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WORKING PAPER – DO NOT CITE OR QUOTE

Twenty-First Century Bankruptcy: Two Decades of Evidence About Consumer Debt and The Stigma of Bankruptcy

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The passage of the 2005 amendments to the Bankruptcy Code represents the turning of a page in the long history of personal bankruptcy in the United States.[1] At the very moment that European countries are liberalizing their treatment of individual debtors,[2] the amendments may make it difficult or impossible for many overindebted Americans to start afresh. This article reports the third of three comparable empirical

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Some of the data cited in this Essay are from the Consumer Bankruptcy Project III, 2001, an empirical study of 1250 families filing for bankruptcy during the first half of 2001 in five judicial districts around the country. The Consumer Bankruptcy Project III was funded through grants from the Ford Foundation, the Harvard Law School, and New York University Law School. The enthusiastic support and assistance of many bankruptcy judges, bankruptcy clerks, Chapter 7 and Chapter 13 trustees, and attorneys also contributed significantly to this work. The principal investigators express our gratitude to the organizations that provided financial support and to each of the judges, clerks, trustees, and lawyers who made this research possible. Without diluting that general thank you in any way, we must express special appreciation to Tom Powers and Beverly Brooks in the Northern District of Texas and XXXXXXXX

No project of this kind could be put together without the contribution of a number of people. Consumer Bankruptcy Project I in 1981 and Consumer Bankruptcy Project II in 1991 were the work of Professors Teresa A. Sullivan, Jay Lawrence Westbrook, and Elizabeth Warren.

All three of us have continued our work into Consumer Bankruptcy Project III, the 2001 study. In addition, Professors David Himmelstein, Bruce Markell, John Pottow, Michael Schill, Deborah Thorne, Susan Wachter, and Steffie Woolhandler have shared in its design and development. John Pottow, Katherine Porter, and Deborah Thorne, all now professors, served as Project Director at different times, participating in the design of the study and managing much of the data collection. Randi Segatore, Ann de Ville, and Cathy Ellis provided extraordinary administrative support, and Alexander Warren designed and managed all the coding databases. We are grateful for the contributions of each of these people in creating a database that permits analysis from so many different perspectives.

[1] Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8 (2005).

[2] *See, e.g.,* Jason J. Kilborn, *The Innovative German Approach to Consumer Debt Relief: Revolutionary Changes in German Law, and Surprising Lessons for the United States*, 24 NW. J. INT’L L. & BUS. 257 (2004); Jay Lawrence Westbrook, *Local Legal Culture and the Fear of Abuse*, 6 Am. Bankr. I. L. Rev. 463 (1998); Johanna Niemi-Kiesilainen, Consumer Bankruptcy in Comparison: Do We Cure A Market Failure or A Social Problem, 37 Osgoode H. L.J. 473 (1999). *See generally*,
Johanna Niemi-Kiesilaunen, Iain Ramsay and William C. Whitford, eds. Consumer Bankruptcy in Global Perspective (Hart ed 2003 (hereafter “*Global Perspective*”).

observations of individual bankruptcy over twenty years, establishing a baseline against which the effects of the new amendments can be studied. The data we discuss also cast light on a longstanding debate: the role of stigma in personal bankruptcy. That debate has been driven by attempts to explain the spectacular increase in filings for personal bankruptcy, a conversation that will undoubtedly continue and even intensify under the new regime.

A remarkable change has taken place across America in the past two decades. Families declaring themselves busted, unable to make it to the next payday, have tumbled into bankruptcy in record numbers. In 1981, shortly after the new bankruptcy code had settled into law, 315,818 households headed to the bankruptcy courts to file non-business bankruptcies.[3] By 2001, the number had leapt to 1,452,030.[4] In 2004, prosperity only slightly slowed the upward trend. In 2004, 1,563,145 nonbusiness bankruptcies were filed, a new bankruptcy case every twenty seconds.[5]

The surge in bankruptcy filings has prompted a ferocious debate. Credit card issuers,[6] popular media,[7] and moral critics[8] claim that bankruptcy has lost its stigma. They argue that such drastically increased filings *must* mean lower stigma.[9] Economists take up the claim as well. Unable to find a strong statistical correlation between bankruptcy and a half-dozen or so economic indicators, "reduced stigma" becomes the residual variable explaining the rise in filings. [10] As shown below, it is an argument closely related to another long-standing claim, that there are substantial numbers of debtors who could pay their debts.[11]

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[3] Administrative Office of the United States Courts. Pp cite

[4] Administrative Office of the United States Courts. Pp cite

[5] In the calendar year 2004, there were 1,563,145 non-business bankruptcy filings. http://www.uscourts.gov/Press_Releases/f2tablejune04.xls (last consulted October 20, 2005). If they were spread around the clock, this would mean one filing every 20.17 seconds. Many of these filings were joint cases filed by a married couple, so the total number of adults filing in 2004 was 2,038,857.

[6] Newspapers.

[7] Newspapers.

[8] Edith H. Jones & Todd J. Zywicki, *It's Time For Means-Testing*, 1999 Brigham Young University Law Review 177. One author has gone so far as to suggest the revival of debtors' prisons (albeit in a modern, subdued form) as a device to return the appropriate stigma to bankruptcy filings. Marcus Cole, *A Modest Proposal for Bankruptcy Reform*, 5 Greenbag 269 (2002). Unfortunately, he does not cite any empirical support for the decline of stigma, although that decline is the central rationale for his proposal. *See also*, Christopher L. Peterson, *Truth, Understanding, And High-Cost Consumer Credit: The Historical Context Of The Truth In Lending Act*, 55 Fla. L. Rev. 807, 863 (2003) (small loan regulation and bankruptcy laws caused decline in stigma since 1898).

[9] *See generally*, Gordon Bermont, Bankruptcy By The Numbers, *What's Stigma Got To Do With It?* Am Bankr. L.J. 22 (July/August 2003) .

[10] Scott A. Fay, Erik Hurst, & Michelle J. White, The Bankruptcy Decision: Does Stigma Matter University of Michigan Working Paper No. 98-01, http:// papers.ssrn.com/ sol3/papers.cfm?abstract_id=70915#PaperDownload (1998). *See also*, Rafael Efrat, *Global Trends In Personal Bankruptcy*, Am. Bankr. L. J. 81 (2002) (hypothesizing a relationship between filing rates and stigma variations in several countries). The argument becomes entirely tautological, with rising filing rates implying stigma which explains rising filing rates.

[11] The concern about abuse of bankruptcy by individuals is found in many countries. *See, e.g., Global Trends*, *supra* note xx; Rafi Efrat, *Legal Culture and Bankruptcy: A Comparative Perspective*, 20 Emory

Part I of this article provides the basic data about Americans who filed for bankruptcy at the beginning of the twenty-first century and compares them with those who sought bankruptcy protection in the last two decades of the twentieth century. We make this comparison through three empirical studies of consumer bankruptcy covering persons filing for bankruptcy in 1981, 1991, and 2001. These data represent a unique time-series, because other studies have generally been limited to snapshots of bankruptcy at a single moment and therefore have been unable to prove or disprove claims about trends in the bankruptcy process. The data reported here include income, debt, assets, encumbrances, and debt/income ratios, as well as social data such as education levels and occupational prestige.[12] The data reveal that the 2001 debtors are still solidly middle-class citizens and, like Americans generally, are ever more deeply in debt, absolutely and in relation to their income and assets. These data will provide a two-decade baseline for studying the changes wrought by the 2005 bankruptcy amendments.

Part II addresses the claim that the increase in bankruptcy filings arises from a decline in the stigma associated with bankruptcy. Measuring changes in stigma is a difficult business. But the stigma hypothesis is subject to some indirect testing. All the families in truly terrible financial shape should still be filing for bankruptcy.[13] If, however, stigma has declined, the bankruptcy filings should be augmented by the addition of many more filers who have less debt and might be capable of repaying if only they had the self-discipline, moral rectitude or old fashioned grit to settle down and make their payments.

The data from three surveys, each a decade apart, will reveal that the families filing for bankruptcy today are actually in worse financial shape than in the previous two decades, with no statistical sign of the supposed newcomers who come too easily or too quickly to the cleansing waters of bankruptcy. In light of this blow to the stigma-decline theory, we explore other explanations consistent with the data, including the possibility that the shame associated with filing for bankruptcy has actually increased.

Background—Three Studies

The Consumer Bankruptcy Study consists of three large studies we have done of natural persons filing bankruptcy in Chapter 7 or Chapter 13 in 1981, 1991, and 2001. The methodological details we have followed in our three studies are set forth in two books and a recent article.[14] In summary, we coded information on income, assets, and

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Bankr. Dev. J. 361, 390 (2004) (views of Official Receivers in Israel); Abuse, *supra* note xx. *See generally*, *Global Perspective*, *supra* note xx.

[12] Note that we did not have data for education levels in the 1981 study.

[13] It is important to keep in mind that most of the people in bankruptcy, like most Americans, are members of families that share their financial plight. *See* Elizabeth Warren, *Bankrupt Children,* 86 Minn. L. Rev. 1003 (2002); Teresa A. Sullivan, Elizabeth Warren, & Jay Lawrence Westbrook, *Bankruptcy and the Family*, 21 Marriage & Family Review 193 (1995) [republished in Families and Law 193 (Lisa J. McIntype & Marvin B. Sussman eds. 1995)].

[14] 1981 Dataset: Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, AS WE FORGIVE OUR DEBTORS; BANKRUPTCY AND CONSUMER CREDIT IN AMERICA 342 (1989); 1991 Dataset: Teresa A.

debts from bankruptcy court records in each study. In 1991 and 2001, we also gathered written questionnaires from debtors. In 2001 we conducted telephone interviews with bankrupt debtors. In 1981, we supplemented our data by interviewing bankruptcy judges and bankruptcy lawyers. The central core of financial information reported in this article comes from the schedules filed with the court. Questionnaires used in 1991 and 2001 provide the primary basis for the demographic (or social) data reported in this article, including information concerning gender, education, and occupation. Telephone interview data have not been included in this report. [15]

Although these studies were not national in scope, each of them involved a number of federal districts and an average of 150 cases per district. The financial information was collected from all the federal districts in three states—Texas, Illinois, and Pennsylvania—in 1981. For 1991 cases, we collected financial information from one district in each of those states, plus one district from our other two sample states for that year, California and Tennessee. The 2001 financial data were drawn from the same districts, except that we sampled the Northern District of Texas instead of the Western District[16] While the financial data are subject to the vagaries of self-reporting, they were filed under penalty of penalty and at the risk of loss of discharge for material untruths. The samples were drawn systematically in each year, with the caveats noted in our more detailed reports.

The questionnaires in 1991 were distributed to debtors who filed bankruptcy during the first two quarters of 1991 in each of the districts in Illinois, Pennsylvania, Texas, and California, and two districts in Tennessee. With the cooperation of the United States Trustee's Office, individuals filing bankruptcy under Chapter 7 or Chapter 13 in these sixteen federal judicial districts were asked to complete a questionnaire that provided information on age, education, occupation, marital status, race or ethnicity, and citizenship. The questionnaire was modeled in part on the 1990 United States Census questionnaire, and was available in both English and Spanish language versions. Debtors were advised that completion of the form was voluntary and that their responses would be confidential. Our report of the data from those questionnaires is based upon a systematic sample of about 150 cases from each district.[17]

The 2001 questionnaires were distributed to a sample of bankrupt debtors in much the same way as in 1991, except that 250 questionnaires were obtained for each of the

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Sullivan, Elizabeth Warren, & Jay Lawrence Westbrook, THE FRAGILE MIDDLE CLASS; AMERICANS IN DEBT 263 (2000); 2001 Dataset: David U. Himmelstein, Elizabeth Warren, Steffie Woolhandler, & Deborah Thorne, Illness and Injury as Contributors to Bankruptcy 2-3 Cite?? (2005).

[15] Two of us, with other co-authors, conducted an additional study in 1999, but those data are not reported here. *See* Melissa B. Jacoby, Teresa A. Sullivan, & Elizabeth Warren, *Rethinking the Debates over Health Care Financing: Evidence from the Bankruptcy Courts*, 76 N.Y.U. L. Rev. 375, 386-391 (2001). One of us has co-authored additional reports on the 2001 data. CR Illness and Injury

[16] The districts sampled in both 1991 and 2001 were Central California, Middle Tennessee, Eastern Pennsylvania, Northern Illinois.

[17] In general, we noted in our report of the 1991 data that some of the information may have been affected by the active and effective work of Philadelphia legal services in the Eastern District of Pennsylvania. Unfortunately, spending cutbacks had reduced that source of bankruptcy assistance by 2001, so we believe that this possible bias was eliminated in 2001. *See* FMC at 278-29.

five districts for which financial information was gathered. The 2001 data collection was completed in the first half of the year, well before the terrorist attacks of September 11.

We have adjusted all the figures in text and tables to 2001 dollars unless otherwise indicated.[18]

I. Two Decades of Bankruptcy Debtors

We first outline the basic financial characteristics of the consumer debtors at three points in the last 20 years: 1981, 1991, and 2001. We lay out the data as to their incomes, assets, and debts, reporting the changes in each of these financial characteristics over that time. The basic numbers are found in Appendix I. These figures are important themselves. When combined, they are useful as indicators of ability to pay. That is especially true of the debt-income ratio of the debtors, which remains the best overall evidence of their ability to pay.

Income: Still Low

Income is a likely place to see any important change. The income picture for the families who file for bankruptcy has remained oppressively grim over the past twenty years. From 1981 to 1991, median household income of families in bankruptcy dropped by nearly 20 percent. From 1991 to 2001, income remained low, statistically unchanged across the decade.[19]

Figure 1: Median Incomes, Families in Bankruptcy 1981, 1991, 2001

The debtors in bankruptcy have always had incomes below those of the households in the population generally.[20] The difference is that over the past twenty years, the gap has widened between the median household in bankruptcy and the median

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[18] We used the Bureau of Labor Statistics inflation adjuster which is based on the Consumer Price Index http://www.bls.gov/bls/inflation.htm (site last visited 10/1905).

[19] There is a shift in the measurement tools across the three time periods. In 1981, there was no Schedule I with the family's current annual income. Instead, only Form 7, listing income for the preceding two years, was available. By 1991, Schedule I had been added. Because it is current, it is likely to be a more accurate and immediate statement of the household's income, so it is the source we use for 1991 and 2001. It is also the case that Schedule I is more likely to be completed in detail. In 1991, none of the 650 court records reviewed were missing information on Schedule I, and in 2001 only 16 of 1250 court records reviewed in the core sample were missing these data. This compares very favorably with 1981 Form 7 data, in which 213 out of 1,557 debtors left blank the Form 7 income data. In 2001, Form 7 data were missing in 173 cases.

It is possible that the difference between the 1981 income reports and those that follow are the result of the change in measurement form, switching from Form 7 to Schedule I information. When we compare 1981 Form 7 data to 2001 Form 7 data, however, the same drop in income reappears, suggesting that incomes have remained low across the twenty year period.

[20] *See* Culhane and White, *supra* note xx, at Table 8. Their income figures are even lower than ours. They did not sample the same districts as we did.

The claim of statistical significance in the text is supported by the footnotes to Appendix Table 1, which report the results of tests of significance.

household in the U.S. In 1981, the difference was relatively small: the median debtor's household income was about 82.2 percent of the median in the U.S. generally, $35,478 across the country compared to $29,167 for those in bankruptcy (both figures in 2001 dollars).[21] By 2001, median income in the U.S. was $42,228 among all households,[22] while the households in bankruptcy reported a median income of $24,406—about 57.8 percent of the U.S. median income. As measured by income, the families in bankruptcy fell further behind their counterparts in the population generally.[23]

The proportion of debtors with extremely low incomes also increased during the past two decades. In 1981, about 24 percent of debtors had incomes that placed them below the then-current poverty line. By 2001, 30.6 percent were below the poverty line at the time of filing.[24]

Interestingly, the proportion of debtors sandwiched between the poverty level and the median income in the United States has remained relatively constant over twenty years, constituting about half of all debtors. The difference over twenty years is a shift among the debtors such that a smaller percentage of them earn more than the national median income and more are now below the poverty line income. Figure 3 illustrates the relative decline in the proportion of debtors with incomes above the median and the rise among those below the poverty line.

Figure 2: Proportion of Bankrupt Families with Incomes Below US Median, US Poverty, 1981, 1991, 2001

We gather social data as well as financial figures. The 2001 debtors, like those we studied in 1981 and 1991, are not the chronically poor. Their relatively high educational levels, high occupational prestige scores, and high rates of homeownership strongly indicate that these families are among the solidly middle class—at least when measured by something other than their current incomes.[25] The single most frequently

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[21] All of the dollar amounts reported in this article are adjusted for inflation to 2001 dollars. Median income in 1981 throughout the U.S. was $46,000 ($19,074 nominal dollars); in 1991 it was $39,000 in 2001 dollars ($30,126 in nominal dollars).

[22] Cite median income data.

[23] Another way to describe this same phenomenon: In 1981, 78 percent of debtors had incomes below the U.S. median, but by 2001, 84 percent of those in bankruptcy had incomes under that level. .

[24] The poverty levels for a family of four in 1981 and 2001 in 2001 dollars were $17,975 ($9,218 in nominal dollars) and $17,960. U.S. Census Bureau, Current Population Survey, Poverty Thresholds by Size of Family and Number of Children, http://www.census.gov/hhes/poverty/threshld.html (last consulted October 19, 2005). Information on the definition of the poverty line is available at http://www.census.gov/hhes/www/poverty/povdef.html (last consulted October 19, 2005).

[25] Among the debtors filing for bankruptcy in 2001, 91.8 percent had been to college, had an occupation in the upper 80 percent of all occupations (as ranked by prestige), or had bought a home. "Two-thirds of the cases (66.6 percent) met two or more criteria, with nearly three in ten —27.4 percent—meeting all three criteria. The data do not separate the middle class from an elite upper class, but they do suggest that the debtors are not concentrated among the chronically poor." Warren, *Financial Collapse and Class Status: Who Goes Bankrupt?* (Lewtas Lecture), 41 Osgoode Hall Law Review 115, 150 (2003). [Bad cite. Liz, please help] Although we had more detailed data in our analysis of families filing bankruptcy in 2001, the conclusion that they are drawn largely from the middle class rather than the chronically poor is an idea we developed in both As We Forgive Our Debtors and The Fragile Middle Class and supported with the

reason for filing bankruptcy most often cited in response to our questionnaires is an income interruption, typically a layoff, cutback or failed small business.[26] The lower incomes of the families at the time they file for bankruptcy are consistent with the picture of middle class families who are filing for bankruptcy after a substantial decline in income. Whether they will someday recover their former economic positions or whether bankruptcy is only a way-station in a continued decline is beyond the scope of the data we report here.

Assets—Trying to Protect the Home

Income alone does not peg a family financially. Other things being equal, a family with substantial accumulated assets can withstand an economic blow better than its counterparts with few assets. In the bankruptcy sample, total assets have risen over the past two decades even after adjustment for inflation. Total median assets were about $27,300 in 1981, dropping to $18,300 in 1991, and rising sharply to $37,000 in 2001. As figure 4 illustrates, when families file for bankruptcy now, they are clearly bringing with them more assets than they brought a generation ago, largely because of an increase in home values. If one looked merely to assets, these families would appear much better off.

Figure 3: Median Assets of Bankrupt Families, 1981, 1991, 2001

The single biggest asset for families in bankruptcy—like the single biggest asset for families not in bankruptcy—is their homes. About half the families in bankruptcy are homeowners, which means that the distribution of assets is really a two-tiered grouping with homeowners owning substantially more assets than their non-home-owning counterparts.[27] The proportion of bankrupt debtors in 2001 who are homeowners is about the same as that in 1981.[28] As the data below suggests, the rise in total asset value is in

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available evidence for the 1981 and 1991 samples. *See* Teresa A. Sullivan, Elizabeth Warren, & Jay Lawrence Westbrook, THE FRAGILE MIDDLE CLASS 27-59 (2000).

[26] FMC; other authors?

[27] Cite and elaboration. of filing, even though their court records listed no home and no home mortgage. Because these questionnaire and phone survey data were available for the first time in 2001, it is not possible to compare underreporting in 2001 with possible underreporting in earlier years. *See generally*, Raisa Bahchieva, Susan Wachter, Elizabeth Warren, *Mortgage Debt, Bankruptcy, and the Sustainability of Homeownership* in XXXX. Culhane and White report a much lower rate of homeownership, about 30%.

[28] It is possible that the homeownership rates have remained fairly stable over time. Using the court record data only, we reported an estimated homeownership rate of about 52 percent for the families filing for bankruptcy in 1981. *As We Forgive Our Debtors*, supra note xx, at 129. This report is remarkably quite close to the 2001 report of 52.5 percent homeowners.

The 1991 data, however, show a drop in homeownership figures. In *Fragile Middle Class*, supra note xx, we speculated that the reported proportion of homeowners in bankruptcy in 1991 was understated in part because the homeownership rate in one of our sample districts, the Central District of Los Angeles was quite low. In Los Angeles in 1991, housing prices were quite high, making it likely that families' mortgages were also quite high. Perhaps because high mortgages made the debtors ineligible for Chapter 13 to try to work out a payment plan with their lenders. Such families, we speculated, might be in Chapter 11 or out of the bankruptcy system altogether. For a more detailed explanation of the 1991 differences

substantial part the consequence of a rise in the value of homes, both for those in bankruptcy and those not in bankruptcy, coupled with a small rise in the value of other assets for those in bankruptcy.[29]

Homeowners are filing for bankruptcy with more valuable homes. In 2001 dollars, the median, inflation-adjusted value of homes for families in bankruptcy moved from $68,250 in 1981 to a statistically indistinguishable $67,275 in 1991 and then soared to $90,000 in 2001. The increase among the 2001debtors is statistically significant.

Inflation adjustment is a good way to be certain that dollar comparisons across time are meaningful. Increases in home values have far outpaced inflation, so we compare the median home value of the family in bankruptcy with the median home value in the U.S. in the same year. In 1981, a median family in bankruptcy owed a home that was worth 53.8 percent of the value of a median home in the U.S. In 1991, that proportion was nearly identical at 53.3 percent. By 2001, the median value of the home of a bankrupt family was worth only 60.9% of the value of a median priced home in the U.S., well-below the general population of homeowners, but relatively higher than the home values of bankrupt families in 1991.[30]

Figure 4 Median Value of Homes Owned by Families in Bankruptcy
Relative to Median Price of Homes in US Generally

Of course, families own more than their homes. They have cars, furniture, clothes, appliances, cash, pets, and other liquid and ill-liquid items they might cash out to pay their debts. In 2001 dollars, families filing for bankruptcy over the past two decades showed a decline in non-real estate assets from 1981 to 1991, from $8,375 to $6,074. In 2001, median non-home assets rose to $9,657. The total value of the non-real estate assets of bankrupt families—from cars to kids' shoes—remains below $10,000 throughout the twenty-year period.[31]

We deal with debt in some detail in the next section. It is worth pausing here, however, to talk about the combined asset/debt picture. Assets are a family's wealth, but the asset/debt picture explains the family's overall net worth. Here the comparison of median assets to median total debt demonstrates the difficulties facing families in bankruptcy. In 1981, median debt divided by median assets was 1.5. That is, at the median, total debts outstripped total assets by one and a half times. By 2001, the ratio had risen to 1.8, meaning that the rise in assets had been outstripped by an even larger rise in total debt.

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among districts, see *Fragile Middle Class*, supra note xx, at 347-38, note 24-28. We estimated that actual homeownership rates in 1991 might have been closer to 50 percent. *Id*. at 204-05.

[29] The data on homeownership is too complex and interesting to summarize here, but two exemplary data are illustrative. Among 2001 bankrupt homeowners as a group, 74% of their assets consist of the value of their homes. Second, again on an overall basis, 2001 home values are 291% of 1981 home values after adjusting for inflation.

[30] However, the ratio of mortgages to home values has not changed significantly over the two decades we have studied.

[31] This datum comes from a separate calculation.

The most crucial point, however, is the amount of debt directly related to assets by virtue of a security interest or lien in favor of a creditor. In 1981, the mean ratio of secured debt to assets was .68. That is, a hypothetical mean, family was likely to have about 68 percent of its total assets locked up by security interests. In 2001, the mean ratio of secured debt to assets was a statistically indistinguishable .69. Therefore, in both years, on a gross measurement,[32] only 32% of the value of the debtors' assets would be available for creditors, even if there were no exemptions.[33]

The asset picture overall shows that assets have risen for the families in bankruptcy, largely because homeowners now come into bankruptcy with somewhat more valuable homes. When debts figure into the picture, their apparent economic gains turn to losses.

Debts—Owing More Than Ever

The third leg to the financial stool is debt. The 2001 data show that at the time they file for bankruptcy the debtors have substantially larger debt loads than in the previous years. Median total debt loads are up an enormous 55.9 percent from 1981 in inflation adjusted dollars. This seems to be a rise that occurred mostly during the 1990s; 1981 and 1991 mean debt loads were statistically indistinguishable from each other, with the climb occurring from 1991 to 2001.[34]

Figure 5: Median Total Debts, Families in Bankruptcy, 1981, 1991, 2001

Of course, total debt figures have a mix of debts—from home mortgages to payday loans. An overall increase can be driven from either side of the secured/unsecured divide. Higher secured debt loads are consistent with greater assets and with the increase in the number of homeowners compared with the 1991 sample.

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[32] This measurement is only roughly correct, because it does not take the value of each item of collateral and compare it to any lien securing it.

[33] All states exempt at least some property from seizure by creditors and therefore protect that property in bankruptcy. Cite Colliers on Bankruptcy¶. Typical examples would be homes (except for mortgages, taxes, and improvement liens), cars, and tools of the debtor's trade. Almost all consumer bankruptcies are "no asset" cases, with nothing available to be sold to pay creditors, primarily because of security interests, taxes, and exemptions. Michael J. Herbert & Domenic E. Pacitti, *Down and Out in Richmond, Virginia: The Distribution of Assets in Chapter 7 Bankruptcy Proceedings Closed in 1984-1987*, 22 Rich. L. Rev. 303, 315-16 (1988); U.S. General Accounting Office, Report to the Chairman, Comm. on the Judiciary, House of Representatives, Bankruptcy Reform Act of 1978: A Before and After Look 56-57 (1983) (reporting that 97% of Chapter 7 cases had no assets for distribution to creditors).

[34] We often cite median values when they seem more reflective of the question being asked, but of course determination if two sets of values are different to a statistically significant extent requires comparison of means. The increase in mean debt (in 2001 dollars) from 1981 to 2001 was 21%. *See* App. Table 1. We should note that the somewhat odd relationship between means and medians in Figure 6 is not anomalous. The two have no necessary relationship.

Overall, secured debt totals showed a jump consistent with the increase in total debt loads, increasing 36.3 percent from 1981 to 2001.[35]

Like all other Americans, the debtors who found their way to the bankruptcy courts had also been the recipients of staggering amounts of credit offered on an unsecured basis. Mean unsecured debt leapt 48.9 percent from 1981 to 2001, although median unsecured debt—held down by those families who owed little to anyone other than their secured debts to a home mortgage company or car lender—increased at a more modest 19.9 percent. Mean unsecured debt showed a consistent rise throughout the twenty year period.

Debt-to-Income Ratios—The Best Measure of Indebtedness

Perhaps the best measure of a family's financial distress is its debt-to-income ratio. A family may earn a substantial amount, but if it owes even more, it may be in worse shape than a family with a lower income but little debt.[36] The debt-to-income ratio measures, on a debtor-by-debtor basis, the families' financial situation when they filed for bankruptcy.

The debt-to-income ratio has a statistical quirk of some importance. Because the rules of basic arithmetic apply in bankruptcy just as they do elsewhere, it is not possible to divide by zero. This means that a family with a substantial debt load and no current income has an incalculable debt-to-income ratio. There are two ways to deal with these zero-income families: either impute a low fictional income so that some calculation is possible or omit them from the analysis. We omitted the families, believing that any imputed income was likely to be wide of the mark in describing that family's circumstances.[37] But by omitting the zero-income families, we necessarily take the families in the very worst economic circumstances out of the calculation. In effect, we make the bankrupt families appear, as a group, more able to pay than they are.

With incomes flat or declining among the families in bankruptcy and debt rising, the change in debt-to-income ratios is predictable. By 2001, the total debt-to-income ratio for the families in bankruptcy is, at the median, 2.3. This means that the median family in bankruptcy owes debts equal to more than two years and four months of

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[35] The data from 1991 had actually shown a decline in the amount of secured debt outstanding—consistent with a decline in the proportion of homeowners in the sample—so that the rebound in secured debt from 1991 to 2001 is even more remarkable—an 88.5 percent jump in just ten years.

[36] The recent bankruptcies of actor Burt Reynolds, *Penthouse* publisher Bob Guccione, and prize fighter Mike Tyson, and director Peter Bogdanovich exemplify this point. For other examples, see http://www.bankruptcy-usa.info/famous-bankruptcies.html (last consulted October 21, 2005).

[37] Zero-income and missing income are not the same. In all cases, forms that are missing data are not included in the calculations. So, for example, someone who simply left blank Schedule I report on income is listed as "missing" on the tables and excluded from all the mean, median, standard deviation and other calculations. Someone who affirmatively listed "zero" as the amount of income, however, has been included in all income analyses up to this point, but is excluded from the debt-to-income ratio calculations for the reasons explained in the text.

income. The mean ratio is an even more staggering 4.6, meaning that the average debts of a bankrupt family are equivalent to more than four-and-a-half year's of total family income.

Figure 6: Median Total Debt-to-Income Ratios, 1981-2001

However, total debt-to-income ratios are not the full picture. They include all debt, which means that the past-due doctor's bill, which is due in full right now, and the mortgage debt, which is to be paid out over the next twenty years, are included in the same calculation. Using this calculation makes the immediacy of the debt irrelevant. Of course, to a family trying to make its regular payments, when the bill is due is not irrelevant. In order to get a truer picture, we also calculate nonmortgage debt-to-income ratios, excluding all mortgage debt on the theory that mortgages are set up for some longer time payment period and not all due immediately (assuming the family is not in foreclosure.) Excluding these long-term debts from the debt-income calculation does not remove them from the family's budget. The debtors must still make the monthly payments or face losing their home. Thus each comparison—total debt as compared to income and nonmortgage debt-to-income—portrays an aspect of the family's financial position and the two together triangulate it.

Figure 7: Median Non-Mortgage Debt-to-Income Ratios, 1981-2001

The non-mortgage debt-to-income ratio makes clear the urgent problems facing the typical debtor. Non-mortgage debt-to-income ratios for the families in bankruptcy has taken a sharp jump from 1981 to 2001. Median non-mortgage debt in 1981 was 80% of annual income, which meant that the family owed 9.6 months' income in short-term debt. By 2001, the ratio had ballooned to 1.17, which means that the median family now owed credit cards, car loans, utility bills, and other non-mortgage debts that equaled 14 months of their total income. To put these figures in perspective, in 2001 it would take the median family more than a year to pay off their unsecured, mostly short-term debts, *even if* somehow interest stopped running, they applied all their income to principal payments, and someone else paid their rent and bought their food, gas, and the other necessities of life.[38]

About half of the total non-mortgage debt is identifiable as credit card debt.[39] The remainder is a potpourri of car loans, payday loans, bank overdrafts, past-due utility payments, and other debts. The car loans would be payable over somewhat longer terms, but the terms are highly variable. As to the credit cards, while the credit card companies

[38] Mean short-term debt-income ratios, inflated by the wretched circumstances of some of the people most indebted in relation to their incomes, were bad in both time periods, running at more than two years' income for the bankrupt families.

[39] In 2001, the median ratio of credit card debt to total non-mortgage debt on a debtor-by-debtor basis was .49, while the mean was a somewhat higher .54. *See also*, Ed Flynn & Gordon Bermant, *Credit Card Debt in Chapter 7 Cases*, Am. Bankr. I. J. 20, December/January 2004. That article, like other reports from the Executive Office of the United States Trustee, is much appreciated, but does not provide details of sample selection, medians and standard deviations, and the like, so we cannot compare it very usefully to our data or the data from other studies.

are usually glad to accept those low, minimum monthly payments, the interest rates are often ruinous for a family with substantial credit card debt. The combination of late fees, over-limit fees, default rates of interest, and other charges mean that credit cards for families in trouble may easily be running at 24 percent interest or more.[40]

Credit card debt has become a dominant form of lending in recent years, and it has characteristics that make it quite different from traditional consumer loans.[41] The credit is granted over long periods of time without additional credit checks and it is used incrementally rather than being borrowed in one sobering moment, offering a chance to go broke one pizza at a time. At the extreme, nearly one in five debtors in 2001—21.8 percent—owe more than a year's income in credit card debt alone. In absolute dollar terms, the amounts are remarkable. More than half (56.2%) of all the families owe more than $10,000 in credit card debt at the time they file for bankruptcy. Many owe much more: More than a third (34.6%) owe more than $20,000 in credit card debt. For families with our sample's median income of about $24,000, a credit card debt of $10,000 likely means the family would have to hand over ten percent of every paycheck to the credit card companies just to stay even—that is, interest only—without paying down a single dollar of debt.[42] For the third of the debtors who owe $20,000, interest only payments would amount to twenty percent—or every fifth paycheck.

The middle-class families who filed for bankruptcy in 2001 are in even worse financial trouble than those who filed during the prior twenty years. While their income and assets are greater, they are burdened with far more debt than their predecessors.

With these data in hand, we will be able to analyze the changes wrought by the 2005 consumer amendments. Will bankruptcy rates decline, as the supporters of the amendments hoped? If so, will it be the best-able-to-pay debtors who cease to file or will exclusion rest on some entirely different factor, such as local legal culture or access to legal services? These are two among many questions that will be addressed with these data as a baseline.

The Disappearing-Stigma Hypothesis[43]

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[40] See note xx *infra*.

[41] FRAGILE MIDDLE CLASS, supra note xx, at 109-40, 245-50.

[42] The calculation is based on a $2,000 a month take-home pay and a 24% annual interest payment to the credit card companies after default, for a monthly interest payment of $200 on $10,000 debt and $400 on $20,000 debt. Typical default rates of interest charged sub-prime customers are in the 24 to 36 percent range, plus monthly over-limit and late-fee charges. A recent Supreme Court decision means that the various charges do not have to be disclosed to consumers as part of the finance charge. *See* Household Credit Services, Inc., v. Pfennig, 541 U.S. 232 (2004).

[43] Aside from the debates we discuss in this article, there are a number of entirely theoretical articles that make arguments about the bad effects of existing consumer bankruptcy law. *See, e.g.,* Barry Adler, Ben Polak, & Alan Schwartz, *Regulating Consumer Bankruptcy: A Theoretical Inquiry*, XX J. Leg. Stud. 585 (2000) (arguing, *inter alia*, that lenient bankruptcy laws reduce efficiency by reducing work incentives). We do not address these approaches in this article, awaiting some factual support for their assertions.

The question of stigma has always been a part of bankruptcy laws. In European countries in the sixteenth and seventeenth centuries, one declaring bankruptcy was required to engage in humiliating public behavior. The law in Padua is illustrative. The bankrupt was required to appear naked or nearly naked in the "vast Paduan Palace of Justice" and to slap his buttocks three times against the "rock of shame" while proclaiming, "I DECLARE BANKRUPTCY."[44] It appears the reason for this requirement was a concern that bankruptcy might otherwise involve too little stigma. In any event, this bit of history illustrates the point that stigma as a element of deterrence or sanction has long been associated with bankruptcy. The traditional notion in many societies is that bankruptcy is, and should be, shameful.

For this paper, we consider that the stigma of bankruptcy means a cost associated with filing for bankruptcy based on injury to reputation or violation of moral standards. Jane and John may decide not to enjoy the benefits of bankruptcy relief because they believe that they will suffer reputational loss (for example, because they will be labeled as failures) or because they believe it is morally wrong not to pay debts.[45] Only the first of these is really a question of "stigma" based on the perceptions of others, but for the sake of clarity, and with reference to the public debate, we will refer to the cost arising from either belief as a stigma cost. The reduced-stigma hypothesis rests on the belief that modern Americans read about Kim Bassinger and or the rock group TLC going into bankruptcy (or former Texas Governor John Connally) and conclude that filing for bankruptcy is no longer such a despised or wrongful thing to do.[46]

The hypothesis that we put to the test in this article is that the great increase in consumer bankruptcy filings over the last 20 years has been largely a function of the decline in stigma.[47] As the number of families who file for bankruptcy has doubled and doubled again over the past two decades, the drumbeat to "tighten" the bankruptcy laws has grown ever louder. The premise behind the call for a change in bankruptcy laws has been that those who are filing for bankruptcy are somehow different from their

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[44] James Q. Whitman, *The Moral Menace of Roman Law and the Making of Commerce: Some Dutch Evidence*, 105 Yale L.J. 1841, 1874 at n. 115 (1996) (citing an Italian lawyer of the Sixteenth Century).

[45] Of course, reputational loss may involve the moral issue as well, if potential filers believe that others will view their filing for bankruptcy as a moral failure. E. Goffman, STIGMA: NOTES ON THE MANAGEMENT OF SPOILED IDENTITY (1963) is the classical analysis of the social effects of stigma. As to bankruptcy, *see* Deborah K. Thorne, *Personal Bankruptcy Through the Eyes of the Stigmatized: Insight into Issues of shame, Gender, and Marital Discord,* unpublished Ph.D. dissertation, Washington State University (2001) (showing that some bankrupt debtors delayed filing because of shame; others tried to keep their bankruptcies secret from families, employers, and others).

[46] If stigma has indeed declined, elements in the credit industry may have contributed substantially to the decline. The billboard on a main street in Austin, Texas, that said "BAD DEBT? BANKRUPTCY? No Problem! Car Loans, call 1-800-XXXXXXX" told Jane and Billy Bob very clearly that bankruptcy is not such a terrible thing with awful consequences. See CR *infra*. Possibly Jane and Billy Bob have also concluded that major airlines and other firms that have declared bankruptcy have suffered only negligible reputational loss.

[47] *See, e.g.,* Jones & Zywicki, *supra* note xx, at n. 149, citing F.H. Buckley & Margaret F. Brinig, *The Bankruptcy Puzzle*, 27 J. Legal Stud. 187, 194 (1998) (high divorce rates in part show decline in bankruptcy stigma indirectly as decline of stigma of promise-breaking) ; Fay, Hurst & White, *supra* note xx.

counterparts twenty years ago. The claim advanced by some in Congress is explicit: the rise in bankruptcy filings is fueled by a new kind of debtor who takes a "bankruptcy of convenience" rather than buckling down and trying harder to repay.[48]

As noted earlier, the debates about consumer bankruptcy in the United States have been driven by the great increase in bankruptcy filings since the adoption of the Bankruptcy Code in 1978. Of course, there would have been some increase in bankruptcy filings as a result of simple population growth,[49] but the increases in bankruptcy filings are much greater. In 1981, there were about 3.6 bankruptcy filings for every thousand households in the U.S.[50] If the filing rate prevalent in 1981 had remained steady, the number of bankruptcy filings in 2001 would have been about 387,000 rather than 1.4 million. Across the twenty year period from 1981 to 2001, bankruptcy filings would have looked like those projected on the lower line below:

Figure 8: Bankruptcy Filings Per 1000 Households, Actual and Projected, 1980-2002

In fact, bankruptcy filings grew at a much faster pace. By 2001, there were 13.8 bankruptcy filings for each 1,000 households. Obviously something has changed to make it more likely that families will declare bankruptcy. If changes in stigma alone were to account for the higher rate of bankruptcy filings, then nearly twelve million filings over the past two decades could be chalked up to changes in moral standards. If just half of the increased filings were the result of changing attitudes, it would represent a sea change in American attitudes in a very short period.

Of course, there are plausible reasons other than stigma for the increase in filings. For example, there might be many more people in financial difficulty in 1991 and still more in 2001. Thus increased filings would be a product of more widespread financial trouble, just as hospital admissions would be expected to rise in a time of epidemic. If that were true, we would expect to find that the persons in bankruptcy were in financial difficulty equally great or even greater than those in the earlier years.[51] The fact that Americans' burden of debts compared to their disposable incomes had risen considerably from 1991 to 2001 would support such a hypothesis.[52] There may be other contributing factors, including increased layoffs, high divorce rates, lack of medical insurance, and rising housing costs.[53] While we do not explore these particular explanations further in this paper, they illustrate the fact that stigma is only one of the possible causes of the

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[48] *See, e.g.,* http://commdocs.house.gov/committees/judiciary/hju61368.000/hju61368_0.htm (statements by Representative Gekas and Senator Grassley; Senator Grassley says explicitly that stigma has disappeared).

[49] From 1981 to 2001, the number of households in the country increased from 82,368,000 to 108,209,000. Bureau of the Census, U.S. Department of the Commerce, Statistical Abstract,pp cite

[50] To be more precise, the filing rate was .003578.

[51] *See* Elizabeth Warren, *The Bankruptcy Crisis*, 73 Ind. L.J. 1079, 1083 (1998).

[52] Donald E. Powell, *The Condition of the Banking Industry,* at 4, Senate Committee on Banking, Housing, and Urban Affairs, April 20, 2004 (Chairman, FDIC) (total household debt at 112 percent of disposable income is historical high) [hereafter "FDIC testimony"]. *See also* Warren, *supra* note xx, at 1083 and authorities there cited;

[53] *See* Teresa A. Sullivan, Elizabeth Warren & Jay L.Westbrook, THE FRAGILE MIDDLE CLASS: AMERICANS IN DEBT (2000) [hereinafter FRAGILE].

dramatic increase in consumer bankruptcy filings over each of the last two decades, especially the last one.

By contrast, if declining stigma accounts for the dramatic increase in the rate of bankruptcy filings, we would expect to see a change in the financial circumstances of those who file today. That is, the reduced-stigma hypothesis must postulate that some sorts of persons in financial difficulty who did not file bankruptcy in 1981 did file in 1991 and that even more such persons filed in 2001. It assumes that the persons who decided not to file in the earlier years were deterred by the prospect of the reputational loss or moral constraint one may describe as stigma. In an earlier year, they regarded stigma cost as exceeding the benefits of bankruptcy relief.[54] We may call them "stigma-deterred" classes of persons. If the missing-stigma hypothesis were correct, in more recent years many of the stigma-deterred would have perceived a reduction in reputational costs and have chosen to file, thus swelling the ranks of the bankrupt.

From a financial perspective, we may hypothesize three categories of stigma-deterred classes. One would be those who are much less financially burdened than the typical bankrupt. More of them would file each year because they would believe the benefits of bankruptcy exceed the lowered costs of stigma. This class is presumably the one that critics have most in mind when they claim bankruptcy's stigma costs have fallen sharply, increasing the number of filings. The second class of the stigma-deterred would consist of persons just as financially burdened as the typical bankrupt, but who viewed the stigma of filing as too costly in 1981 or 1991. Again, the stigma hypothesis is that more of them would be filing in 2001. The third class would include those who are much more burdened financially than the typical bankrupt, but who nonetheless refused to file previously because they viewed the stigma loss as extremely costly. We may call them the rather-be-dead-than-bankrupt persons.

If an increased willingness to file is found in the first group, the less burdened debtors, then mathematically it should be that the overall financial circumstances of the debtors in bankruptcy in 2001 will be better than in 1991 and in 1991 better than in 1981. There are various tests that might be applied to see if the data support the hypothesis that more persons in this first class are filing bankruptcy because of declining stigma, but we will suggest that the ratio between the debtors' debts and their incomes is the most cogent test to apply.[55] Thus if fewer persons in this group are deterred by stigma, then debt-income ratios of the group as a whole would be lower (less debt as compared to income).

If there are more people filing who are in the second class of the stigma-deterred, the people who are similar to typical bankrupts, then by the same logic the debt-income ratios of bankrupts as a whole should stay about the same. There would simply be more

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[54] It should be noted that there is no reason to think that the benefits of bankruptcy relief increased from 1981 to 2001. Indeed, if anything, those benefits may have been reduced, especially by the 1984 amendments to the Bankruptcy Code. *See* Culhane & White, *Debt After Discharge: An Empirical Study of Reaffirmation*, 73 Am. Bankr. L.J. 709, 715-16 (1999).

[55] CR

people of about the same sort in the bankruptcy courts, because a smaller percentage of people in those financial circumstances would be deterred from filing by stigma.

Finally, if those who once would have been rather-be-dead-than-bankrupt have more recently become willing to file, then the data should show that bankrupts as a whole have worse mean and median debt-income ratios, dragged down by the worse ratios of these additional filers.[56]

As to normative conclusions, whether the possible expansion of filers in the second and third groups is good or bad, the reader can judge in looking at the data. That is, depending on one's economic and normative views, it might or might not be a bad thing that more of these heavily indebted debtors have chosen bankruptcy relief and the "fresh start." Some observers might see a greater willingness to file within these groups (that is, less stigma deterrence) as a positive development, because members of this group may have been mistaken previously in evaluating the costs to their families of not filing.[57] In any case, the thrust of the argument made by the proponents of the reduced-stigma hypothesis is that the first group—those better able to pay who did not file for bankruptcy in the past—represents the normatively troubling development.

The data presented here are strongly inconsistent with that claim. There is no evidence that the mix of families filing for bankruptcy today is more able to repay than were the bankrupt debtors of the good old days when bankruptcy filing rates were much lower. On the contrary, the data show that by a considerable margin they are actually in greater financial distress. There may be more bankrupts today with the same or worse financial problems than in the past, but there are not large numbers of bankrupts who are better off.

There remains the possibility that the overall numbers are masking the presence of the convenience bankrupts who could pay. There could be so many new filers who are even worse off than their predecessors that they make debtors as a whole worse off. To test that proposition, we examined the lowest (best-able-to-pay) decile of the 2001 sample. We chose 10% in part because the proponents of tougher bankruptcy laws have recently used the 10% figure as an estimate of those who would be forced to pay under the recently adopted amendments.[58] It also represented the outer limit of our estimate of the number of 1981 debtors who might be able to pay their debts at a high level of

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[56] Two caveats are in order. First, we emphasize these hypothesized classes are a necessary part of the stigma hypothesis, not various other explanations. Second, within the stigma hypothesis, there could be more elaborate distributions. Others can look at the distributions revealed by the figures and tables and consider other possibilities. We analyze the data overall and at the lowest or best-able-to-pay quartile of debtors. CR.

[57] Note e.g.?

[58] cite Our empirical data from 2001 suggest a much lower percentage who will be affected by the means test, a result broadly consistent with the Culhane and White study. Elizabeth Warren & Jay Lawrence Westbrook, THE LAW OF DEBTORS AND CREDITORS 161 (5th ed. 2005) (forthcoming).

hardship.[59] The results of our investigation of the lowest decile of 2001 debtors by ability to pay are found in Table XX.[60]

[Constructed table A for best able to pay goes about here.]

The most important finding is that over twenty years from 1981 to 2001 the debtors best able to pay looked very much the same in their burdens of nonmortgage debt, while their ratios of total debt to income got substantially worse. In 1981, the bankrupt debtors best able to pay owed an average of 5% of their annual incomes in nonmortage debt; in 2001 they owed a statistically indistinguishable 4% of a year's income. On the other hand, their ratios of annual income to their total debts got significantly worse: the average total debt/income ratio rose from 30% of their income to 64%

The debtors who were best able to pay in 2001 were at least as debt-burdened as the 1981 debtors who were best able to pay. These data are quite inconsistent with the missing-stigma hypothesis. They do not reveal the hypothesized cohort of convenience filers who would be willing to enter bankruptcy with lighter debt burdens because they are no longer troubled by the stigma imposed by bankruptcy in times past.

No data have been advanced to support the reduced-stigma hypothesis, beyond the increased number of bankruptcies. Indeed one of its principal proponents has provided perhaps the best available evidence to prove the negative, that bankruptcy has not lost its stigma. Professor Michelle White made a move that we had never been able to make, getting a question concerning bankruptcy added to the famous Panel Study of Income Dynamics, conducted by the University of Michigan.[61] Because that study represents a national sample thought to be fairly representative of the entire American population, its data are taken especially seriously. In a posted, but un unpublished paper reporting the results, she and her co-authors argue that reduced stigma is an important factor in increased bankruptcy filings.[62]

Yet in the data reported from the PSID bankruptcy question we find that the rate of bankruptcy admitted by the respondents in the panel sample is one half that of the

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[59] As We Forgive Our Debtors, *supra* note xx, at 212.

[60] Note that the two deciles consist mostly of different people. For example, in the 2001 sample only 11 debtors out of 120 were in the lowest (best-able-to-pay) deciles for both total and unsecured debt.

[61] "The Panel Study of Income Dynamics (PSID), begun in 1968, is a longitudinal study of a representative sample of U.S. individuals (men, women, and children) and the family units in which they reside. It emphasizes the dynamic aspects of economic and demographic behavior, but its content is broad, including sociological and psychological measures. As a consequence of low attrition rates and the success in following young adults as they form their own families and recontact efforts (of those declining an interview in prior years), the sample size has grown from 4,800 families in 1968 to more than 7,000 families in 2001. At the conclusion of 2003 data collection, the PSID will have collected information about more than 65,000 individuals spanning as much as 36 years of their lives." http://psidonline.isr.umich.edu/Guide/Overview.html (last consulted May 8, 2005). *See also*, Fay, Hurst, & White, *supra* note xx.

[62] *Id.*

actual nationwide filing rate.[63] Given that the panel is thought to be a representative sample, it would appear that *about half the panel respondents who had filed for bankruptcy lied about it to the panel investigators*. It would be hard to produce more concrete evidence that the stigma of bankruptcy, although perhaps lower than it was in Padua in the Sixteenth Century, remains quite robust in twenty-first century America.

Not all critics of current bankruptcy policy subscribe to the simple model put forth by Congress and the economists. The Honorable Edith Jones and Professor Todd Zywicki argue that bankruptcy filings have increased by the combination of two factors: permissive bankruptcy laws and reduced stigma.[64]

As to the second, the Jones-Zywicki missing-stigma argument moves the debate to another point in the debtors' financial lives. They do not look at these families at the moment when they are deciding whether to file for bankruptcy, but at an earlier time when they are deciding whether to incur debt. The claim is that the reduced stigma of filing bankruptcy influences people to charge irresponsibly, knowing they can file for bankruptcy to eliminate their debt with a lower reputational cost. Because this claim relates to pre-bankruptcy behavior, it cannot be fully tested with bankruptcy data. Yet some of our findings are inconsistent with it. The Jones-Zywicki account has people running up debts, then heading to bankruptcy when they feel overloaded. But that implies that bankruptcy should be an easier choice for everyone, including those in less trouble. The psychological ease of bankruptcy—a shift Jones and Zywicki say is strong enough to affect consumer buying years in advance of financial trouble—should be producing more filers with modest problems, as well as those filers with bigger problems.

The larger point to be made about the Jones-Zywicki hypothesis is that it is sheer speculation. There is strong empirical support for other explanations for the great increase in bankruptcy filings. As discussed earlier, the great increase in the ratio of debt to disposable income in recent years, persistent, large-scale layoffs, the widespread absence of health insurance, and other factors have been shown to bear a strong relationship to the increase in bankruptcy filings.[65] Given all these plausible explanations, supported by data, the proponents of the Jones-Zywicki hypothesis must produce some hard facts to support their claims. Until they do, it is hard to take them seriously. This field is not one of those where all the disputants may revel in abstract debate, unburdened by evidence. Careful empirical work has been done here, so that data are now the price of admission to the academic conversation.[66]

The data are consistent, however, with several other possibilities. As noted above, for example, the pool of American families with substantial burdens of debt has increased considerably in the last ten years (and had done so during the ten years before

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[63] Fay, Hurst, & White, at 21 (PSID filing rate is only half of the national filing rate).
[64] *See* It's Time, *supra* note xx.
[65] FRAGILE, *supra* note xx. See also Figure 9.
[66] Jay Lawrence Westbrook, *Empirical Research in Consumer Bankruptcy*, 80 Tex. L. Rev.2123 (2002). Of course, the price of admission to the political conversation may be much lower: a bullhorn or a campaign contribution.

that).[67] Thus the hospital might simply be admitting more, and sicker, people from a larger pool of illness. However, another hypothesis might also contribute to understanding these data: that families are trying harder than ever to stay out of bankruptcy and that they have more opportunities to try to do that. Among the possible explanations for such state of affairs are two of special interest. One is that stigma has actually increased, deterring a family from filing until it is in greater financial distress. A second is that the industry's change in credit practices has permitted debtors to become more indebted before filing for bankruptcy.

Increased stigma.

If debtors and their families are in more financial trouble before they file, then it is logical to infer that the non-financial pressures that might deter someone from filing may have grown over time. The obvious possibility—oddly ignored in the debate—is that it may be more painful for families to file for bankruptcy than ever before because the stigma of a bankruptcy filing has actually increased.

How could it be that stigma has increased? One possibility is the greatly increased likelihood that a bankruptcy filing will become public. While filing records have always been a matter of public record, the fact was that most people could file for bankruptcy secure in the knowledge that it would be difficult for a nosy neighbor or concerned family member to learn of the filing. Bankruptcy records were all on paper, typically behind the desk in a federal courthouse. While some local newspapers published local bankruptcy filings, most did not, and debtors in 1981 and 1991 could often slip in and out of bankruptcy with their secret safe.

In the age of the internet, bankruptcy filings have gone public. Try googling the name of your neighbors, and bankruptcy filings may appear along with wedding notices and real estate purchases. Some services advertise that they will tell paying customers about their neighbors—including the fact of their bankruptcies. Anyone in financial trouble in the Twenty-First Century must consider the much greater likelihood that there are no secrets any longer. For some people, such information could be a substantial deterrent to filing. Only when there was no hope of salvaging their financial lives without bankruptcy would some finally consider a bankruptcy option.

The new and well-publicized availability of a free annual credit report has also offered an opportunity for the credit bureaus to remind consumers of the importance of an individual's credit score.[68] Not only does the score affect whether a consumer gets credit and at what interest rate, but the score is also used by insurance companies to set premiums and it is used by landlords and employers to judge worthiness as a renter or employee. A substantially lowered score as a result of bankruptcy is a tangible type of stigma – not quite a scarlet letter A, but a quantitative measure of reputational loss.

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[67] CR

[68] Experian, one of the three major credit reporting services, advises consumers that their credit score can be used by a number of third parties, and Experian offers advice on raising one's score. http://www.experian.com/credit_score_basics/index.html (last consulted on October 20, 2005). Avoiding bankruptcy is a conspicuous piece of advice.

Stigma might also have increased as a result of the credit industry's relentless public relations campaign over the past decade. Beginning with its introduction of a bankruptcy bill in 1997, the industry has hired multiple public relations firms to drive home the message that deadbeats now populate the bankruptcy courts. One group of creditors organized an effort to proclaim bankruptcy to be a "ten-year mistake" to remind the consumer that a bankruptcy remains on their credit report for ten years. Consumers who searched the word "bankruptcy" on the internet would get a brightly colored banner that proclaimed bankruptcy to be a ten-year mistake and offered a web address with details. [69]

In 1981, someone considering bankruptcy was unlikely to have read a single story in a newspaper or magazine about families in bankruptcy because such stories were almost non-existent. Moreover, such a person would never have seen a full-page advertisement claiming that people filing for bankruptcy cost the rest of us $400 in costs passed along.[70] By 2001, someone considering bankruptcy would have been bombarded with stories. Many carry the repeated claims of senators and other luminaries that those in bankruptcy are cheaters and charlatans. Of course, many of the stories would have been deeply sympathetic, but even those stories might have given troubled families pause. The stories are so sympathetic—families with dying children and years of joblessness[71]—that someone merely three months behind on the mortgage and carrying a year's worth of short-term debt might think bankruptcy was for people with bigger problems.

On the other hand, as noted below, a portion of the credit industry avidly courts debtors who have been through bankruptcy, assuring them is it "no problem" when it comes to new loans. [72] It is hard to know which of the industry's messages is most resonant. This paper offers no direct measure of stigma, but anyone who wants to talk about a changing environment for the families who contemplate bankruptcy must at least consider the possibility that the environment has become more—not less—hostile to those who file. That is, given the widely acknowledged fact that the indebtedness of ordinary Americans has soared,[73] it is plausible that the increase in bankruptcy filings actually represents a smaller percentage of a larger pool of over-indebtedness, because a larger percentage of overindebted Americans are deterred from filing.

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[69] This marketing effort is described at http://bankrupt.com/TCR_Public/960906.MBX (last consulted October 21, 2005). Others have also picked up the term "ten-year mistake" in their consumer education. See, for example, Bellco Credit Union's admonition against bankruptcy. http://www.bellco.org/bankruptcy.asp (last consulted October 21, 2005). See also the CBM Credit Education Foundation website; http://www.cbmfoundation.org/files/13.doc (last consulted October 21, 2005); and the American Federation of Government Employees web site; http://www.afge.org/Index.cfm?Page=HowToCorner&file=archives/2004_09_08.htm (last consulted October 21, 2005).

[70] cite

[71] Cite

[72] CR Austin billboard.

[73] *See* FDIC Testimony, *supra* note xx.

Changes in Industry Practices

If families' reluctance to turn to bankruptcy (stigma) had remained about the same over the past twenty years, but if credit for people already in financial trouble had increased dramatically, we might expect to see the very change in the bankruptcy data that we report above. Families would be waiting longer in the cycle of their financial collapse before they filed for bankruptcy, self-financing through periods of unemployment, medical problems or divorce. Some would succeed in weathering the crisis because of the continued availability of credit; others would simply experience deepening insolvency. The evidence of this would be more families in bankruptcy carrying substantially more debt today than they did a generation ago—exactly what the data show. Thus that model of contemporary consumer bankruptcy also fits the data.

In the late Seventies and Eighties, when the credit spigot was turned off, families may have found other mechanisms to deal with serious financial reversals—move in with family members, accept charity or state-sponsored welfare, farm out the children, sell off household items, switch to the underground economy with day labor or other cash-only employment. Some headed into bankruptcy, but others may have sought alternatives that permitted the family to survive without increasing its debt load beyond levels that it could never repay. In the late Nineties, because of the availability of credit to financially distressed families, more of them might survive a period of unemployment or medical problem without turning to charity or the underground economy, but more would load themselves with debt that quickly became unmanageable. Retail credit flows, permitting even an unemployed person to make every purchase from food to utilities to taxes.[74] When a debtor charges a purchase over the credit limit, the response is likely to be that the creditor simply raises the limit, although often imposing a hefty fee for doing it.[75] A new player—the payday lender—makes sure there is cash to pay the landlord or the daycare center even for those with the worst credit records.[76] If someone has no income or the bills are overwhelming, the music eventually stops, but in the meantime creditors will offer debt in abundance.

In this contemporary financial environment, families could self-fund themselves through a difficult financial stretch using credit, but if they misjudged how long they would be unemployed or how high the medical bills would go, they would find themselves unable to regain their economic footing because their debts were now sky-high. In other words, the changes in the credit industry in making money available to troubled borrowers may actually have changed the calculus that leads to bankruptcy.

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[74] In the Eighties, the movie "Kramer v. Kramer" derived much of its humor from the idea that the family that was broke could survive by charging everything at Bergdorf's. We wonder if the rising generation would see any anomaly at which to smile. It may be that credit as a survival tool, available to the broke and the solvent alike, has come to seem commonplace.

[75] *See, e.g.,* Household Credit Services, Inc., v. Pfennig 541 U.S. 232, 236 (2004).

[76] *See generally*, Creola Johnson, *Payday Loans: Shrewd Business Or Predatory Lending?*, 87 Minn. L. Rev. 1 (2002); Catherine E. Vance & Paige Barr, *The Facts & Fiction Of Bankruptcy Reform*, 1 Depaul Bus. & Comm. L.J. 361 (2003).

The data presented in this paper are consistent with the proposition that changes in credit availability have increased the number of consumer bankruptcies by providing credit to families already in trouble. Moreover, the rise in the amount of debt families are carrying at the time of their bankruptcies and the decline in their incomes (suggesting weaker borrowers) are also consistent with this hypothesis. The strongest support for this hypothesis, however, comes from the credit industry itself. Fair Isaacs argues that minimal credit screening could save credit card issuers billions each year.[77]

Why the change? The effective repeal of usury laws combined with the falling wholesale cost of money has altered the economics of consumer lending.[78] Sub-prime lenders have learned that when inflation is low, lending out at 18, 22 or 34 percent can be extraordinarily profitable even if a substantial portion of borrowers ultimately default on their loans. The math is nothing short of stunning. At a time when the wholesale cost of money is 4%, for example, a sub-prime lender who places a $10,000 loan at 26% by year four has earned over $7,000 in profit and has received a total amount equal to the full loan, while the borrower still owes more than half of the loan. Once they have worked out the math, it is little wonder that mainstream lenders such as Citibank and Ford Motor Credit have taken their place alongside marginal operations that target financially troubled families. Indeed, nowadays commercial lending is a declining source of income for the major banks; their most important profit center is the interest and fees generated by consumer debt.[79]

This phenomenon—the availability of credit to people already in financial trouble—raises important questions of morality and public policy. Are American families and our society as a whole better or worse off as a result? Is a greater opportunity to bridge the gap between one job and another, for example, worth the costs imposed by the greater indebtedness suffered and then discharged by those who do not succeed? We are inclined to be skeptical about the benign effects of this continued lending, because twenty years of empirical work have taught us that trouble tends to breed trouble and debtors in difficulty are often too optimistic. Although that discussion that will have to await another paper, we note that deliberately extending still more credit to debtors in financial distress, whether a struggling family or a corporation with a bad balance sheet, creates a partnership of hope, in which the lender and borrower have raised their bets and will succeed or fail together.[80]

Although it seems unlikely that anyone will succeed in making a persuasive empirical case that increased bankruptcy filings result to some material extent from

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[77] Fair Isaacs cite and explain what is.

[78] Diana Ellis, *supra* note xx.

[79] Cite WSJ. *See also* FDIC testimony, *supra* note xx, at 14 ("Bank commercial and industrial lending has declined sharply . . . .").

[80] The extension is knowing, because the pattern of minimum payments, late fees, over-limit charges, and the like is readily detectable by the grantors' computers and regularly followed by its staff. Ronald J. Mann, Charging Ahead: THE GROWTH AND REGULATION OF PAYMENT CARD MARKETS AROUND THE WORLD, CH. 17 (Cambridge U. Press forthcoming 2006). If it is not, they are likely to be in serious financial trouble themselves. *See, e.g.,* Amy Merrick, *Credit-Card Bet Forces Spiegel to Seek Bankruptcy Protection*, Wall S.J. March 18, 2003.

decreased stigma, it is interesting to consider what would be a likely cause of the decline. If, for example, such a decline resulted from a general moral decadence, then toughening of the law would be a logical response, although probably a futile one. However, the earlier discussion demonstrates that a plausible source of stigma reduction is the advertising of sub-prime lenders and the credit practices of much of the credit industry.[81] If it is, then self-restraint by credit grantors or legal adjustments that reduced the attractiveness of selling credit to bankrupts and near-bankrupts might contribute to lowering the bankruptcy filing rates—and, more importantly, the human cost of overindebtedness.

Increased Debt

Sometimes the simplest explanations are the best. The dramatic increase in the consumer debt burden may be the simple, direct explanation for the growth in bankruptcy filings: "Total household debt is at an historical high of 112 percent of disposable personal income."[82] Figure 9 shows three simple charts relating increases in outstanding consumer debt to increases in bankruptcy filings. Two reflect our experience in the United States and the other in Australia. The match between bankruptcy filings and the rise in consumer debt burdens is remarkably good, especially with a time lag. As noted previously, consumer debt has climbed precipitously in the last twenty years, in the United States and many other countries. Given the eternal verity that "time and chance happenth to them all,"[83] the existence of more debtors in the zone of default-risk could plausibly be a sufficient explanation of the increase in bankruptcy filings, without more.

Figure 9. Consumer Debt and Bankruptcy Filings

There may be other theories consistent with the changing financial profile of the families who file for bankruptcy. But one thing is certain: without a far more elaborate model, the simple assertion that the rise in bankruptcy filings has been prompted by a decline in stigma is inconsistent with the data presented and is less intuitively persuasive than a number of other available explanations.

Conclusion

Empirical data have become central to the debates about personal bankruptcy.[84] As we have noted, for twenty years the central datum has been the dramatic rise in bankruptcy filings. In 1995, the credit industry thought it prudent to begin its struggle for "tougher" bankruptcy laws with an empirical study, albeit one that was distributed by political relations persons rather than published in the professional literature.[85] The legislation the industry put forward was in turn significantly narrowed because of two

[81] CR
[82] FDIC Testimony, *supra* note xx, at 4.
[83] Ecclesiastes 9:11.
[84] Empirical Research, *supra* note xx.
[85] *Id.* at n. 40.

empirical studies revealing the weaknesses of some of the proposed provisions.[86] In the end, only enormous political effort overcame the data that had cast serious doubt on the bill's premises.[87]

This article provides compelling evidence that a principal argument supporting the legislation is simply wrong. The data are inconsistent with the hypothesis that declining stigma explains the increase in bankruptcy filings over the last twenty years. Given that there are a number of more plausible explanations available that fit the data much more closely, anyone who attempts to resurrect the declining-stigma hypothesis will bear a heavy burden of supplying concrete empirical evidence in its support.

Beyond that specific debate, this article offers a baseline of data reflecting United States personal bankruptcies over two decades. These data can be compared with the data that will describe the experience that emerges under the new legislation. The collision between the legislative assumptions and the reality revealed by the existing data means will make a fascinating collision—as long as one is not personally at the point of contact, of course.

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[86] *See* Marianne B. Culhane & Michaela M. White, *Taking the New Consumer Bankruptcy Model for a Test Drive: Means-Testing for Chapter 7 Debtors*, 7 Am. Bankr. Inst. L. Rev. 27 (1999); Teresa A. Sullivan & Elizabeth Warren, *Women in Bankruptcy*, at http://www.abiworld.org/research/womenbank.html (July 13, 1999); Teresa A. Sullivan & Elizabeth Warren, *More Women in Bankruptcy*, at http://www.abiworld.org/research/morewomen.html (July 30, 1999). *See generally*, Westbrook, *supra* note xx, at 2129-33.

[87] *See generally,* Rafael Efrat, *Attribution Theory Bias And The Perception Of Abuse In Consumer Bankruptcy*, 10 Geo. J. on Poverty L. & Pol'y 205 (2003).

Appendix 1—Basic Financial Characteristics of Debtors, 1981, 1991, 2001

Table 1a)-Distribution of Income, Assets, and Debts for Bankruptcy Petitioners in 2001

Distribution	Family Income	Total Assets	Total Debt	Secured Debt	Unsecured Debt
Mean	26,982ab	69,715ab	91,155ab	56,905ab	34,425a
s.d.	15,966	88,071	91,787	74,383	51,863
25th percentile	16,098	6,813	27,103	2,000	9,950
Median	24,006	36,910	63,673	25,485	20,450
75th percentile	34,374	107,100	124,915	92,257	40,129
N	1,224	1,211	1,232	1,230	1,229
Outliers removed	10	10	10	10	10
Missing	16	29	8	10	11

Table 1b)-Distribution of Income, Assets, and Debts for Bankruptcy Petitioners in 1991 (2001 dollars)

Distribution	Family Income	Total Assets	Total Debt	Secured Debt	Unsecured Debt
Mean	26,565ac	49,253ac	68,142c	40,088c	28,008
s.d.	15,952	67,867	86,265	65,419	46,600
25th percentile	15,600	4,114	19,407	1,110	8,633
Median	23,400	18,330	38,480	13,517	16,201
75th percentile	34,729	75,602	84,614	60,162	28,921
N	622	622	621	621	622
Outliers removed	5	5	5	5	5
Missing	0	0	1	1	0

Table 1c)-Distribution of Income, Assets, and Debts for Bankruptcy Petitioners in 1981 (2001 dollars)

Distribution	Family Income	Total Assets	Total Debt	Secured Debt	Unsecured Debt
Mean	30,735bc	57,179bc	75,186c	44,867c	30,187c
s.d.	12,492	52,044	71,260	50,136	40,648
25th percentile	18,403	5,820	18,966	3,051	7,453
Median	29,167	27,318	40,819	18,702	13,736
75th percentile	41,545	86,356	86,641	59,332	27,144
N	1,289	1,490	1,496	1,501	1,495
Outliers removed	44	44	44	44	44
Missing	213	12	6	1	7

a--Significantly different from the 1981 survey at the .05 level
b--Significantly different from the 1991 survey at the .05 level
c--Significantly different from the 2001 survey at the .05 level

Appendix II—Debt-to-Income Ratios, Family by Family, 1981, 1991, 2001

Table 2-Distribution of Total Debt/Income Ratio for Bankruptcy Petitioners

Year	Distribution	Total Debt/ Income Ratio
2001		
	Mean	4.63
	s.d.	20
	25th percentile	1.21
	Median	2.3
	75th percentile	4.12
	N	1059
	Outliers removed	14
	Missing	176
1991		
	Mean	2.54
	s.d.	2.98
	25th percentile	1.07
	Median	1.79
	75th percentile	3.1
	N	415
	Zero income	7
	Outliers removed	5
	Missing	21
1981		
	Mean	3.2
	s.d.	10.45
	25th percentile	0.7
	Median	1.41
	75th percentile	2.6
	N	1,241
	Zero income	47
	Missing	214
Statistical Test		
	t-value	1.26 (a)

a-not statistically significant at the .05 level

Table 3-Distribution of Total Nonmortgage Debt/Income Ratios for Bankruptcy Petitioners

Year	Distribution	Total Nonmortgage Debt/ Income Ratio
2001		
	Mean	2.12
	s.d.	3.85
	25th percentile	0.59
	Median	1.17
	75th percentile	2.08
	N	1060
	Outliers removed	14
	Missing	175
1991	Distribution	Total Nonmortgage Debt/ Income Ratio
	Mean	1.62
	s.d.	2.53
	25th percentile	0.62
	Median	1.06
	75th percentile	1.7
	N	414
	Zero income	7
	Outliers removed	5
	Missing	22
1981	Distribution	Total Nonmortgage Debt/ Income Ratio
	Mean	2.11
	s.d.	8.05
	25th percentile	0.48
	Median	0.79
	75th percentile	1.46
	N	1,147
	Zero income	35
	Missing	313
Statistical Test		
	t-value	1.21(a)

a-not significant at the .05 level

TABLE A

Debt Burdens of Debtors "Best Able to Pay"[a] 1981 to 2001

	Mean Total Debt to Income Ratio[b]	Mean NonmortgageDebt to Income Ratio[c]
1981	.30	.05
1991	.39	.07
2001	.64	.04

a. "Best able to pay" defined as the decile of debtors with the lowest ratio of debt to income
b. All significantly different from one another at $p < .001$
c. 1981 and 2001 significantly different from 1991at $p < .001$.