

BANKRUPTCY BY THE NUMBERS

BY: ED FLYNN
& GORDON BERMANT

Executive Office for United States Trustees^{1/}
Burke, Virginia

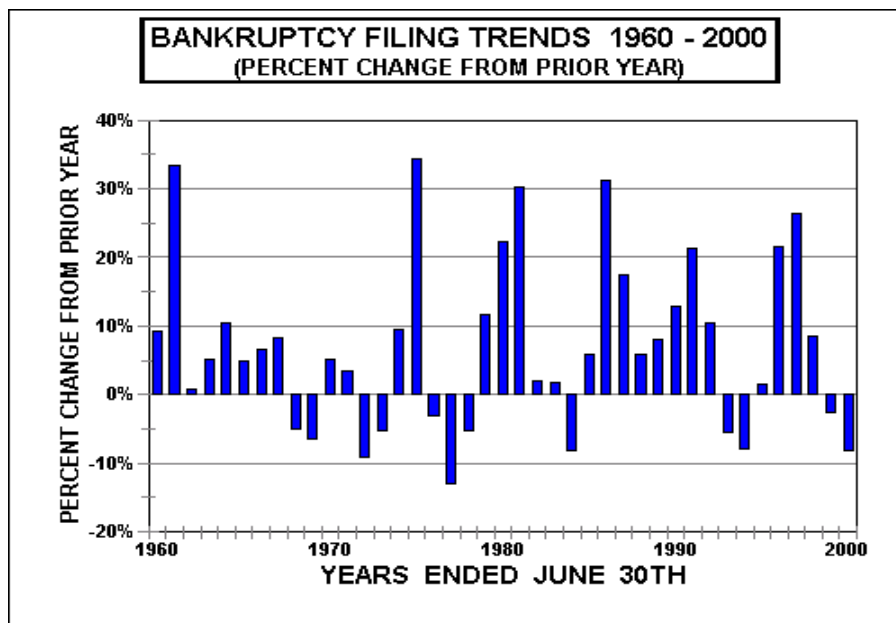
Edward.Flynn@usdoj.gov
gbermant@erols.com

FILING PROJECTIONS:

Bankruptcy filings are volatile, and anyone who makes projections on filings in the short-term runs the risk of looking foolish. Here, we try to predict where bankruptcy filing levels might go between 2001 and 2006 if reform legislation is enacted. For the purpose of these projections, we assume that reform legislation comparable to S. 420 or H.R. 333 will be signed by the President in early July, and become effective at the beginning of 2002.

The first step is to determine what filings would do if the existing laws are not changed. Next we will adjust these projections to account for changes resulting from reform legislation.

We appear to be at the end of a drop in filings that has lasted for two years. Filings have dropped by about 13% from their peak during this period, from 1,442,549 in 1998 to 1,253,444 in 2000. This decline is consistent with past decreases. As shown on this chart, there have been six periods of declining bankruptcy filings since 1960. On each occasion, the decrease lasted between one and three years, with the total decline from the peak of between 10% and 20%.



As the chart also shows, when filings start to increase, the increase is usually modest during the first year, followed by much higher increases in the second and third years. If the rate of change in the next cycle approximates those that have occurred over the last 20 years, we could expect to see a modest increase in 2001, substantial increases in 2002 and 2003, a modest increase in 2004, and declines in 2005 and 2006. Thus, without legislation our rough estimate of filings for the next six years would be as follows

^{1/} All views expressed in this article are those of the authors, and do not necessarily represent the views of the Executive Office for United States Trustees or the Department of Justice.

PROJECTED BANKRUPTCY FILINGS – WITHOUT REFORM LEGISLATION		
CALENDAR YEAR	PROJECTED FILINGS	CHANGE FROM PRIOR YEAR
<i>2000 (ACTUAL)</i>	<i>1,253,444</i>	<i>[-5%]</i>
2001	1,378,000	10%
2002	1,656,000	20%
2003	1,904,000	15%
2004	2,000,000	5%
2005	1,840,000	[-8%]
2006	1,693,000	[-8%]

IMPACT OF LEGISLATION: Reform legislation would have a significant impact on filings, both in the short term and in the long term.

SIX-MONTH IMPLEMENTATION PERIOD: Most provisions in the proposed legislation will become effective six months after the bill is signed by the President. News accounts around the time of passage of S. 420 may have over-emphasized the potential impact of the bill, and under-emphasized the fact that there was a six-month period between enactment and the effective date of means testing. We have heard anecdotal evidence of a surge in filings in March of this year. We would expect a similar, but larger surge to occur after a bill is signed by the President, and an even larger surge in filings to occur in the month or two before means testing becomes effective. In total, these surges may increase filings by 100,000 - 200,000 this year, over what they would have been without legislation. These additional cases would consist both of debtors who would have filed just after the effective date, along with some debtors who would not have filed at all, absent reform legislation.

FILINGS UNDER THE NEW LAW: Immediately after the bill becomes effective, filings will likely drop off sharply as many debtors would have filed just prior to the effective date and others will be wary of how they would fare under the new law. We estimate that this decrease will amount to about 100,000 cases— nearly one month’s average filings.

Several other factors in the reform legislation will affect future filings. Mandatory credit counseling prior to bankruptcy may have the biggest impact on future filing levels. About 20% of potential debtors will have incomes above the applicable median income threshold for their state and family size. A substantial proportion of these higher income debtors may enter into debt payment plans with credit counselors. Certain below median income debtors may also be able to enter debt repayment plans and avoid filing for bankruptcy. Additionally, the means test, the documentary verification that will be needed (past tax returns and wage statements), and the possibility of an audit will also have an impact on filing levels. Overall, in consideration of these factors, our rough estimate is that reform legislation will reduce filings by about 15% over what they would have been without legislation. Although the legislation will affect total filings, it may not cause a significant change in the

proportions of Chapter 7 and Chapter 13 cases.² The following chart shows our projections of total filings for the next six years with and without reform legislation.

CHAPTER MIX:

PROJECTED BANKRUPTCY FILINGS		
CALENDAR YEAR	WITHOUT LEGISLATION	WITH LEGISLATION
2001	1,378,000	1,528,000
2002	1,656,000	1,308,000
2003	1,904,000	1,618,000
2004	2,000,000	1,700,000
2005	1,840,000	1,564,000
2006	1,693,000	1,439,000

In summary, if Bankruptcy reform becomes effective at the beginning of 2002, we see filings rising to record levels in 2001, falling in 2002, rising sharply in 2003 and 2004, and falling modestly in 2005 and 2006. If this scenario is correct, filings in 2006 will be about the same as they were in 1998.

If this scenario is not correct, we hope to be in a new line of work by 2006.

²For the past two decades there has been roughly a 70/30 mix of Chapter 7 to Chapter 13 cases. (Chapter 11 and Chapter 12 cases comprise well under one percent of all filings.) The legislation will have an impact on the chapter choice of many debtors. Some would-be Chapter 7 filers will be required to file under Chapter 13. Many current Chapter 13 filers would be eligible for Chapter 7 under means testing. Other provisions in the legislation may affect chapter choice of individual debtors. Overall, however, that these factors may cancel themselves out, and that the proportion of filings could remain very close to the present 70% Chapter 7 and 30% Chapter 13.