample size and the probability that Mississippi Southern is a statistically aberrant district. To begin with, the percentage of chapter 13 filings (41%) is considerably higher than the national average. Second, the income distribution within the district is lower than average; the median income for the study population, \$14,400, would count as poverty level for families in many parts of the country. (One wonders what the median income of chapter 7 filers is in the district.) Third, the median duration of proposed plans, 48 months, may be longer than average. And so on. Without data from many other districts, the validity of the conclusions based on these 71 cases cannot be gauged beyond their borders.

### **The Future**

We are optimistic that it will be possible to pursue this kind of analysis into other districts. There are administrative reasons to do so that are important irrespective of how the results work out for the more general

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<sup>15</sup> Id., at 448-449.

<sup>16</sup> Id., at 445, table 13.

<sup>17</sup> Id., at 454.

<sup>18</sup> Id., at 461.

debates about consumer bankruptcy policy. The support that the Mississippi Southern data provide for some earlier published conclusions, as well as the doubt they cast on others, show the value of developing an accurate portrayal of the substance and trajectories of chapter 13 cases throughout the country -- a portrayal that permits a national summary without losing the importance of regional and local variations.