THE FAILURE OF BANKRUPTCY'S FRESH START

Katherine Porter† *&* *Dr. Deborah Thorne*††

An untested assumption of Chapter 7 bankruptcy is that it rehabilitates debtors for a fresh start in the economy. Using original, longitudinal data, we examine this assumption against the realities of life after bankruptcy. Our findings challenge the fresh start as the theoretical underpinning for consumer bankruptcy relief. We found that just one year postbankruptcy, one in four debtors was struggling to pay routine bills, and one in three debtors reported an overall financial situation similar to, or worse than, when that debtor filed bankruptcy. Our analysis of these data demonstrates that steady and sufficient income is the key to improved postbankruptcy financial health. Factors that cause household income to decline, such as unemployment and underemployment, illness or injury, and old age, undermine the chances of financial recovery. These data reveal the limitations of bankruptcy as a social safety net and highlight the fragile economic situations of American families. We conclude that bankruptcy is an incomplete tool to rehabilitate those in financial distress, and we suggest adjustments to bankruptcy law and social programs that will improve the ability of consumers to achieve a fresh start after financial failure.

† Associate Professor of Law, University of Iowa.
†† Assistant Professor of Sociology, Ohio University.

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Introduction

The principal theory of consumer bankruptcy in America is that it provides a "fresh start" to debtors.[1] Courts,[2] Congress,[3] and scholars[4] repeatedly cite the fresh start as the justification for a particular interpretation of our consumer bankruptcy system. Despite its ubiquity in the bankruptcy landscape, the fresh start remains an elusive concept.[5] Most frequently, people equate the fresh start with the economic rehabilitation of debtors through bankruptcy's discharge of debt.[6] Central to this rehabilitation is the promise that life after bankruptcy will be free of financial hardship.[7] The belief is that the fresh start enables former debtors to earn, spend, borrow, and repay money at a manageable pace.[8] Arming former bankrupts with a "new opportunity in life," the fresh start supposedly sets them on a path to prosperity.[9] The promise of a better financial life after bankruptcy lures families to file for bankruptcy relief when they are overwhelmed with debt, and the transformative power of bankruptcy is central to the policy debates about our consumer bankruptcy system.[10]

Yet, buried in the rhetoric of rehabilitation is a powerful but untested assumption: Filing bankruptcy is an effective solution to financial distress. From theoretical defenses penned by scholars[11] to the sweeping bankruptcy law reforms that Congress recently enacted,[12] the core assumption that shapes our bankruptcy laws is that bankruptcy offers debtors an effective way to improve their financial pros-

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1 *See* Margaret Howard, *A Theory of Discharge in Consumer Bankruptcy*, 48 Ohio St. L.J. 1047, 1047, 1059 (1987).

2 *See, e.g.*, Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934).

3 *See, e.g.*, Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc. No. 93-137, pt. 1, at 71, 79–80 (1973).

4 *See* Karen Gross, Failure and Forgiveness: Rebalancing the Bankruptcy System 91 (1999) ("Some scholars just reiterate the term *fresh start* in their justifications, saying, for example, that debtors should have an 'opportunity to begin anew' or a 'chance to start over.'").

5 *See* Howard, *supra* note 1, at 1059 (comparing the term "rehabilitation" with the "equally elusive term 'fresh start'").

6 *See* Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc. No. 93-137, pt. 1, at 71, 79–80 (1973).

7 *See id.* at 79–80.

8 *See* Gross, *supra* note 4, at 99.

9 Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934).

10 *See infra* Part I.A.

11 *See, e.g.*, Gross, supra note 4, at 91–103.

12 *See, e.g.*, Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (codified in scattered sections of 11 U.S.C.) (effective Oct. 2005).

pects. On the surface, this assumption seems correct, perhaps even self-evident. Bankruptcy allows debtors to eliminate all or most of their debt; with the stroke of a pen, a judge can instantly sign away thousands of dollars of debt.[13] Thus, a natural assumption is that bankruptcy discharge steers debtors toward economic success. Newly healed from their financial crises, these families should be ready to enjoy the future rewards of participating in the American economy.

This Article explores the assumption that consumer bankruptcy offers families a better financial future. Using original data, we evaluate how the theory of a fresh start operates in the lives of families who file bankruptcy. Focusing on the powerful, immediate discharge of debt available in Chapter 7 bankruptcy, we assess how families fare in the year after their bankruptcies. Our data come primarily from extensive telephone interviews with 359 debtors, which we conducted approximately one year after the debtors' bankruptcy filings.[14] We correlate the postbankruptcy interview data with the debtors' responses to a questionnaire that the debtors completed near the time of their bankruptcy filings and with their bankruptcy court records.[15] These multifaceted data provide a rich picture of how Chapter 7 affects the lives of those who go bankrupt and represent the first systematic effort to document the postbankruptcy experiences of Chapter 7 debtors under the Bankruptcy Code.[16]

One of our simplest questions about life postbankruptcy yielded a shocking finding. We asked debtors the following question: "Overall, since you filed for bankruptcy, has your financial situation improved, stayed about the same, or worsened?"[17] Based on the fresh-start rhetoric and the perceived benefits of a Chapter 7 discharge, we expected that nearly all debtors would report an improved financial situation one year after their bankruptcies. The data nullified this hypothesis. Although 65% of debtors stated that their financial situations had improved since they filed Chapter 7, more than one-third of the debtors reported that their financial situations were actually the same as or worse than at the time of their bankruptcies.[18] Thus, while bankruptcy appears to help a majority of families to obtain a sustainable

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13 *See* 11 U.S.C. § 727 (2000) (discharge).

14 See *infra* Appendix for details about our methodology.

15 *See infra* Parts II & III.

16 We know of only one other sizeable study of American debtors' postbankruptcy experiences, and it was conducted before Congress enacted the 1978 Bankruptcy Code, a major overhaul to the nation's bankruptcy laws. *See* David T. Stanley & Marjorie Girth, Bankruptcy: Problem, Process, Reform (1971) (interviewing families two years after their bankruptcy filings). See *infra* Part I.B for further discussion of Stanley and Girth's findings.

17 All research records to which this Article refers, including questionnaires and telephone interview questions and responses, are on file with the authors.

18 *See infra* Part II.B.

fresh start, many former debtors continue to experience financial hardship that is as bad as or worse than the distress that initially triggered their bankruptcy filings. For many families, the fresh start either failed to materialize or dissipated within one year of the discharge of their debts. Data that we gathered on postbankruptcy financial management buttressed this finding: One year after bankruptcy, one in four families reported that paying their expenses was an ongoing struggle.[19] For these families, the promise of a better life was a theoretical hope, distant from the reality of their continuing financial difficulties.

In light of these findings about the hardships of postbankruptcy life, we examined our data to document the ways in which bankruptcy leaves families vulnerable to financial distress. We compared those families who reported sustained financial improvement with those who reported that their financial situations had remained unchanged or worsened, analyzing the two groups across dozens of demographic and economic variables.[20] We identified one key trait that distinguished those families who continued to struggle after bankruptcy: Lack of adequate steady income.[21] Chronic or new postbankruptcy income declines plagued families for whom the fresh start never materialized. The data supporting this finding offer important insights into the sources of these income problems and the privations that families suffer as they strain to pay living costs such as utilities, insurance premiums, and rent that accumulate postbankruptcy. A true and lasting economic transformation requires more than erasing past debt; it requires families to retool their financial lives to close the gap between income and expenses. For families whose income is declining, this task is likely futile, if not impossible. Bankruptcy may offer a temporary refuge, but it does not generate sufficient or steady enough income to shelter families with chronic income problems from further economic distress.

We conclude that the theory of the fresh start obfuscates the complicated reality of financial distress. The previously untested assumption that Chapter 7 bankruptcy offers an effective means to financial success is suspect. The current bankruptcy system is an inadequate solution for chronic income problems and does not insulate families from future financial shocks. Thus, understanding the limitations of a bankruptcy discharge to effectuate a fresh start has far-reaching implications for redirecting consumer bankruptcy law. The last decade of bankruptcy scholarship has focused on documenting the causes of

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19 *See infra* Part II.A.

20 *See infra* Part III.A.

21 *See id.*

bankruptcy.[22] However, we also must attend to analyzing how bankruptcy law could better help families solve the underlying problems that lead to overindebtedness. Recognizing the primacy of income stability to lasting financial well-being reorients bankruptcy law to its principal goal of providing a fresh start. With this new perspective, we offer a comprehensive view of the practical realities that debtors must overcome to rebuild their financial lives. Making our consumer bankruptcy system more effective requires finding ways for bankruptcy law to deliver more consistently on the promise of the fresh start.

This Article explores the postbankruptcy financial experiences of families and the implications of these experiences. In Part I, we examine theoretical perspectives and prior studies on the efficacy of consumer bankruptcy as a rehabilitative tool, and we discuss the methodology of our study. In Part II, we describe the financial stresses that many families confront in the year after their bankruptcies. In Part III, we explore the factors that correlate with a failure to achieve economic recovery after bankruptcy. We isolate steady and sufficient income as the key variable and refute several alternative hypotheses. We conclude in Part IV with the policy implications of our findings. A rich, complete understanding of consumer bankruptcy requires a nuanced perspective of the limitations of bankruptcy's fresh start as a means to economically rehabilitate families.

I
Background

The long-standing and much-touted theory of consumer debt relief is that it provides a fresh start for debt-laden individuals.[23] Despite the prevalence of the fresh-start concept, a dearth of knowledge exists about what happens to people after they file bankruptcy and only limited theorizing exists on what the contours of a fresh start should look like. The data we analyze in this Article use multiple instruments to measure financial well-being and offer a complex and textured portrait of postbankruptcy life.

A. The Rhetoric of Rehabilitation

The contours of the fresh start are elusive despite the phrase's ubiquity in consumer bankruptcy literature.[24] The idea of a fresh start predates the current Bankruptcy Code that Congress enacted in 1978 and appears to have roots in America's development of a discharge

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22 *See, e.g.*, Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, The Fragile Middle Class: Americans in Debt (2000).

23 *See* Gross, *supra* note 4, at 91.

24 *See* Howard, *supra* note 1, at 1059.

injunction for individuals who filed bankruptcy.[25] The Supreme Court used this phrase as early as the 1930s, citing rehabilitation as the principal goal of a bankruptcy system.[26] The Court emphasized bankruptcy's opportunity for a new beginning as a crucial underpinning of a free-market, commercial economy.[27] The legislative history of America's various bankruptcy laws is replete with references to the fresh start.[28] In 1973, the Bankruptcy Commission summarized the prevailing view: Bankruptcy should "rehabilitate debtors for continued and more value-productive participation" in economic life.[29] During the recent reforms to the Bankruptcy Code,[30] Congress noted its intent to preserve the "fresh start for the honest debtor."[31] This rhetoric is especially notable because the general nature of the reforms was unfriendly to most consumer debtors.[32] Nevertheless, congressional representatives affirmed or at least gave the appearance of affirming bankruptcy's importance as an opportunity for a fresh start.[33]

Because the fresh start dominates theoretical discussions about consumer bankruptcy, scholars have attempted to examine and justify

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25 *See* Charles Jordan Tabb, *The Historical Evolution of the Bankruptcy Discharge*, 65 AM. BANKR. L.J. 325, 355 (1991) (stating that the Bankruptcy Act of 1867 was motivated "by a desire 'to relieve the plight of debtors'" (quoting C. WARREN, BANKRUPTCY IN UNITED STATES HISTORY 105 (1935))).

26 *See* Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) ("One of the primary purposes of the Bankruptcy Act is to 'relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.'" (quoting Williams v. U.S. Fidelity & Guar. Co., 236 U.S. 549, 554–55 (1915))).

27 *See id.*; *see also* Grogan v. Garner, 498 U.S. 279, 286 (1991) (giving effect to the "fresh start" policy of the Bankruptcy Code).

28 *See, e.g.*, 151 CONG. REC. H2053 (daily ed. Apr. 14, 2005) (statement of Rep. Goodlatte) ("The application of such objective standards will help ensure that the fresh start provisions of Chapter VII will be granted to those who need them . . . ."); 145 CONG. REC. H2655 (daily ed. May 5, 1999) (statement of Rep. Gekas) ("We, our enlightened forefathers, saw fit to allow the Congress to evolve in a situation in which a fresh start would be accorded to an ordinary citizen who cannot meet his obligations . . . .").

29 REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 93-137, pt. 1, at 71 (1973).

30 *See* Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (codified in scattered sections of 11 U.S.C.) (effective Oct. 2005).

31 Press Release, U.S. Sen. Chuck Grassley, Grassley Praises President for Signing Comprehensive Bankruptcy Reform Legislation (Apr. 20, 2005), *available at* http://grassley.senate.gov/index.cfm?FuseAction=PressReleases.View&PressRelease_id=4897 [hereinafter Grassley April Press Release].

32 *See* Charles Jordan Tabb, *The Death of Consumer Bankruptcy in the United States?*, 18 BANKR. DEV. J. 1, 6–8 (2001) (explicating numerous ways that bankruptcy law will likely harm most individual debtors).

33 *See, e.g.*, Grassley April Press Release, *supra* note 31 (quoting Senator Grassley as stating, "The Bankruptcy bill preserves a fresh start for people who are overwhelmed by medical debts, loss of a job, or sudden unforeseen emergencies").

the normative underpinnings of the fresh start.[34] Margaret Howard, who has explicated the multiple ways in which the fresh start could rehabilitate consumer debtors, observes that rehabilitation encompasses at least three goals: consumer financial education of the debtor, emotional and psychological relief from financial failure, and renewed debtor participation in the open-credit economy.[35] Each of these components presents a different way to evaluate the efficacy of the Bankruptcy Code for individuals who seek debt relief.

Until 2005, the Bankruptcy Code did not provide for financial education, although a very small number of instructional programs did exist.[36] The newly amended Bankruptcy Code requires that an individual debtor complete a program of financial education to be eligible for a discharge.[37] This reform suggests that Congress views financial education as a valuable tool that enables debtors to capitalize on the fresh start. Recent academic research has evaluated the role that financial education plays in helping debtors avoid financial distress in the future.[38] Eventually, financial education may be a proven component of bankruptcy's fresh start, but historically, bankruptcy law has embraced a different model of rehabilitation.

Similarly, the law does not explicitly effectuate the psychological and emotional relief that families should experience from filing bankruptcy. The automatic stay and the discharge do relieve debtors from the pressure of negotiating with creditors, but these provisions serve other purposes as well.[39] Limited data are available to evaluate the psychological benefits of bankruptcy for debtors and their families.[40] Nevertheless, such benefits may well be substantial, and future re-

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34 *See, e.g.*, F.H. Buckley, *The American Fresh Start*, 4 S. CAL. INTERDISC. L.J. 67 (1994); Richard E. Flint, *Bankruptcy Policy: Toward a Moral Justification for Financial Rehabilitation of the Consumer Debtor*, 48 WASH. & LEE L. REV. 515 (1991); Charles G. Hallinan, *The "Fresh Start" Policy in Consumer Bankruptcy: A Historical Inventory and an Interpretive Theory*, 21 U. RICH. L. REV. 49 (1986); Thomas H. Jackson, *The Fresh-Start Policy in Bankruptcy Law*, 98 HARV. L. REV. 1393, 1397 ("[A] normative theory of the fresh-start policy must . . . explain why, in the context of a social and economic order premised on individual autonomy, the law should make inalienable the right to a fresh start.").

35 *See* Howard, *supra* note 1, at 1060–62.

36 *See* Jean Braucher, *An Empirical Study of Debtor Education in Bankruptcy: Impact on Chapter 13 Completion Not Shown*, 9 AM. BANKR. L. REV. 557, 560–61 (2001) (discussing a handful of financial education programs for Chapter 13 debtors that operated before the 2005 bankruptcy amendments and noting that education was less common for Chapter 7 debtors).

37 *See* 11 U.S.C.A. § 1328(g)(1) (West 2005).

38 *See, e.g.*, Richard L. Wiener et al., *Unwrapping Assumptions: Applying Social Analytic Jurisprudence to Consumer Bankruptcy Education Requirements and Policy*, 79 AM. BANKR. L.J. 453, 473–74 (suggesting ways to implement the content and delivery of financial education that the amended Bankruptcy Code requires).

39 *See* 11 U.S.C. § 362 (2000) (automatic stay); 11 U.S.C. § 727 (2000) (discharge).

40 *See* STANLEY & GIRTH, s*upra* note 16, at 69.

search of an ethnographic nature would enrich our understanding of how psychological harm and debt intersect.

The third goal, economic rehabilitation, is the core of the fresh-start policy in bankruptcy, at least as far as scholars have historically articulated the concept. A legal discharge from debt is the primary mechanism for economic rehabilitation and many often view it as being synonymous with the fresh start.[41] However, discharge seeks merely to implement the rehabilitation of debtors; it is no more than the chosen means to an end. Therefore, a narrow focus on discharge does not justify the fresh-start policy or help define when such rehabilitation should be available.[42] Moreover, a discharge of past debt does not ensure or even adequately delineate the contours of future economic success. Most scholarship generally asserts that rehabilitation consists of merely positioning the debtor to reenter the economy unhampered by past debt, but the ultimate objective is to provide the debtor with the incentive to earn income, spend money, and reenter the credit economy.[43] Such successful borrowing sustains the macroeconomy, which increasingly relies on consumer debt.[44] Strong economic health also prevents individuals from turning to social welfare programs for support.[45] Presumably, borrowing facilitates an immediately improved lifestyle for individuals and helps smooth gaps between income and consumption. Broadly conceived, the goal of bankruptcy rehabilitation is not to change the consumer behavior of borrowing, but to foster a different outcome of the behavior: Repayment instead of default.[46] As Karen Gross has explained, "[w]e do not want debtors simply to stop incurring debt[;] . . . we want debtors to be able to *continue* borrowing if they put themselves in the position to be able to repay what they owe their creditors."[47]

If we interpret the fresh-start policy in this way, what happens to people after bankruptcy defines the success or failure of our bankruptcy system. The adequacy of a rehabilitative system does not de-

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41 *See* Howard, *supra* note 1, at 1047 ("The purpose of the consumer bankruptcy system, effectuated by discharge, is to give a fresh start to the 'honest but unfortunate debtor.'"); Jackson, *supra* note 34, at 1393 ("For these reasons, discharge is viewed as granting the debtor a financial 'fresh start.'").

42 *See* GROSS, *supra* note 4, at 91; Howard, *supra* note 1, at 1062.

43 *See* Howard, *supra* note 1, at 1059, 1062.

44 *See* SUSAN BURHOUSE, FED. DEPOSIT INS. CORP., EVALUATING THE CONSUMER LENDING REVOLUTION (2003), http://www.fdic.gov/bank/analytical/fyi/2003/091703fyi.html (noting that consumer spending makes up more than two-thirds of America's gross domestic product and contributed over 85% of the nation's economic growth between 2001 and 2003).

45 *See* SULLIVAN, WARREN & WESTBROOK, *supra* note 22, at 259–60 (discussing bankruptcy in the free-market economy as an individualized risk alternative to government social safety programs that collectivize the risk of financial failure).

46 *See* GROSS, *supra* note 4, at 99.

47 *Id.*

pend on changes in the number of bankruptcy filings or dollars discharged.[48] These statistics may reflect the depth and breadth of financial distress in American society, but they reveal nothing about whether bankruptcy functions effectively to rehabilitate debtors. To evaluate accurately whether bankruptcy law is effectuating the goal of giving debtors a meaningful fresh start, the most crucial data to examine are the economic situations of families after their bankruptcies. The rhetoric about rehabilitation is powerful, and the academic and political consensus about the fresh start as the principal theory of consumer bankruptcy is strong and stable. To date, however, the empirical evidence necessary to assess the reality of the fresh start has been missing.[49]

B. Prior Studies

There is a paucity of data about how debtors fare after bankruptcy. Do families successfully regain financial health after receiving a discharge of debt? For those families who experience financial distress again, what factors explain this outcome? Jean Braucher recently identified the importance of gathering data to answer these questions.[50] She notes that "[w]e do not know to what extent bankruptcy is a turning point in consumer debtors' financial lives, and how many continue to be over-indebted and for what reasons . . . . [T]he obstacles to long-term financial security after bankruptcy are a matter of conjecture."[51] As Braucher further states, "gaping holes in our knowledge" make it difficult to evaluate the adequacy of the current bankruptcy system.[52]

The prior research on life postbankruptcy is sparse but suggestive of the complex nature of financial recovery. The best available data are from cases filed under Chapter 13 of the Bankruptcy Code. Because families who file Chapter 13 bankruptcy do not receive a discharge of their debts until the end of a three- to five-year period,

48 Yet, in recent years, Congress focused on exactly these two criteria in debating whether to amend the Bankruptcy Code. *See* BANKRUPTCY REFORM ACT OF 1999, S. REP. NO. 106-49, at 2 (1999); *see also* Melissa B. Jacoby, *Negotiating Bankruptcy Legislation Through the News Media*, 41 HOUS. L. REV. 1091, 1096 (2004) (documenting media and legislative response to an annual bankruptcy filing rate exceeding one million in 1996); Elizabeth Warren, *The Phantom $400*, 13 J. BANKR. L. & PRAC. 77, 84 (2004) (quoting congressional representatives who cited the total amount of discharged debt as the reason for their support of the bankruptcy reform bill).

49 Mark L. Power, Tahira K. Hira & Roger P. Murphy, *Personal Bankruptcy a Risk Management Technique: Policy Implications*, RISK MGMT. & INS. REV., Winter 1999, at 81, 82–83 ("A review of bankruptcy literature shows that none of the studies have reported the long-term personal and financial consequences of filing bankruptcy.").

50 *See* Jean Braucher, *Consumer Bankruptcy as Part of the Social Safety Net: Fresh Start or Treadmill?*, 44 SANTA CLARA L. REV. 1065, 1068, 1090–91 (2004).

51 *Id.* at 1070.

52 *Id.* at 1091.

during which they must use their wages to repay a portion of their past debts, the court system monitors these debtors throughout the Chapter 13 process.[53] A few longitudinal studies have followed some of these families.[54] These studies aimed to measure what percentage of debtors completed their Chapter 13 payments and received a discharge.[55] Generally, the authors found a relatively low rate of Chapter 13 completion but noted that the percentage of Chapter 13 debtors receiving a discharge varied greatly in districts across the country.[56] These findings caused scholars and bankruptcy professionals to express concern about the efficacy of Chapter 13 and provoked a call for the repeal or revision of Chapter 13.[57] The Chapter 13 failure rate suggests that debtors may experience financial instability after filing bankruptcy given that a missed payment is often the cause of Chapter 13 dismissal.[58] The published studies do not attempt to measure the source or nature of such financial problems, likely because of the difficulty and expense of locating families, obtaining research consent, and developing and coding a primary data instrument such as a survey or personal interview.[59] These same factors have probably hindered any meaningful research about what happens to those families who do receive a Chapter 13 discharge upon completion of their bankruptcies.

Even less is known about the outcomes of Chapter 7 bankruptcy. Chapter 7 is "liquidation bankruptcy," in which a debtor receives an immediate discharge of most past unsecured debt in return for surrendering nonexempt assets.[60] Most families receive a discharge of all of their unsecured debts within two or three months of filing for relief under Chapter 7.[61] The immediacy of relief in a consumer liquidation case partially eases the longitudinal data collection issues identified regarding Chapter 13 cases. Yet, there are no empirical data on the postbankruptcy experiences of families who file under Chapter 7

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53 *See* 11 U.S.C.A. § 1322(d)(2)(C) (West 2005).

54 *See, e.g.*, Braucher, *supra* note 36.

55 *See id.* at 557.

56 *See id.* at 571–74 (summarizing variations in Chapter 13 completion rates in several studies).

57 *See, e.g.*, Jean Braucher, *Lawyers and Consumer Bankruptcy: One Code, Many Cultures*, 67 AM. BANKR. L.J. 501, 506 n.19 (1993); William C. Whitford, *Has the Time Come to Repeal Chapter 13?*, 65 IND. L.J. 85, 104 (1989); William C. Whitford, *The Ideal of Individualized Justice: Consumer Bankruptcy as Consumer Protection, and Consumer Protection in Consumer Bankruptcy*, 68 AM. BANKR. L.J. 397, 415–17 (1994).

58 *See* TERESA A. SULLIVAN, ELIZABETH WARREN & JAY LAWRENCE WESTBROOK, AS WE FORGIVE OUR DEBTORS: BANKRUPTCY AND CONSUMER CREDIT IN AMERICA 38–39 (1989).

59 *See, e.g.*, STANLEY & GIRTH, *supra* note 16, at 225.

60 ELIZABETH WARREN & JAY LAWRENCE WESTBROOK, THE LAW OF DEBTORS AND CREDITORS: TEXT, CASES, AND PROBLEMS 121 (5th ed. 2006).

61 *See* 11 U.S.C. § 727 (2000).

of the Bankruptcy Code.[62] The only recent study that has inquired about the postbankruptcy experiences of debtors who filed liquidation bankruptcy was conducted in Australia.[63]

The best data about American debtors are forty years old and were collected under the pre-1978 bankruptcy law, which was called the Bankruptcy Act.[64] In the mid-1960s, David Stanley and Marjorie Girth conducted landmark bankruptcy research that the Brookings Institute funded. A component of this large study included interviewing four hundred people who had filed bankruptcy two years prior.[65] The researchers asked the former debtors to describe their financial situations at the time of the interviews as compared with when they filed bankruptcy.[66] The table below shows the responses from the Chapter 7 debtors in their sample.

TABLE 1: RESPONSES TO THE QUESTION: "HOW WOULD YOU DESCRIBE YOUR FINANCIAL SITUATION NOW, COMPARED WITH WHEN YOU WENT INTO BANKRUPTCY COURT?"

Answer	Percent
Much better	34
A little better	29
About the same	28
Even worse	8
Much worse	2

n=400
Source: 1966 interviews with former bankrupts, Stanley and Girth at 67

These responses demonstrate that among those who filed Chapter 7 bankruptcy, more than one in three families experienced financial situations that were the same as or worse than at the time of their bankruptcies. The remaining 63% of families reported that their financial situations two years postbankruptcy were either a little better or much

62 *See* Jay Lawrence Westbrook, *Empirical Research in Consumer Bankruptcy*, 80 TEX. L. REV. 2123, 2147 (2002) (characterizing the state of knowledge about what happens to debtors postbankruptcy as "silence"); *see generally* Power, Hira & Murphy, *supra* note 49, at 82 (comparing the number of personal bankruptcies filed between 1980 and 1996 under Chapters 7, 11, and 13).

63 A published study of Australian debtors does exist. *See* MARTIN RYAN, THE LAST RESORT: A STUDY OF CONSUMER BANKRUPTS (1995). Ryan conducted interviews with seventy-six debtors who had filed bankruptcy in the prior seventeen months. *See id.* at 80. Under the Australian bankruptcy system, these debtors were not yet eligible for a discharge of their debts. *See id.* at 7–8. Differences in the American and Australian bankruptcy laws and in the demographics of bankruptcy filers in the two countries sharply limit the applicability of Ryan's findings to American debtors.

64 Bankruptcy Act of 1898, ch. 541, 30 Stat. 544 (repealed 1978).

65 *See* STANLEY & GIRTH, *supra* note 16, at 41.

66 *See id.* at 66–67.

better than when they declared bankruptcy.[67] These findings suggest that Chapter 7 bankruptcy produced mixed results. While a majority of families reported improved financial situations, a substantial minority remained in financial hardship similar to or worse than what they faced when they initially sought bankruptcy relief.[68] These data suggest that a discharge of debt does not adequately equip all families with the capacity to avoid future financial difficulties.

However, Stanley and Girth's research has several limitations. First, the study is decades old.[69] The researchers conducted the study before the enactment of the 1978 Bankruptcy Code,[70] a major revision to U.S. bankruptcy law.[71] Economic conditions have also changed in the last several decades, including job stability, availability of consumer credit, and family structures.[72] Second, Stanley and Girth provided only minimal discussion of their postbankruptcy data.[73] For example, they failed to discuss how such data intersect with the theoretical construct of the fresh start or any specific provisions of the Bankruptcy Code. Finally, data collection problems hindered a rich analysis of their findings. In their initial study of debtors, they collected demographic and financial data from a large sample of consumer debtors.[74] At the time of the interviews, however, the researchers were unable to locate any substantial portion of this original sample and had to construct a new sample for their interviews.[75] This technique prevented Stanley and Girth from correlating the postbankruptcy findings with the demographic and court record data and sharply limited their ability to determine the shared characteristics of debtors who reported different levels of postbankruptcy financial well-being.

Notwithstanding these limitations, it is surprising that no scholar has seized on Stanley and Girth's postbankruptcy data. Such knowledge is critical both to evaluate the adequacy of the bankruptcy system and to understand how a discharge of debt affects the economic circumstances of individuals. This failure to explore the consequences

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67 *See id.* at 67.

68 *See id.*

69 *See id.* at 6 n.1, 7.

70 *See id.*

71 *See* Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended in scattered sections of 11 U.S.C.).

72 *See generally* ROBERT D. MANNING, CREDIT CARD NATION: THE CONSEQUENCES OF AMERICA'S ADDICTION TO CREDIT (2000) (documenting access to credit); KATHERINE S. NEWMAN, FALLING FROM GRACE: DOWNWARD MOBILITY IN THE AGE OF AFFLUENCE (1999) (discussing increased job instability); ELIZABETH WARREN & AMELIA WARREN TYAGI, THE TWO-INCOME TRAP: WHY MIDDLE-CLASS MOTHERS AND FATHERS ARE GOING BROKE (2003) (explaining changes in family structures).

73 *See* STANLEY & GIRTH, *supra* note 16, at 66–67.

74 *See id.* at 41.

75 *See id.*

of bankruptcy probably has both practical and theoretical explanations. Because there is rarely any court interaction with consumer debtors after their debts are discharged, postbankruptcy research cannot rely on public court filings, published opinions, or regulatory records. Further, conducting such longitudinal research is expensive and time consuming, because it requires creating data instruments and analyzing primary data.[76] Legal scholars have therefore eschewed postbankruptcy research in favor of examining debtors during bankruptcy, at which point the practical barriers, though formidable, are fewer.

The extraordinary nature of the discharge as a theoretical remedy may also distract attention from measuring postbankruptcy outcomes. The transformative power of bankruptcy has a strong allure in America, a land touted for its second chances and opportunities for renewal.[77] American bankruptcy law provides the most generous debt relief system in the world,[78] which may explain the predominance of the untested assumption that discharge is an effective cure. The discharge is typically glorified without empirical examination: "The advantages of bankruptcy are typically so profound that people who struggle to repay their debts, rather than having them erased, are often seen as foolish for continuing to throw good money after bad debts."[79] Such statements construct a view of the bankruptcy discharge as costless and miraculously transformative. Many assume that discharge guarantees a life free of further financial strain.[80] However, this view exaggerates the legal consequences of bankruptcy discharge, which the law carefully circumscribes. The legal construct of a discharge of past debt does not insulate families from experiencing financial hardship again and struggling with the same types of situations, such as job loss, that led to their overindebtedness.[81]

During the recent debates over consumer bankruptcy reform, Congress portrayed Chapter 7 bankruptcy as fast, painless, and easily abused. In 2005, Senator Chuck Grassley stated that bankruptcy " 'was

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76 *See, e.g.*, SULLIVAN, WARREN & WESTBROOK, *supra* note 22, at 263–87.

77 *See* BRUCE H. MANN, REPUBLIC OF DEBTORS: BANKRUPTCY IN THE AGE OF AMERICAN INDEPENDENCE 255–56 (2002) (describing how passage of America's first federal bankruptcy act was influenced by recognition that debt was an inevitable part of an entrepreneurial, commercial economy).

78 *See* Nathalie Martin, *The Role of History and Culture in Developing Bankruptcy and Insolvency Systems: The Perils of Legal Transplantation*, 28 B.C. INT'L & COMP. L. REV. 1, 28–29 (2005) ("The U.S. personal bankruptcy system is unquestionably the most forgiving in the world, and strongly encourages persons who have failed financially to get back into the economy and try again.").

79 Liz Pulliam Weston, *Why Going Broke Is a Fact of Life in America*, http://moneycentral.msn-ppe.com/content/Banking/bankruptcyguide/P102899.asp (last visited May 19, 2006).

80 *See supra* text accompanying notes 1–4.

81 *See infra* Parts II.B & III.A.

not intended to be a convenient financial planning tool where deadbeats can get out of paying their debt scott-free [sic] while honest Americans who play by the rules have to foot the bill.'"[82] Five years before, Republican Representative Bill McCollum of Florida complained that "bankruptcy has become a first stop rather than a last resort."[83] These descriptions reflect an assumption that an immediate discharge of debt is a generous remedy that provides easy relief to those who file bankruptcy.

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 restricts access to Chapter 7 bankruptcy.[84] This change in bankruptcy policy may reflect Congress's belief that an immediate fresh start is such a generous benefit that it should be limited to those who are judged truly needy because they lack the means to pay their debts. However, no data support this rosy view about the benefits of bankruptcy, and once again, the fresh-start policy was articulated in a theoretical vacuum rather than informed by empirical reality.

The shortage of research on what happens to debtors after bankruptcy has allowed the concept of the fresh start to flourish unchecked. The dominant vision of bankruptcy's fresh start—that debtors simply "bounce back from financial failure"[85]—has obfuscated the complex realities of life postbankruptcy. Stanley and Girth's research suggests that although a majority of families report improved financial situations in the years after their bankruptcies, many do not.[86] However, the full implications of their findings have gone unrecognized, and scholars have failed to study how and why a substantial percentage of formerly bankrupt families continue to experience financial hardship. Without an understanding of why many families remain in distress after bankruptcy, it is impossible to evaluate the efficacy of the bankruptcy system. The rhetoric of rehabilitation has masked the realities of the fresh start and fundamentally limited a complete assessment of bankruptcy law in action.

C. Methodology and General Findings

The data in this Article were collected during Phase III of the Consumer Bankruptcy Project, a large, multiresearcher, multistate

82 Press Release, U.S. Sen. Chuck Grassley, *Grassley Renews Effort to Reform Bankruptcy Code* (Feb. 2, 2005), http://grassley.senate.gov/index.cfm?FuseAction=PressReleases.Detail&PressRelease_id=4873&Month=2&Year=2005 [hereinafter Grassley February Press Release].

83 *Bankruptcy Reform Act of 1998: Hearing on H.R. 3150 Before the Subcomm. on Commercial and Admin. Law of the House Comm. on the Judiciary*, 105th Cong. 8 (1998) (statement of Rep. McCollum).

84 *See* Pub. L. No. 109-8, 119 Stat. 23, 27 (to be codified at 11 U.S.C. § 707(b)).

85 Weston, *supra* note 79.

86 *See* STANLEY & GIRTH, *supra* note 16, at 66–67.

study of consumer bankruptcy.[87] The research sample consists of consumer bankruptcy cases filed in the first months of 2001 in five judicial districts across the nation. The core sample contains 1,250 consumer bankruptcy cases. The ratio of sampled Chapter 7 and Chapter 13 cases reflected the distribution in each judicial district. Consequently, we gathered data on 780 Chapter 7 bankruptcies and 470 Chapter 13 bankruptcies.

The Consumer Bankruptcy Project used three instruments to gather data. First, a questionnaire was distributed to debtors at the mandatory meetings of creditors.[88] The questionnaire requested demographic information such as age, occupation, and marital status, and inquired about the family's reasons for seeking bankruptcy relief. For each debtor who completed a questionnaire, we collected data from the corresponding public court records, including the bankruptcy petition and schedules. This second data instrument yielded information about the debtors' assets, liabilities, income, and expenses at the time of their bankruptcies.

The questionnaire invited debtors to participate in a series of three follow-up telephone interviews in return for compensation of fifty dollars per interview. These telephone interviews comprise the third method of data collection. Approximately one year after their bankruptcies, 930 debtors completed telephone interviews. The data presented in this Article were generated from a subsample of 359 interview participants who filed Chapter 7 bankruptcy.[89] This subsample captures 46% of the 780 Chapter 7 cases in the study's core sample.[90] A small team of trained researchers conducted telephone interviews that were approximately one hour long. Responses to the

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87 We each served as Project Director of the Consumer Bankruptcy Project for a period. Our responsibilities included overseeing the data collection process. The other professors who contributed to the design and implementation of the study were David Himmelstein, Robert Lawless, Bruce Markell, Michael Schill, Teresa Sullivan, Susan Wachter, Elizabeth Warren, Jay Lawrence Westbrook, and Steffie Woolhandler. A fuller discussion of the Consumer Bankruptcy Project's methodology is available in the Appendix.

88 *See* 11 U.S.C. § 341 (2000).

89 Families who filed Chapter 13 bankruptcy are ineligible by law to receive a discharge until three to five years after their bankruptcy filings. *See* 11 U.S.C.A. § 1325(b)(4)(A) (West 2005). The experiences of Chapter 13 debtors while they are repaying their debts offer a rich field for further study but are beyond the scope of this Article.

90 Because the contact information that many of the debtors provided was no longer correct, we were unable to reach them for an interview. Consequently, our data may overrepresent the economic stability of the postbankruptcy population. That is, those who could not be located may be the most financially distressed group, considering that they moved and changed telephone numbers in the immediate aftermath of their bankruptcies. In anticipation of this problem, we asked debtors to provide us with two alternative contacts, which increased the response rate. Nevertheless, some debtors gave only their own information, and sometimes, we were still unable to locate them.

interviews were coded into a specially designed database.[91] Most questions were close-ended, and many were designed to explore families' postbankruptcy financial status.

Primary petitioners in the subsample averaged forty-three years old. Approximately one-third were married and living with a spouse, while another 7% were married but living separately. The median occupational prestige score was 36;[92] this score represents occupations such as office clerk, bricklayer, teacher's assistant, and steel worker. Approximately 32% of the respondents reported that they owned their homes at the time of filing. When we reviewed the economic variables, we found a wide range of incomes. Eight debtors, or just over 2% of the sample, reported no income whatsoever. At the other end of the spectrum, one debtor reported annual earnings of just over $101,000. Overall, median annual income for the subsample was $21,870 and median unsecured debt was $27,573.

Debtors who completed the telephone interviews were self-selected, introducing the possibility of respondent bias.[93] To test for this bias, we compared interview participants and nonparticipants on several important demographic and economic variables. Demographically, the two groups were comparable on the variables of age, employment status, and homeownership. However, interview participants were significantly more likely to be single and white than those who did not complete interviews. Analysis of the economic variables did not reveal any statistically significant differences between the two groups. Debtors' court records revealed similar incomes, assets, and liabilities. Overall, we conclude that our subsample was representative of the 780 Chapter 7 cases that comprised the Consumer Bankruptcy Project's core sample.[94] To further test the validity of our sample, we compared it to the samples that previous bankruptcy studies used. These studies measured common demographic and economic characteristics of debtors, such as age, marital status, occupational prestige score, homeownership, median annual income, and median unsecured debt.[95] The data from our subsample are consistent with prior profiles of families who filed bankruptcy. We con-

91 Katherine Porter & Deborah Thorne, Debtor Survey Responses, Consumer Bankruptcy Project, Phase III 1 (2001) (on file with authors).

92 *See* SULLIVAN, WARREN & WESTBROOK, *supra* note 58, at 89–91 (describing the occupation prestige score that the U.S. Census bureau uses).

93 *See* EARL BABBIE, THE PRACTICE OF SOCIAL RESEARCH 187–89 (10th ed. 2004).

94 See *infra* Appendix for further detail on the participant and nonparticipant analyses.

95 *See* SULLIVAN, WARREN & WESTBROOK, *supra* note 22; WARREN & TYAGI, *supra* note 72; *see generally* Elizabeth Warren, *The New Economics of the American Family*, 12 AM. BANKR. INST. L. REV. 1 (2004).

clude, like other researchers,[96] that most debtors are demographically similar to middle-class Americans but earn much lower incomes at the time of their bankruptcies.

We generated the analysis presented in this Article from two main lines of inquiry that we designed for the telephone interviews. First, we asked interview participants if at the time of the interview they were experiencing any financial difficulties. We were interested in how many families were struggling postbankruptcy and what types of financial problems they were facing. We also asked participants to compare their financial situations at the time of their bankruptcies with their situations at the time of the interviews, approximately one year postbankruptcy. From these principal data points, we are able to explore whether and how Chapter 7's discharge of debt affects the financial future of former debtors.

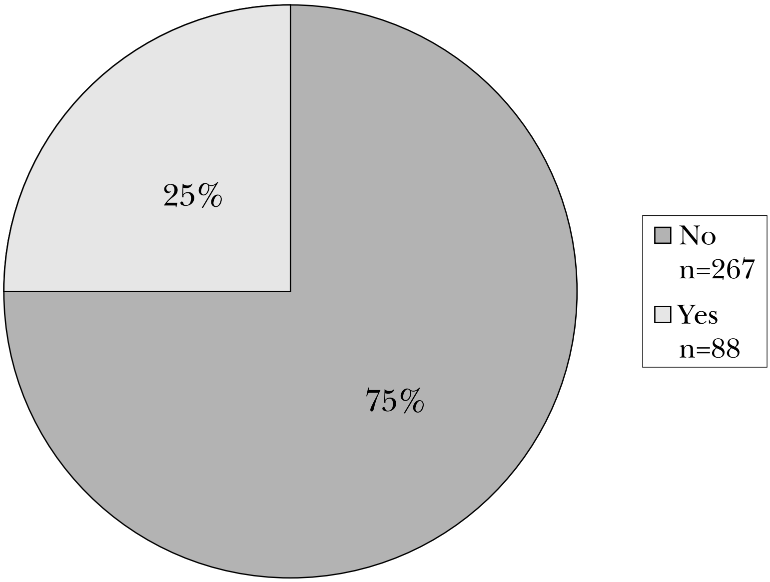
II
The Postbankruptcy Experiences of Chapter 7 Debtors

A. Struggling to Make Ends Meet

Our initial analysis examined how the families in our subsample dealt with their postbankruptcy financial obligations. Our interest was twofold. First, we wanted to measure families' postbankruptcy financial health. Were they able to pay new bills after the discharge released them from their past unsecured debts? Second, we wanted to examine what a troubled financial situation meant in the context of families' daily lives. When families continue to experience hardship after bankruptcy, how does this translate into the everyday realities of making ends meet? To explore these issues, we began by asking debtors the following question: "Do you have any debts that you are currently having difficulties paying?" As Figure 1 shows, a full quarter of debtors in our subsample affirmed that they struggled to pay some debts postbankruptcy.

96 *See* Sullivan, Warren & Westbrook, *supra* note 22, at 27; Elizabeth Warren, *Financial Collapse and Class Status: Who Goes Bankrupt?*, 41 Osgoode Hall L.J. 115, 124–25, 144 (2003).

FIGURE 1: PERCENT OF DEBTORS HAVING DIFFICULTY PAYING DEBTS



These former debtors had already received an immediate discharge of most of their unsecured debt, a mechanism many herald as a means to reenter the consumer economy.[97] Despite this relief, 25% of families reported postbankruptcy financial stress. In light of the rhetoric about Chapter 7 bankruptcy allowing debtors to get off "scott-free [sic],"[98] these data are a powerful reminder that a fresh start does not equal a free ride. In the year following bankruptcy, these families still confronted twelve months of new expenses. Thus, the Chapter 7 discharge—the "holy grail of debt relief"[99]—does not generate adequate income. Postbankruptcy, new bills remain a challenge for a significant number of families. This finding reveals the precarious economic circumstances that many families face after filing bankruptcy.

One hypothesis as to why some families continue to experience financial problems is that debtors are inherently profligate.[100] Proponents of this perspective might assert that bankrupt families are spendthrifts who simply continue their pattern of frivolous spending after bankruptcy. Our data challenge this view. Our research asked debtors who reported having difficulties paying their postbankruptcy

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97 *See* REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 93-137, pt. 1, at 71, 79–80 (1973).

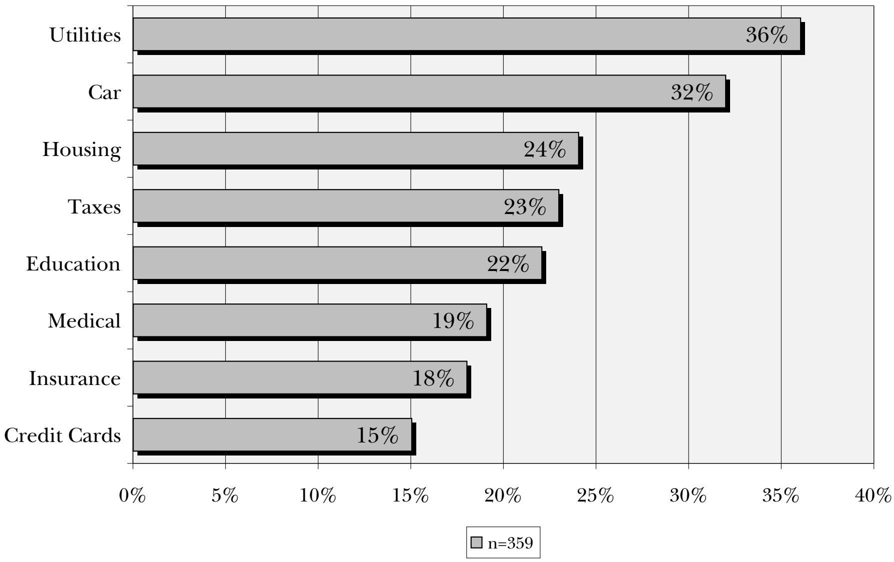
98 *See* Grassley February Press Release, *supra* note 82.

99 MANN, *supra* note 77, at 177.

100 *See* Edith H. Jones & Todd J. Zywicki, *It's Time for Means-Testing*, BYU L. REV. 177, 183 (1999) ("Society should not broadly afford relief to well-off, able bodied debtors when poorer people, who have not elected that remedy, struggle to keep their commitments and live within their means.").

bills to choose the sources of their hardship from a list of multiple types of debts.[101] We designed this question to reveal which specific expenses troubled families after bankruptcy. Figure 2 illustrates these findings.

FIGURE 2: TYPES OF BILLS THAT FAMILIES ARE STRUGGLING TO PAY



The postbankruptcy expenses that families struggled to pay were mundane. More than one-third of the families reported that it was difficult to pay their monthly utility bills, such as heat, electricity, water, phone, or garbage. Approximately one in three families struggled with car payments or car repairs. An African-American debtor from California described how, despite some improvements following bankruptcy, he was still struggling to keep current on his car payments: "I am catching up now. I have a job and can afford to eat. I am still hiding my car so they won't repo[ssess] it. I am still a couple of payments behind on that."[102] This debtor's fear of losing his car illustrates the desperation that many families feel as they cling to the slender reed of hope that the fresh start offers. Even more alarming, about one-fourth of families found it hard to make their mortgage or rent payments after bankruptcy. Thus, even without the burden of debt, many postbankruptcy debtors struggle to meet their families' basic needs.

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[101] The exact language we used was, "Do you have any debts that you are currently having difficulties paying?" If the debtor said yes, we then asked him or her, "What types of debts are those?" The answer options were the following: medical bills, mortgage or rent payments, credit card bills, utility bills, car payments or repairs, taxes, insurance payments, student loans, and child support or alimony payments.

[102] Porter & Thorne, *supra* note 91 (quoting survey respondent CA-07-055).

These data illustrate another important point: These families are not struggling because they are misusing credit. Rather, the debts that worry these families, such as utilities, transportation, housing, and taxes, are mostly for necessities and are frequently not even "credit" purchases; utilities, housing, and transportation are normally prepaid or carry a deposit to protect the merchant. Credit cards were a problem for fewer than one in six families. One year postbankruptcy, families are not borrowing themselves back into debt. Their difficulties arise from trying to meet typical middle-class expenses: keeping a roof over their family's heads, fixing their car's radiator, or repaying the family doctor.

Many families who emerge from bankruptcy do not live in financial ease; in fact, financial stress characterizes their postbankruptcy lives. One-fourth of families continue to struggle to pay ordinary monthly bills. Clearly, the everyday expenses of middle-class families do not end with a bankruptcy court's stamp on a discharge order. Filing bankruptcy is a dose of the law's strongest medicine for financial distress, and the fact that this remedy proves insufficient for 25% of families suggests that we must reappraise the power of the fresh start.

B. Postbankruptcy Financial Situations

A second measure of postbankruptcy financial well-being examined how debtors' overall financial situations had changed after bankruptcy. Each family was asked the following question: "Overall, since you filed for bankruptcy, has your financial situation improved, stayed about the same, or worsened?" For comparison, we modeled this question on the inquiry that Stanley and Girth had used in their bankruptcy study.[103] The available response options were objective; we did not ask debtors to apply subjective labels such as "good" or "bad" to their situations. In addition, families were not asked to rate their financial situations in terms of external criteria, such as by using phrases like "compared to other Americans." Such results would not be helpful because we would expect bankrupt families to require time to accumulate savings and establish security equal to that of their nonbankrupt counterparts. Instead, we intended the question's design to elicit a comparison between the family's financial situation at the time of the bankruptcy filing and at the time of the interview, one year postbankruptcy.[104] Based on the powerful relief that the dis-

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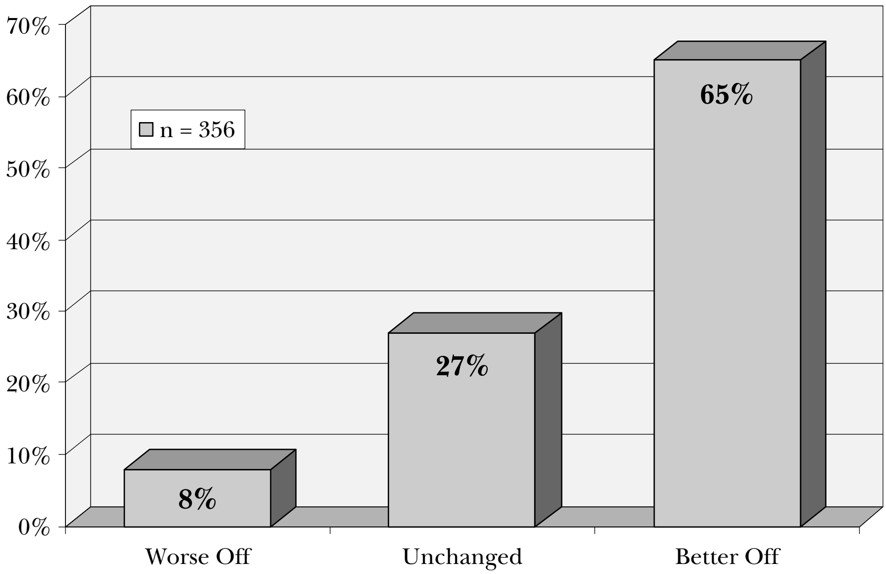
103 STANLEY & GIRTH, *supra* note 16, at 66 ("How would you describe your own financial situation now, compared with when you went into bankruptcy court?").

104 The question's wording was potentially ambiguous. We believed that debtors would interpret the question such that they would compare their current situations with their situations at the time of bankruptcy. Some respondents may have assumed that

charge supposedly affords and the rhetoric of rehabilitation that surrounds consumer bankruptcy, we expected that the immediate discharge in Chapter 7 bankruptcy would translate to dramatic economic improvement for nearly all families.

Figure 3 illustrates responses to the inquiry about whether debtors' financial situations had "improved," "stayed about the same," or "worsened." Throughout the discussion, we shall refer to the three groups in shorthand: "better-off families," "unchanged families," and "worse-off families."

FIGURE 3: POSTBANKRUPTCY FINANCIAL SITUATIONS OF FAMILIES



The majority, 65% of families, reported that their financial situations had improved since they filed bankruptcy. The Chapter 7 discharge appears to have worked effectively to reduce or eliminate the hardship facing these families. Free from most past debts, these families are able to concentrate their future income on ongoing expenses rather than struggling with overwhelming old debt. Although the power of the discharge may lead some observers to expect that the percentage of families with improved financial situations would be even higher, these results are generally heartening. From these data, it appears that approximately two in three families have achieved a meaningful

"since you filed for bankruptcy" referred to the period immediately following bankruptcy. However, because the discharge of debt normally occurs at least sixty days after filing bankruptcy, families still had liabilities for a period after their bankruptcy filings. Therefore, even if the survey respondents did interpret the question as asking about the time immediately following their bankruptcy, the potential ambiguity is moot. The families were likely all comparing their financial situations, including the debts that they brought to bankruptcy, with their situations after discharge.

fresh start after bankruptcy and are on the road to financial health. Additional longitudinal study would help measure whether these families are able to sustain their improved circumstances, but these initial data offer convincing evidence that bankruptcy often succeeds in improving families' financial health.

For a substantial minority of families, however, postbankruptcy life did not fulfill the optimistic promise of the fresh start. More than one in three families stated that their financial situations had either stayed the same or worsened since the time of their bankruptcies. Over a quarter of families reported that their financial circumstances were unchanged; things were, financially speaking, as bad now as when the families went bankrupt. Another 8% of families reported that their financial situations had worsened, which is the exact opposite of the expected outcome of Chapter 7's fresh start. One in twelve households was not just in financial trouble after bankruptcy—they actually perceived that their postbankruptcy financial problems exceeded the problems they had when they initially sought bankruptcy relief. We emphasize the comparative nature of these data, because it makes our finding even more compelling. The families whose situations are unchanged or worse are not merely reporting that they have some modicum of financial strain, which may be an expected part of adjusting after a financial crisis. Instead, 35% of families indicated that they continued to experience financial problems equivalent to or more severe than those that drove them to seek bankruptcy relief in the first place. Extrapolating from our sample to the population of bankrupt households, we estimate that approximately 361,000 families of the 1.03 million families who filed Chapter 7 nonbusiness bankruptcy in 2001 were in the same or worse financial health one year later.[105] For these families, the immediate discharge in Chapter 7 bankruptcy appears to have been inadequate.

These data highlight a critical reality about the bankruptcy system and should give pause to those who bemoan the generosity of Chapter 7 bankruptcy. The most fundamental assumption of consumer bankruptcy—that the fresh start results in a productive end—is suspect. Life after bankruptcy is not unequivocally better for many families. These findings are a powerful reminder of the limitations of the consumer bankruptcy system. Although many describe bankruptcy as a

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105 *See* News Release, Admin. Office of the U.S. Courts, Table F-2 U.S. Bankruptcy Courts, Business and Nonbusiness Bankruptcy Cases Commenced, By Chapter of the Bankruptcy Code, During the 12-Month Period Ending December 31, 2001 (Feb. 19, 2002), http://www.uscourts.gov/Press_Releases/1201f2.xls. We estimate that 278,500 of families who filed consumer Chapter 7 cases in 2001 are likely to be in a financial situation that is unchanged since their bankruptcy. Another 82,520 families are likely to be worse off financially now than they were before they sought relief under Chapter 7.

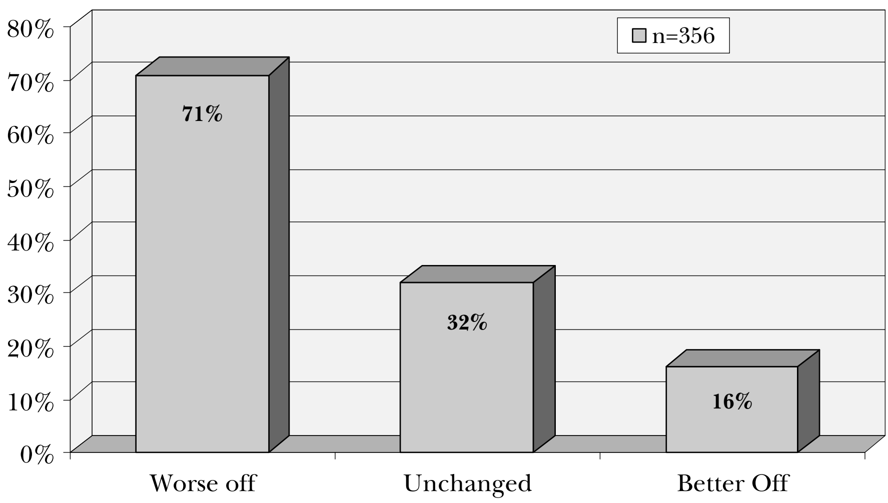
"safety net" for families,[106] its ability to buoy up families appears to be more fragile and incomplete than often assumed.

C. Broke After Bankruptcy: The Plight of the Worse-Off Families

We compared families' postbankruptcy financial situations with their reported abilities to meet their current bills. This allowed us to explore how poor financial health after bankruptcy translated into immediate difficulty in making ends meet. We conclude that worse-off families are struggling because they do not have adequate income to cover even their most basic expenses. Unless these families can either increase their income or reduce their expenses, they will likely face another economic collapse. Examining the plight of worse-off families sheds light on the limitations of the bankruptcy system's ability to ensure a fresh start for all debtors.

Figure 4 illustrates the relationship between a family's postbankruptcy financial situation and the likelihood that the family continued to have difficulty paying bills.

FIGURE 4: PERCENT OF FAMILIES STRUGGLING TO PAY BILLS BY POSTBANKRUPTCY FINANCIAL SITUATION



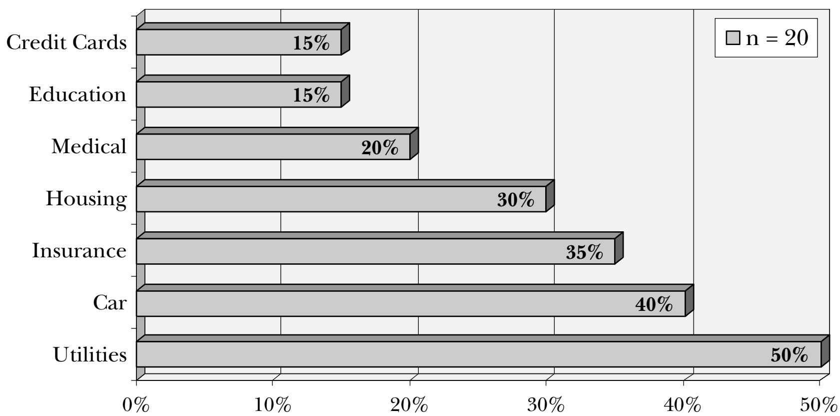
Among worse-off families, 71% reported that they struggled to pay their bills. Compared to families whose financial situations had improved, worse-off families were about 4.5 times more likely to have difficulty making ends meet. These data corroborate that worse-off

106 *See, e.g.*, Katherine Porter, *Going Broke the Hard Way: The Economics of Rural Failure*, WIS. L. REV. 969, 1019 (2005) (discussing the importance of bankruptcy as a "safety net" for rural families); *see generally* Susan Block-Lieb, *Mandatory Protections As Veiled Punishments*, 69 BROOK. L. REV. 425, 425–27 (2004) (referring to consumer bankruptcy discharge as a "safety net").

families continue to experience financial distress similar to their prebankruptcy struggles. Unchanged and better-off families reported notably less difficulty paying their debts. However, even among families who reported an unchanged financial situation, one in three struggled to meet postbankruptcy bills. Among the better-off families, this number dropped to about one in six.[107] The findings in Figure 4 reveal that difficulty paying postbankruptcy bills correlates with chronic financial distress that continues despite bankruptcy.

For the worse-off families, financial distress translates into experiencing serious privation after bankruptcy. As Figure 5 illustrates, these families report difficulty paying routine bills for their households' basic needs. Half of worse-off families are having trouble paying their utility bills. Forty percent cannot afford the costs of their cars or car repairs. Thirty percent struggle to make their rent payments.[108]

FIGURE 5: TYPES OF BILLS THAT WORSE-OFF FAMILIES ARE STRUGGLING TO PAY



The consequences of filing bankruptcy exacerbate the hardship that worse-off families experience. As a 28-year-old debtor from Texas explains,

> My finances have worsened since I filed bankruptcy, because even though I'm back at my job, I had to take a pay cut. It's harder now. Since I filed bankruptcy, I had to put down an extra deposit on an apartment in order to get it; but at least I did get one.[109]

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107 The differences among the three groups were statistically significant. Throughout the paper, we interpret statistical significance as $p < 0.05$.

108 Fewer than one in five (18%) of the worse-off families owned their homes. The remaining 82% either rented or lived with family.

109 Porter & Thorne, *supra* note 91, at 5 (quoting survey respondent TX-07-042).

For the worse-off families, bankruptcy may signal a renewed period of financial distress instead of the end of such struggles.

The worse-off families were generally struggling with the same types of debts as the unchanged and better-off families. This suggests that worse-off families are typical in the types of financial pressures they face. The only statistically significant exception among the percentages of better-off, unchanged, and worse-off families that owe expenses was insurance bills. Only 8% of the better-off families struggled to pay insurance premiums. In contrast, 35% of worse-off families reported that paying insurance premiums was a problem. This finding is alarming in light of the role of insurance in preventing financial disaster. A worse-off family can least afford a large, sudden expense, yet it is four times more likely than a better-off family to be struggling to keep current on insurance premiums. Worse-off families' inability to pay for insurance puts them at a much greater risk of another financial collapse in the future as a result of catastrophic debt from severe illness, natural disaster, an accident, or other sudden hardship.

A vast majority of worse-off families cannot stretch their meager incomes far enough to cover their current expenses. The data show that worse-off families are not awash in rash credit expenses but instead are struggling to meet routine monthly expenses. Their difficulties arise from bills that typical middle-class families face each month: utilities, insurance premiums, and medical expenses. These are not areas of luxury spending. Further, worse-off families are not spendthrifts. For example, the median worse-off family spent $582 for housing when it filed bankruptcy, which is significantly less than the $620 that the median better-off family spent.[110] Neither group is profligate. Indeed worse-off families are making do on less.

At the time of its bankruptcy, the median worse-off family earned an annual income of $20,718. The median income for the sample was only slightly higher, at $21,870.[111] Worse-off families should not be castigated for their failure to make ends meet on these incomes. These families are earning incomes near the poverty threshold for a family of four, which in 2001 was $18,104.[112] Indeed, in 2000, a ma-

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110 We obtained these figures from the Schedule J that each debtor in our sample filed. Schedule J is part of the official court records that each debtor must file in a bankruptcy case. SCHEDULE J—CURRENT EXPENDITURES OF INDIVIDUAL DEBTOR(S) (2005), *available at* http://www.uscourts.gov/rules/Revised_Rules_and_Forms/BK_Form_B6J.pdf. These records are publicly available. See *infra* Appendix for further information.

111 The median annual income of better-off and unchanged families was $22,884 and $19,332, respectively. These amounts were not significantly different from the median annual income of worse-off families.

112 *See* U.S. CENSUS BUREAU, POVERTY 2001, http://www.census.gov/hhes/poverty/threshld/thresh01.html (last modified Sept. 24, 2002). The poverty threshold in 2001 for a family of two was $11,569 in annual income. *See id.*

jority of Americans stated that a family needed $35,000 just to get by.[113] Worse-off families are facing future economic collapse because retooling their expenses to match their incomes is either impossible or, at minimum, will require a program of sacrifice and deprivation that families are unable to implement in the year immediately following bankruptcy.

The problems facing Monique, a debtor from California, illustrate the difficulty in recovering after bankruptcy. Monique explained that the noise level in her neighborhood was so high that she was unable to sleep, and her numerous medical problems—fibromyalgia, rheumatoid arthritis, and a sleeping disorder—were worsening.[114] She said that she wanted to move, but the cost was prohibitive:

> I have no choice, I can't get better here. I don't know how I'll make it. I will have to plan very carefully, because my income won't change. I have to make it on what I have, and that isn't going to be easy. Also, I worry about not being able to rent anything with the bankruptcy on my credit report.[115]

If unpaid, the bills confronting the worse-off families will undoubtedly result in crisis. If a utility payment is late, families will have to do without heat, lights, or water. If a landlord does not get the full rent owed under the lease, a family will face eviction or even homelessness. If a car payment is missed, repossession is imminent and transportation to work is threatened. Falling behind on these bills is not just embarrassing and inconvenient; it means that just as they were before bankruptcy, these families are once again teetering on the edge of financial catastrophe. If they do not improve their financial conditions, these families risk collapse as self-sufficient economic units. Because a Chapter 7 discharge is only available every eight years,[116] bankruptcy relief either will be unavailable or will take the form of a repayment plan under Chapter 13. Alternatively, these worse-off families may continue to decline in well-being until they are eligible for government support, such as food stamps or subsidized housing. Further longitudinal study is necessary to understand how the worse-off families fare beyond one year after bankruptcy. Understanding the trajectory of their financial decline reveals how bankruptcy fails to help debtors make a lasting financial recovery.

While Chapter 7 bankruptcy improves the financial lives of a majority of families who seek relief, one in four continues to struggle

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113 *See* JOBS FOR THE FUTURE, A NATIONAL SURVEY OF AMERICAN ATTITUDES TOWARDS LOW-WAGE WORKERS AND WELFARE RELFORM [sic] 3 (2000), *available at* http://www.listproc.bucknell.edu/archives/femecon-l/200209/pdf00001.pdf.

114 *See* Porter & Thorne, *supra* note 91, at 9 (survey respondent CA-07-002).

115 *See id.*

116 *See* 11 U.S.C. § 727(a)(8) (2000).

with bills, and one in three families finds that a year after bankruptcy, its financial situation has deteriorated or remains strained. These principal findings call into question the rehabilitative realities of bankruptcy. For many families, the fresh start either never materialized or quickly went stale. Instead, the bankruptcy discharge signaled little more than the beginning of another long period of trying—but apparently failing—to make ends meet. Bankruptcy certainly reduced these families' total debt levels and provided a temporary reprieve from creditor pressures. However, the bankruptcy discharge did not produce lasting financial relief. The remainder of this Article explores the nuances behind these data in an effort to understand the differences between families who recover financial health and those who continue to struggle and analyzes the implications of these findings for the consumer bankruptcy system.

III
Explaining Postbankruptcy Distress: What Went Wrong?

Results from three decades of consumer bankruptcy research reveal that two principal factors propel debtors into the financial crises that precipitate their bankruptcies: job problems and medical problems.[117] These are the issues that most affect households *before* bankruptcy. Whether they are predictive of how families fare *after* bankruptcy has been largely speculative. We sought to understand what factors debtors believe contributed to their postbankruptcy financial difficulties. Our analysis suggests that the key determinant of postbankruptcy financial health is income stability. Factors that dampen income potential, such as old age, correlate with worsened postbankruptcy outcomes. Job and medical problems continue to be the leading reasons cited by families in financial distress, and a close analysis of the postbankruptcy data shows that these problems' negative impact on income undermines families' attempts to recover. Constructing effective bankruptcy relief requires a primary focus on income, rather than the current law's emphasis exclusively on addressing debt.

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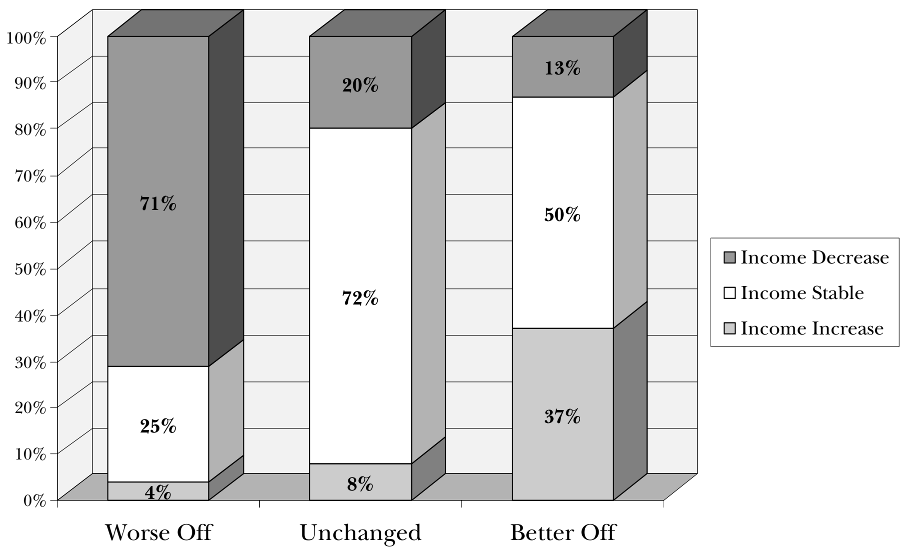
117 *See* Sullivan, Warren & Westbrook, *supra* note 22, at 75–107, 141–71; Sullivan, Warren & Westbrook, *supra* note 58, at 85–86, 166–75; Warren & Tyagi, *supra* note 72, at 81–82 (discussing how job and medical problems are most likely to trigger consumer bankruptcy); David U. Himmelstein et al., *Market Watch: Illness and Injury as Contributors to Bankruptcy*, Health Aff., Feb. 2005, *available at* http://content.healthaffairs.org/cgi/reprint/hlthaff.w5.63v1.pdf (analyzing the connection between illness or injury and personal bankruptcy).

A. The Primacy of Income

During the interviews, worse-off families were asked to identify the circumstances that explained their diminished financial situations after bankruptcy.[118] The options from which families could choose were prebankruptcy job problems, postbankruptcy job problems, prebankruptcy illness or injury, postbankruptcy illness or injury, death in the family, birth of a child, divorce or separation, major home repairs, other recent expenses, and an ongoing problem of too much debt and too little income.[119] By asking debtors to identify the reasons for their postbankruptcy income changes, we were able to isolate postbankruptcy income as the critical factor.[120] To capture only significant income changes, debtors were asked in the interviews whether their income "increased by 10% or more," "stayed the same," or "decreased by 10% or more." Debtors' responses reveal a strong and statistically significant relationship between a family's postbankruptcy change in income and that family's postbankruptcy financial situation. Figure 6 shows this correlation.

FIGURE 6: POSTBANKRUPTCY FINANCIAL SITUATIONS BY CHANGES IN INCOME



Compared to the other groups, worse-off families were much more likely to have experienced a postbankruptcy decline in income.

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118 This set of questions was posed only to families who reported that their financial situations had worsened since bankruptcy.

119 Multiple responses were permissible.

120 The question posed to debtors read as follows: "Since your bankruptcy, has there been a significant change in your household income? Has your income increased by 10 percent or more, stayed about the same, or decreased by 10 percent or more?"

In fact, worse-off families were *five and a half times* more likely than better-off families to report an income drop of at least 10%. While more than one-third of better-off families reported an increase in income, only 4% of worse-off families reported the same. Measured against the worse-off families, better-off families were nearly ten times more likely to have experienced a rise in income. Families who reported that their financial situations had remained unchanged were also most likely to have experienced unchanged or stable income levels. The relationship between postbankruptcy income change and postbankruptcy financial outcome is unmistakable.

When asked to explain their worsened situations, over two-thirds (68%) of worse-off families indicated an "ongoing problem of too much debt and too little income." Interpreting the meaning of this response is complex. Debtors are obviously struggling to reconcile income and expenses, but we wanted to identify more precisely whether and how postbankruptcy outcomes related to income or debt levels. Our analysis sought to determine whether prebankruptcy financial characteristics correlated with postbankruptcy outcomes.

We began by examining the financial characteristics of families at the time that they filed bankruptcy. Using the court records bankrupt families filed in each bankruptcy case, we extrapolated data on annual household income by multiplying by twelve the family's monthly income at the time of the bankruptcy.[121] The median income of all households in the sample was $21,870.[122] This figure is less than half

[121] Income data come from the Schedule I that each debtor in our sample filed. Schedule I is part of the official court records that each debtor must file in a bankruptcy case. SCHEDULE I—CURRENT INCOME OF INDIVIDUAL DEBTORS (2005), *available at* http://www.uscourts.gov/rules/Revised_Rules_and_Forms/B6I-Fix.pdf. These records are publicly available. See *infra* Appendix for further information. Schedule I requires debtors to report a detailed accounting of current monthly income from both wage and nonwage sources. We include income from all sources. *See* SCHEDULE I—CURRENT INCOME OF INDIVIDUAL DEBTORS (2005), *available at* http://www.uscourts.gov/rules/Revised_Rules_and_Forms/B6I-Fix.pdf. If a married couple filed a joint case, we include income from both people. The Statement of Financial Affairs, which is also part of each debtor's court records, also has data about income; it asks debtors to report their income for the three years prior to filing. FORM 7—STATEMENT OF FINANCIAL AFFAIRS (2005), *available at* http://www.uscourts.gov/rules/Revised_Rules_and_Forms/BK_Form_B7.pdf#search=%22statement%20of%20financial%20affairs%20bankruptcy%22. However, these data were much more likely to be missing or incomplete and to vary in how they were reported. Further, we believe that current income at the time of filing is the best way to understand the immediate financial pressures facing families at the time that they decided to file bankruptcy and therefore draw the income data from Schedule I.

[122] Annual incomes ranged from a minimum of $0 to a maximum of $101,652. The mean annual income for our sample of Chapter 7 debtors was $24,300. Families' annual incomes at the 25th, 50th, and 75th percentiles were $14,220, $21,840, and $31,824, respectively.

the median annual household income in the United States in 2001.[123] The median worse-off debtor had an annual household income of $20,718—a bit more than the median unchanged debtor ($19,332) and a bit less than the median better-off debtor ($22,884).[124] The differences between the groups are not statistically significant.[125] The amount of annual income at the time of filing bankruptcy does not itself appear to be determinative of how a family fares postbankruptcy. Instead, it is the direction of income change that influences whether a family is able to capitalize on the fresh start offered by a bankruptcy discharge. This relationship is illustrated in Figure 6. This conclusion emphasizes that the critical problem that families face postbankruptcy is adjusting their expenses to address the reality of their declining or stagnant incomes. Yet, for the worse-off families, this income-expense adjustment may be an impractical, if not impossible, task. Even if a worse-off family's income declined by only the minimum 10% threshold we established, it would have a household income of approximately $18,650 per year. With so few disposable dollars, many families are having difficulty paying bills for essential living expenses.

Contrary to the academic literature's emphasis on prebankruptcy debt,[126] we were unable to establish any meaningful relationship between the debts that families brought to bankruptcy and their postbankruptcy financial situations. We tallied all unsecured debts that debtors reported in their court records.[127] The median unsecured debt for the sample was $27,573.[128] This is a substantial sum in light of the median debtor's income of $21,870. Although the

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123 The median household income in the United States in 2001 was $42,228. *See* Warren, *supra* note 96, at 125 & n.24 (citing U.S. CENSUS BUREAU, INCOME 2001, *available at* http://www.census.gov/hhes/income/income01/inctab1.html).

124 When we compared annual income using 5% trimmed means, the incomes between the families remained similar. Better-off, unchanged, and worse-off families had median annual incomes of $24,217, $22,617, and $20,838 respectively.

125 We analyzed data using One-Way Analysis of Variance (ANOVA). ANOVA is a method of testing for statistical significance by comparing means of several groups. *See* ALAN AGRESTI & BARBARA FINLAY, STATISTICAL METHODS FOR THE SOCIAL SCIENCES 439 (1997).

126 *See, e.g.*, SULLIVAN, WARREN & WESTBROOK, *supra* note 22; Jill Brader, *Personal Bankruptcy: Not the End of Your Credit World—How a Secured Credit Card Can Give You a Fresh Start*, 12 AM. BANKR. INST. J. 26, 33 (1993); Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, *Consumer Debtors Ten Years Later: A Financial Comparison of Consumer Bankrupts 1981–1991*, 68 AM. BANKR. L.J. 121, 135–39 (1994).

127 The data on unsecured debts are as reported by each debtor in our sample on Schedule F, which is part of the publicly available official court records that all debtors are required to complete. SCHEDULE F—CREDITORS HOLDING UNSECURED NONPRIORITY CLAIMS (2005), *available at* http://www.uscourts.gov/rules/Revised_Rules_and_Forms/BK_Form_B6F.pdf. For further information, see *infra* Appendix. We exclude any unsecured priority debts, such as past alimony or past taxes, from these calculations. Such debts were relatively infrequent.

128 The amount of unsecured debt ranged from $0 to one debtor who owed $2,445,149. The mean amount of unsecured debt, which was severely skewed due to the $2

point has been made before,[129] it bears repeating in this context: The typical family who files Chapter 7 bankruptcy is facing unsecured debts that dwarf its income.

To measure meaningfully the implications of such debts for families, we used debtors' bankruptcy schedules to calculate a debt-to-income ratio for each household in the sample. This ratio represents the total amount of unsecured debt for each debtor divided by that debtor's annual income at the time of bankruptcy. At the median, the debt-to-income ratio was 1.35:1. Thus, for every $100 that a family earned, it owed $135 to creditors.[130] In concrete terms, this statistic means that the families in our sample would have to devote approximately sixteen months of their entire income, without incurring any expenses or any new debts, to pay off their unsecured debts. Importantly, there were no statistically significant differences between the worse-off, unchanged, and better-off families with respect to their unsecured debt-to-income ratios.[131] The amount of unsecured debt that these groups discharged in bankruptcy was also statistically indistinguishable.[132] These findings strongly suggest that the failure to thrive after bankruptcy hinges on postbankruptcy factors. Neither the amount of debt that drives a family to file bankruptcy nor the amount of prebankruptcy income explains how families will fare following bankruptcy. The postbankruptcy financial troubles that families report are not about absolute dollars but instead stem from incongruities between income and expenses.

We then examined how these postbankruptcy expenses intersected with recovery. As we discussed above in Part I.C, our findings indicate that most worse-off families are struggling to pay bills for basic expenses such as utilities, insurance, and medical care. These data suggest that the "ongoing problem of debt" reported by the worse-off

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million outlier, was $50,819. Unsecured debt at the 25th, 50th, and 75th percentiles was $16,200, $27,573, and $48,225, respectively.

129 *See* Elizabeth Warren, *The Bankruptcy Crisis*, 73 Ind. L.J. 1079, 1080 (1998) ("[C]onsumer bankruptcies are rising because consumers' debts are rising faster than their incomes."); Todd J. Zywicki, *An Economic Analysis of the Consumer Bankruptcy Crisis*, 99 Nw. U. L. Rev. 1463, 1476 (2005) ("[I]t is observed that there is a high correlation between consumer bankruptcies on one hand and consumer debt-to-income ratios on the other.").

130 The mean debt-to-income ratio was 1,034:1. This extreme statistic is the result of eight debtors who had no income but owed unsecured debts ranging from $6,700 to $219,010. When we remove these outliers from the analysis, the mean debt-to-income ratio is 2.4:1.

131 Among the three groups, there is no statistically significant difference in the median unsecured debt-to-income ratios. Those who were worse off had a ratio of 1.36:1; the ratio was 1.35:1 for debtors whose postbankruptcy financial status was unchanged; those whose situations had improved had a ratio of 1.34:1.

132 Total unsecured debt levels for each of the three groups of families, based on how they were faring postbankruptcy, are not statistically different from each other. Worse-off families had median unsecured debt of $27,852. The median unchanged family owed $28,060, and the median better-off family owed $27,299.

families usually stems from routine monthly bills. The debts that plague families postbankruptcy are not the result of the extension of credit; they are new obligations for current goods and services.

This observation breaks significantly from the existing literature on postbankruptcy debts. Scholars have repeatedly expressed consternation about reaffirming a debt, which requires promising to repay a debt that could be discharged in bankruptcy.[133] These scholars point out that reaffirmation could blight a debtor's fresh start.[134] Although bankruptcy law explicitly permits and regulates reaffirmations of debts,[135] these renewed obligations limit the effectiveness of the bankruptcy discharge in eliminating the consequences of a family's past financial decisions. Given the low median income in our sample, we were also dubious about the ability of households both to service old debt postbankruptcy and to meet future expenses. Therefore, we hypothesized that a decision to reaffirm a debt would negatively affect a family's postbankruptcy financial situation.

To explore this relationship, we analyzed the extent to which families who reaffirmed a debt were overrepresented among the worse-off or unchanged families. We did not find any statistically significant correlation between reaffirmation and postbankruptcy financial situation. Approximately the same percentages of families in each of our three groups had participated in reaffirmation agreements.[136] In fact, we observed an unexpected trend: Those in the worse-off group were least likely to have reaffirmed a debt. We strongly caution against drawing anything other than a tentative conclusion from these data, however, because only a small number of debtors (sixty-four households) in the sample reaffirmed any debt.[137] The sample size

133 *See, e.g.*, Marianne B. Culhane & Michaela M. White, *Debt After Discharge: An Empirical Study of Reaffirmation*, 73 AM. BANKR. L.J. 709, 710 (1999) ("Debtors can abuse the reaffirmation process. If they enter into improvident and burdensome affirmations, they doom themselves and their families to prolonged financial distress.").

134 *See, e.g.*, Braucher, *supra* note 50, at 1087 ("Reaffirming unsecured debts is almost always a bad idea, yet many debtors do and a get a 'stale start,' in that they emerge from bankruptcy personally obligated for debts that they could have discharged." (footnote omitted)); Culhane & White, *supra* note 133, at 764 (cautioning that their empirical review of reaffirmations "raises serious questions as to whether the debtor's fresh start is adequately protected" by allowing reaffirmations).

135 *See* 11 U.S.C. § 524(c)–(d) (2000).

136 Fourteen percent of worse-off families reaffirmed at least one debt. Twenty percent of the unchanged families reaffirmed at least one debt. Eighteen percent of better-off families reaffirmed at least one debt.

137 These sixty-four households represent 18% of the debtors in our sample of Chapter 7 cases. This number is somewhat smaller than the best existing estimate of the national average. *See* SULLIVAN, WARREN & WESTBROOK, *supra* note 58, at 319 (determining that approximately 20% of Chapter 7 debtors in ten judicial districts in three states reaffirmed a debt); Culhane & White, *supra* note 133, at 720 (finding that 28% of 1,043 Chapter 7 cases from seven judicial districts in seven states contained at least one reaffirmation agreement).

hinders any conclusion that reaffirming debts does not affect postbankruptcy outcomes.[138] Although we collected data on the type of debt that was reaffirmed,[139] the sample size hindered meaningful analysis. Future studies on debt reaffirmation should consider tracking debtors longitudinally to assess more rigorously if and how reaffirmations influence families' postbankruptcy financial situations.

Our findings show that a change in postbankruptcy income is the primary reason some families recover and others do not. Families whose postbankruptcy income increases frequently experience an authentic fresh start. In contrast, the fresh start is likely to elude families whose incomes decrease, even after discharging debts. In some ways, this conclusion is not remarkable. Bankruptcy law does not attempt to prevent future income interruptions or to cushion families from a decline in income. Regardless, this finding is a powerful reminder of the limitations of bankruptcy relief. Successful postbankruptcy rehabilitation appears to rest on sustained or increased income, yet bankruptcy law does not address this critically important need. Without income support or stability, bankruptcy provides only partial aid for those seeking financial rehabilitation.

B. Income Trigger: Job Problems

Prior research has established that job problems are the leading "cause" of bankruptcy.[140] Elizabeth Warren, Jay Lawrence Westbrook, and Teresa A. Sullivan simply state: "The jobs data are overwhelming: by every measure, the debtors in bankruptcy are there as a result of trouble at work."[141] Our research buttresses this finding. Job problems are a key factor in understanding postbankruptcy health. Among our sample of worse-off families, job problems were the leading reason identified for their worsened financial situations.[142] Specifically, nearly eight in ten (79%) of worse-off households reported that their continued financial difficulties could be explained by job problems.

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138 While sixty-four debtors reaffirmed debts, only four (14%) were in the "worse-off" category; nineteen (20%) were in the "unchanged" category; forty-one (18%) reported being better off. Despite these small numbers, the overall trend seems clear.

139 A vast majority of these households (83%) chose to reaffirm only one debt. Eleven households reaffirmed a mortgage. Forty-one households reaffirmed a car loan. Twelve households reaffirmed a different type of debt.

140 *See* SULLIVAN, WARREN & WESTBROOK, *supra* note 22, at 105; WARREN & TYAGI, *supra* note 72, at 80–81.

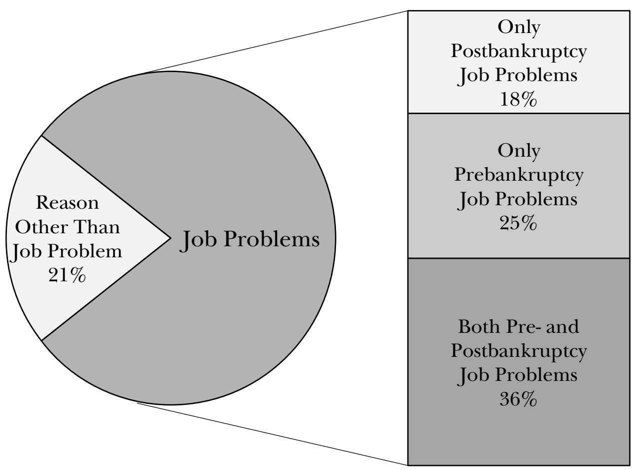
141 SULLIVAN, WARREN & WESTBROOK, *supra* note 22, at 105.

142 We asked respondents whether "job problems" were the reason for their worsened financial situations. We did not define what a job problem was but instead left it to the respondent to make that determination.

Inarguably, job problems are income problems. Earned wages from jobs are the leading source of income for American families.[143] The income declines that cause families to suffer postbankruptcy financial hardship most likely result from job problems. Job problems produce unsteady and inadequate income, which hinders financial recovery. In this way, the jobs data are a subset of our finding about the primacy of income in determining financial recovery after bankruptcy. Of the worse-off debtors who reported decreased income, 80% had experienced job problems. Jobs appear to be a crucial link to stable and increasing income.

To develop a more nuanced picture of how job problems affect postbankruptcy financial health, we asked families whether their worsened financial situations resulted from prebankruptcy or postbankruptcy job problems. Figure 7 illustrates the breakdown of responses to this inquiry. It is important to note that prebankruptcy job problems did not end at the time of bankruptcy. This term encompasses job problems that began before bankruptcy and persisted after bankruptcy. Postbankruptcy job problems are new situations that arose after the family filed bankruptcy.

FIGURE 7: FAMILIES REPORTING JOB PROBLEMS AS CAUSE OF WORSENED FINANCIAL SITUATION



Prebankruptcy job problems plagued 61% of worse-off families. Twenty-five percent of these families reported that job problems that began before their bankruptcies contributed to their worsened financial situations. Another 36% experienced *both* prebankruptcy job problems and additional job problems that began after they filed bankruptcy. These findings demonstrate that many families do not

143 *See* SULLIVAN, WARREN & WESTBROOK, *supra* note 22, at 105–06.

quickly recover from a job loss or a significant decline in income. Recovering from a job problem may take many years or may elude a family altogether. One year after a bankruptcy discharge, these families were still seeking meaningful solutions to the job problems that arose before bankruptcy.

Data from the questionnaires that debtors completed at the time of their bankruptcies corroborate the prevalence of prebankruptcy job problems that debtors reported in the telephone interviews. One in four of the respondents from the worse-off families indicated on the questionnaire that either the respondent or the respondent's spouse was unemployed and seeking work at the time of the bankruptcy filing. For these families, the problem may be that one year postbankruptcy, they still had not found employment. In 2001, the median duration of unemployment was 6.8 weeks, and the average duration of unemployment was 13.2 weeks.[144] Although these figures are much less than one year, they represent the entire U.S. population. Bankrupt debtors may have more trouble obtaining a job.

Prebankruptcy job problems also resulted in "job skids" that continued after bankruptcy.[145] The experience of Linda, a 46-year-old woman from southern California, is illustrative.[146] Linda was laid off three times in the year before she went bankrupt.[147] She was employed at the time of her bankruptcy, but inconsistent employment and underemployment had plagued her since her bankruptcy:

> Companies are going belly-up. People don't realize the major impact that it causes. I started out making $75,000 per year, now I'm down to $40,000. My salary goes down and down, [i]f I can even keep a job, while everything else goes up and up. There isn't any way to keep up with it anymore. The cost of living is too high at the time when wages are going down and companies are going under.[148]

Linda was able to return to full-time work before filing bankruptcy, but the wages in her new position were inadequate to keep pace with climbing expenses.[149] For example, between 2000 and 2001, the year of Linda's bankruptcy, real estate prices climbed 7% in the Los Angeles metropolitan area.[150] Medical expenses rose nearly 8% in the year

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144 *See* BUREAU OF LABOR STATISTICS, U.S. DEP'T OF LABOR, *Unemployment Spells Lengthened in 2002*, MONTHLY LAB. REV., Jan. 27, 2003, http://www.bls.gov/opub/ted/2003/jan/wk4/art01.htm.

145 *See* SULLIVAN, WARREN & WESTBROOK, *supra* note 22, at 88–96.

146 *See* Porter & Thorne, *supra* note 91, at 1–2 (survey respondent CA-07-071).

147 *See id.* at 3.

148 *Id.*

149 *See id.*

150 *See* JOINT CTR. FOR HOUS. STUDIES OF HARV. UNIV., THE STATE OF THE NATION'S HOUSING: 2002, at 2 fig.1 (2002), *available at* http://www.jchs.harvard.edu/publications/markets/Son2002.pdf (showing inflation-adjusted home prices from 1992 to 2001).

after Linda's bankruptcy.[151] These increases may seem modest, but for a person like Linda, who has a declining income because of chronic job problems, escalating living expenses leave her vulnerable to continued financial hardship. Linda's recovery from her prebankruptcy job problem of repeated layoffs was incomplete; she remains vulnerable to new financial problems after her bankruptcy because of declining income.

The debt relief that bankruptcy brings helps families avoid collection calls, repossession of their property, and perhaps eviction or foreclosure during the period of their unemployment. However, bankruptcy does not provide a cure for job problems. The mounting debts from a loss of income that initially drove unemployed families to file bankruptcy may have been erased, but such debts are likely to accumulate again in the postbankruptcy period when obtaining a new job or compensating for a drop in income proves difficult or impossible.

Another subset of worse-off families described a different job-related reason for their diminished financial situations. Fifty-four percent of the worse-off families reported that *post*bankruptcy job problems explained their continued hardship.[152] Eighteen percent of all worse-off families experienced only postbankruptcy job problems. This subset of families had jobs before bankruptcy. Their financial problems may have resulted from increased expenses rather than a loss of income before bankruptcy. For these families, a discharge from debts in theory offered a comprehensive and effective solution to their financial distress. In reality, however, postbankruptcy life created new obstacles for them. Their inability to achieve financial health is the result of new job problems that occurred in the one-year period after they filed bankruptcy. Despite freedom from old debt via a bankruptcy discharge, these families find themselves without adequate income to avoid sliding back into financial trouble after bankruptcy.

Anne, a 37-year-old wife and mother of two young children from Texas, explained how her family's financial situation worsened.[153] Just a few months after their bankruptcy, Anne's husband, Peter, lost his job.[154] They struggled to survive on his unemployment check and

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151 *See* Press Release, Bureau of Labor Statistics, U.S. Dep't of Labor, Consumer Expenditures in 2002 (Nov. 21, 2003), *available at* http://www.bls.gov/news.release/archives/cesan_11212003.pdf.

152 The 54% represents the sum of those families that experienced only postbankruptcy job problems (18%) and those that experienced both pre- and postbankruptcy job problems (36%).

153 *See* Porter & Thorne, *supra* note 91, at 8–9 (survey respondent TX-07-121).

154 *See id.* at 9.

part-time job.[155] The family cut back on expenses to try to make ends meet on their reduced income.[156] They canceled COBRA health insurance[157] for their children because they could not afford the premiums.[158] Unfortunately, until Peter finds a new job with an income similar to that of his previous work, the family must continue to make hard choices about spending priorities, which include going without health insurance, or else turn to accumulating new debt to make up the gap in income.

The plight of Anne, Peter, and their children illustrates an obvious but important point: Job loss remains a risk after bankruptcy. Families trying to climb out of a financial hole may find that a crucial job—the ladder to financial success—suddenly disappears during the months following bankruptcy. Families lack perfect information on their employer's stability, the cycles of the national economy, and their future wage potential. As a result, they may file bankruptcy and receive a discharge of prebankruptcy debts, only to face a job loss. Even with most of their old debt eliminated, these families no longer have adequate income to make ends meet.

Of the families who were worse off due to job problems, more than 36% reported that *both* old and new job problems contributed to their postbankruptcy financial difficulties. These families either had a wage earner lose a job or had experienced a decrease in family income before they filed. They then experienced additional job problems in the year after their bankruptcies.

Pam, a 26-year-old single Caucasian woman from Texas, tells a typical story.[159] Before she decided to file bankruptcy, Pam experienced "periods of unemployment" that left her "extremely behind" on her bills, particularly her credit card payments.[160] Chapter 7 bankruptcy and its immediate discharge of unsecured debt seemed to be the perfect antidote to Pam's financial woes. However, after her bankruptcy, which erased most of her past bills, she experienced further job problems.[161] She explains: "After I filed I was unemployed again; I was laid off, but they brought me back again. My finances have worsened since I filed bankruptcy, because even though I'm back at my job, I had to take a pay cut. It's harder now."[162] Pam thought that her

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155 *See id.*

156 *See id.*

157 COBRA refers to the Consolidated Omnibus Budget Reconciliation Act of 1985 that Congress passed in 1986 giving certain former employees, retirees, spouses, and dependent children the right to temporary continuation of health coverage at group rates. *See* Pub. L. No. 99-272, 100 Stat. 82 (1986).

158 *See* Porter & Thorne, *supra* note 91, at 9.

159 *See id.* at 6 (survey respondent TX-07-042).

160 *See id.*

161 *See id.*

162 *Id.*

job problems were resolved. She followed the advice of leading experts to wait to file bankruptcy until the crisis that caused her financial problems—unemployment—had passed.[163]

Pam's experience with a second, postbankruptcy round of job problems demonstrates the difficulty of achieving financial security. A cyclical free-market economy hinders people from predicting their job security and accurately anticipating future income. Relief from debt accrued during a previous job problem does not insulate families from being hit again, after bankruptcy, with a layoff, permanent job loss, or reduced income. Indeed, bankruptcy may exacerbate job problems. A young debtor from California, fresh out of college, described how bankruptcy added to her struggles: "[My] [a]ttorney said that things would get better. Doesn't seem to get better. Applying for jobs with government . . . and they told me [the bankruptcy] would stay on my [credit] record forever."[164]

The data on job problems reveal why many bankrupt families face the ongoing problem of having too much debt and too little income.[165] Even after the discharge frees a family from the responsibilities of debt, a declining income may leave it struggling to meet current bills. Existing job problems do not magically abate after bankruptcy, and nothing about a discharge of debt inoculates families from future job problems. Job problems lead to diminished income while expenses hold steady or climb. Income is crucial to postbankruptcy health, and a job that pays an adequate income is the key to unlocking the gate to stable income.[166]

C. Income Trigger: Medical Problems

Medical problems are the second most common factor in bankruptcy.[167] A recent study concluded that medical problems might explain as many as half of all bankruptcies.[168] Medical problems contribute to financial distress in two ways. First, like job problems, medical problems are often directly linked to a loss of income. Seriously ill or injured people may not be able to work, or otherwise healthy individuals may have to leave their jobs to care for an ill child,

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163 *See* WARREN & TYAGI, *supra* note 72, at 169–70.

164 *See* Porter & Thorne, *supra* note 91, at 1 (survey respondent CA-07-065).

165 *See supra* Part III.A.

166 *See* Deborah Thorne, Personal Bankruptcy, the Credit Report, and Social Mobility 5 (Mar. 7, 2006) (unpublished manuscript, on file with authors). To exacerbate the issue further, debtors may find that having a bankruptcy on their credit report severely hampers their chances of finding employment. In some instances, employed debtors reported that they were fired when their employers learned of the bankruptcies. Although the Bankruptcy Code expressly prohibits this action, *see* 11 U.S.C. § 525(b) (2000), it seems to occur nonetheless.

167 *See* WARREN & TYAGI, *supra* note 72, at 81 fig.41.

168 *See* Himmelstein et al., *supra* note 117, at W5-70.

parent, or other family member. Second, medical problems create unexpected expenses. Even with insurance, many families face substantial co-payments, deductibles, or expenses for prescription drugs. The effect of medical problems on families' finances can be conceptualized as a vise: Income is lowered, while simultaneously expenses climb. The resulting squeeze forces families to the financial breaking point of filing bankruptcy.[169]

Just as they contribute to families' needs for bankruptcy relief, medical problems significantly correlate with families' postbankruptcy financial well-being. Medical problems were second only to job and income problems as reasons for a family's worse-off financial situation. Slightly under half (46%) of worse-off families reported that an illness or injury was a significant factor in their ongoing financial struggles.

Chronic medical problems—those that began before bankruptcy and continued a year later—caused families the most financial distress. Among worse-off families who reported a medical problem, 43% said that medical problems that began before bankruptcy persisted more than one year later and continued to hinder their financial recovery. Julie and Lyle, a couple from California in their early 50s, described how chronic health troubles hindered their fresh start.[170] Before bankruptcy, an auto accident left Lyle disabled and unable to work.[171] The resulting medical problems sent the couple into a financial tailspin. Despite their best efforts to "head [bankruptcy] off" by selling many of their possessions, eating "a lot of soup, a lot of soup," and living "as economically as possible," they could not avoid bankruptcy.[172] At the time of our interview, more than one year after their bankruptcy, Lyle's application for workers' compensation still had not been approved, and he continued to wait for Social Security disability payments.[173] Julie expressed frustration that, despite filing bankruptcy, she and Lyle remained in financial trouble:

> We've always rented, we just never seem to be able to put enough away to put down on a house of our own; though I wish we could. Now we, probably, never will own anything . . . . Now, in this country, two people have to work. That's how the system is set up. I don't know how we are ever going to have a pot to pee in the way things are. It seems unfair, for so many reasons . . . . It's too bad; it really is. Not just for us, for lots of people, especially the young people.[174]

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169 *See* WARREN & TYAGI, *supra* note 72, at 80–81.

170 *See* Porter & Thorne, *supra* note 91, at 2–3 (survey respondent CA-07-163).

171 *See id.* at 2.

172 *Id.*

173 *See id.*

174 *Id.* at 3.

Julie's disenchantment with the American dream of homeownership and independence through financial stability is a vivid reminder of the sometimes-illusory nature of bankruptcy's fresh start. Julie and Lyle may have desperately needed relief from the stress and pressure of overdue hospital bills or threats to turn off their utilities, but this financial fresh start did not heal Lyle's injury. Nor did bankruptcy aid them in their struggle with America's fragmented and inadequate medical compensation systems. A full recovery for Lyle and Julie requires more than a discharge of debt. Like many families, this couple needs comprehensive health care and disability insurance. A more functional social safety net, or to a smaller degree, personal savings, would help families with chronic medical problems supplement income or meet increased expenses, features lacking in our current bankruptcy system.

A few worse-off families (14%) experienced a medical double-whammy. Before bankruptcy, a medical problem contributed to their financial distress. Then, after their bankruptcies, these same families were struck with a new illness or injury. Xavier, a 42-year-old painter from Texas, is a case in point.[175] He broke his back when he fell off a ladder at work.[176] Burdened with over $35,000 in medical bills that he could not pay, he filed bankruptcy.[177] Less than a year later, Xavier was injured again; he fell and broke his pelvis, triggering another round of medical bills and lost work income.[178] At the time of his postbankruptcy interview, he described how his medical problems left him feeling defeated:

> My earning power is one-quarter of what it used to be. I can't lift anything. When you cry and [creditors] still call you, I just can't take it anymore. But for a man, I think it's different. Because a man's supposed to take [c]are of the family and I felt very, very embarrassed.[179]

Xavier is not only in worse financial shape after bankruptcy, he is also in worse physical and psychological shape. Indeed, his frustration and humiliation at finding himself back in financial trouble illustrate the mental anguish that worse-off families commonly expressed. Already exhausted by his previous bout of hardship, Xavier's second injury thrust him into a second round of financial trouble. His new medical bills and his inability to work as a painter after his postbankruptcy injury are setting him up for a financial crisis similar to the one that precipitated his first bankruptcy. Unfortunately, Xavier can-

175 *See* Porter & Thorne, *supra* note 91, at 6–7 (survey respondent TX-07-049).
176 *See id.* at 6.
177 *See id.*
178 *See id.*
179 *Id.*

not turn to the bankruptcy system for relief anytime soon. Due to a recent amendment to the Bankruptcy Code, the period of time that must pass before a person is eligible for a subsequent discharge of debts after a prior bankruptcy has increased from six years to eight years.[180]

Income loss and medical problems are often tightly braided. Our data suggest that the link between income decline and illness or injury is just as strong a factor in families' postbankruptcy recovery as it is a contributor to financial despair before bankruptcy.[181] For many families, the initial medical bills are only the harbinger of worse financial troubles to come. Consider the situation of Jean, a woman from Texas who worked as an executive secretary for a mortgage lender and whose husband owned a successful business.[182] Before bankruptcy, their joint income allowed them to manage the monthly obligations on a startling $87,000 of unsecured debt.[183] Then Jean was diagnosed with multiple sclerosis. During this same period, her husband's business "slowed to a crawl."[184] Overwhelmed and unable to make their minimum monthly payments, the couple filed bankruptcy and discharged their unsecured debt.[185] Despite eliminating thousands of dollars in monthly debt service, Jean insists that her family's financial situation had worsened.[186] She describes a tightening spiral of medical and income problems. Bankruptcy did not cure her multiple sclerosis or boost her husband's business, and the couple's income continued to dwindle while Jean's medical bills increased as her prognosis worsened.[187] The family has substantial, and nonnegotiable, medical expenses arising from Jean's illness: Her injections are $1,400 each month, and each prescription pill that she takes for her headaches costs her more than $19.[188] Based on these costs alone, we estimate that Jean is accumulating at least $20,000 in medical bills each year and trying to meet them on her husband's diminishing income. Jean's story is tragic. She has an expensive and terminal illness, she cannot work, and her husband's business continues to flounder. Bankruptcy was a very short-lived reprieve for this family; it addressed what arguably was a past mistake: Carrying too much unsecured debt even when the family's financial prospects looked bright

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180 *See* 11 U.S.C. § 727(a)(8) (2000).

181 *Cf.* SULLIVAN, WARREN & WESTBROOK, *supra* note 22, at 146 (stating that for many families, "the high *cost* of medical care translates directly into the high *debt* to meet those costs").

182 *See* Porter & Thorne, *supra* note 91, at 7–8 (survey respondent TX-07-110).

183 *See id.* at 8.

184 *Id.*

185 *See id.*

186 *See id.*

187 *See id.*

188 *See id.*

and its income was high. However, bankruptcy did not cure Jean's illness. Her physical health and her financial health are locked in tandem. Far from a fresh start, the future for Jean looks increasingly bleak.

Critics may argue that these families could have avoided bankruptcy if only they had health insurance. Research suggests, however, that the vast majority of families who file medical bankruptcies do indeed have health insurance at the time of their illnesses or injuries.[189] Unfortunately, for many of the families we studied, their insurance was tied to their employment. The result is that when they became too ill to work, they also became too ill to have insurance. This is a tenuous and intractable situation. When illness or injury prevents employment, employer-provided health insurance is worthless. For those who purchased private health insurance, a job loss likely meant they were no longer able to afford the cost of the premiums.

As prior research has established, employer-based and private insurance policies cannot adequately protect families from medical bankruptcies. Our findings demonstrate that these same forms of insurance are inadequate following bankruptcy because of health problems that prevent many former debtors from working. The probability of financial rebound is diminished particularly when injury and chronic illness are part of the equation. These individuals typically experience a decline in income because they are unable to work,[190] and simultaneously experience a rapid increase in expenses and debt from medical bills and prescription costs. Even when a strong economy provides jobs for healthy unemployed or underemployed bankrupt individuals, sick or injured individuals find themselves too unwell to take advantage of these employment opportunities. For those suffering from chronic medical conditions, bankruptcy may well prove to be only a short-term solution to a long-term problem. Improving the outlook for these families requires a two-pronged approach. A national health care system or guaranteed access to affordable private health insurance that is not tied to employment would help prevent these families from drowning in new medical debt. More comprehensive government unemployment benefits or private unemployment insurance would help insulate ill families from the income shocks caused by inability to work because of illness or injury. With a median annual income of only $21,870 at the

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189 *See* Himmelstein et al., *supra* note 117, at W5-69 (reporting that 76% of all debtors who filed medical bankruptcies were covered by health insurance at the onset of the illness or injury).

190 *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, 407–08 (2001) (describing how this "income effect" can create a financial hardship that health insurance was never designed to cover).

time of their bankruptcies,[191] these families cannot afford the private health or unemployment insurance that is currently available to some Americans. The result is that people with chronic medical conditions continue to suffer both ill personal health and ill financial health after bankruptcy.

D. Income Trigger: Age

Three decades of research on who files bankruptcy has identified several persistent trends. Elizabeth Warren recently renewed her claim that "the families that file for bankruptcy are an overwhelmingly middle-class group, a cross-section of America that concentrates its numbers in the middle."[192] Although these findings have proven durable, no previous study has investigated how some of the most common demographic factors affect families' postbankruptcy outcomes.

Before we analyzed the data, we hypothesized that demographic variables such as age, level of education, marital status, number of dependent children, and race would correlate with a debtor's recovery. These hypotheses were largely unsupported. We found no significant relationship between a family's postbankruptcy financial status and the primary debtor's educational level, marital status, race, or financial responsibility for a dependent child.[193] There was, however, a sole exception: Age is negatively correlated with an improved postbankruptcy financial situation. Older debtors are more likely to experience continuing financial difficulty. Although the data are inconclusive, we suggest that age appears to influence postbankruptcy outcomes for the same reason as job and medical problems do: Older debtors are more likely to have declining, or at least stagnant, incomes.

A prior analysis of Consumer Bankruptcy Project data revealed a significant increase in the rate at which older debtors are seeking bankruptcy protection.[194] A study of the general, but not necessarily bankrupt, elderly population similarly concluded that many older Americans are experiencing grave financial struggles and that hardship among seniors has increased in recent years.[195] Many elderly families are refinancing their homes, thereby entering retirement sad-

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191 *See supra* Part I.C.

192 Warren, *supra* note 96, at 118–19.

193 *See infra* notes 210–213 (reporting our findings on the noncorrelative variables).

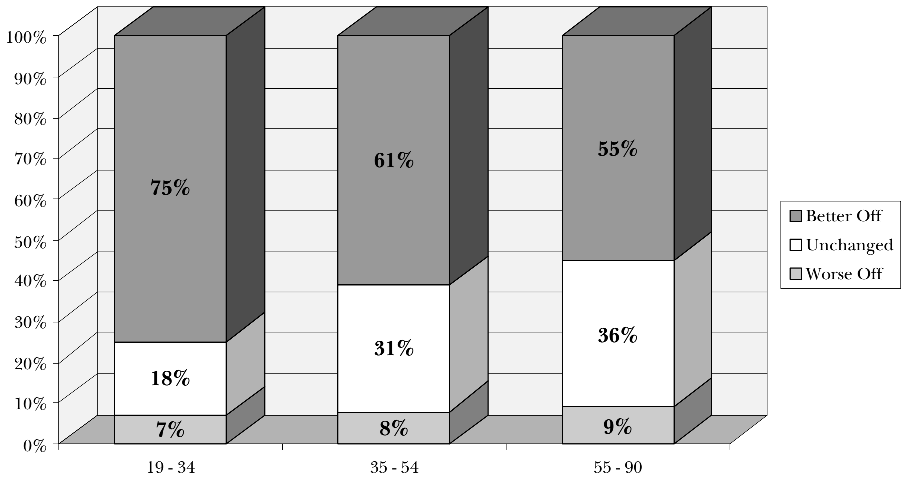
194 *See* Teresa Sullivan, Deborah Thorne & Elizabeth Warren, *Young, Old, and In Between: Who Files for Bankruptcy?*, NORTON BANKR. L. ADVISER, Sept. 2001, at 2. For a discussion of the Consumer Bankruptcy Project, see *infra* Appendix.

195 *See* HEATHER C. MCGHEE & TAMARA DRAUT, DEMOS, RETIRING IN THE RED: THE GROWTH OF DEBT AMONG OLDER AMERICANS (2d ed. 2004), *available at* http://www.demos.org/pubs/Retiring_2ed.pdf.

dled with mortgage payments.[196] Credit card use among older Americans also has exploded in the last several years.[197] These findings suggest that age does not immunize one from financial stress. In fact, it seems that older Americans may face unique challenges to sustaining financial health. Based on this research, we hypothesized that older Americans would be disproportionately likely to struggle after bankruptcy.

To test this hypothesis, we correlated age and postbankruptcy financial status, using the age of the first or primary petitioner as reported on the debtor questionnaire.[198] We constructed the following age categories: 19 to 34 years old, 35 to 54 years old, and 55 to 80 years old. We found a statistically significant relationship between age and postbankruptcy financial status.[199] As illustrated in Figure 8, age and recovery after bankruptcy are related.

FIGURE 8: POSTBANKRUPTCY FINANCIAL SITUATION BY AGE



First, note that all age groups are about equally likely to report being in worse financial shape. That is, between 7% and 9% of fami-

[196] *See id.* at 7. McGhee and Draut describe how "more and more seniors are now borrowing against their homes." *Id.* As a result, the percentage of senior homeowners who owed money on their homes increased from 19% in 1980 to over 28% in 2000. *Id.*

[197] *See id.* at 3. Between 1992 and 2001, the amount of credit card debt that debtors over 65 years old carried increased by 89% to an average of $4,041. *Id.* Moreover, the credit card debt that debtors aged 65 to 69 owed grew the fastest: 217%, to an average of $5,844. *Id.*

[198] If only one adult filed the bankruptcy case, that person was the primary petitioner. If a married couple filed a joint bankruptcy case, the questionnaire asked for the age of each adult. For these analyses, we rely on the age of the person whom the couple designated as the "primary or first petitioner."

[199] We also analyzed the data using six age cohorts: under 25, 25 to 34, 35 to 44, 45 to 54, 55 to 64, and 65 and over. The trend was consistent with the three-age cohort data reported in detail.

lies in each of the age groups reported that their financial situations were worse one year after bankruptcy. Statistically, age does not correlate with worsened financial condition. However, families headed by younger debtors are significantly more likely than families headed by older debtors to achieve a better financial recovery following bankruptcy. Three in four debtors in the youngest age group reported that their financial situations had improved. In contrast, only 55% of households in the oldest group of debtors, those aged fifty-five to eighty years old, indicated that their financial situations were better.

Debtors in the oldest age group were the most likely to report that their financial situations remained unchanged. More than one in three debtors aged fifty-five to eighty reported that his or her financial condition remained about the same. The youngest debtors were half as likely as older debtors to be in the same postbankruptcy financial situation. Although there may be some comfort in knowing that older families do not face an increased risk of being worse off, we caution that the measure of postbankruptcy financial health was a comparative one. Even the unchanged families are in approximately as much financial trouble as when they declared themselves broke and sought debt relief.

These findings on the relationship between age and postbankruptcy financial situation dovetail with our conclusion about the importance of income growth and good health in achieving an improved economic situation after bankruptcy. Young people are likely to have more economic mobility and job opportunity, and they are less likely to suffer from chronic or terminal illnesses or recurring injuries. These data suggest that younger families are best at capturing the rehabilitative power of bankruptcy's fresh start.

On the other hand, the plight of older debtors is grim.[200] Older households represent a disproportionately large portion of debtors whose financial problems continue or worsen. If a bankruptcy discharge—the law's strongest remedy for financial distress—does not adequately restore older families' financial stability, we question what alternate relief will be available to them as they continue to struggle.

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200 *See, e.g.*, Ed Flynn, Gordon Bermant & Karen Bakewell, *Bankruptcy by the Numbers: A Closer Look at Elderly Chapter 7 Debtors*, 21 AM. BANKR. INST. J. 22 (2002); Robyn L. Meadows, Comment, *Bankruptcy Reform and the Elderly: The Effect of Means-Testing on Older Debtors*, 36 IDAHO L. REV. 227, 229–30 (2000) ("Over 10% of Americans over the age of sixty-five lived below the poverty line in 1995. Thus, while older Americans are collectively a financially stable and prosperous group, that financial soundness does not extend to all older Americans. Some of the less financially stable will be forced to seek bankruptcy protection, and as the size of this population segment grows, so will the number of their bankruptcies."); *see generally* Daniel L. Skoler, *The Elderly and Bankruptcy Relief: Problems, Protections, and Realities*, 6 BANKR. DEV. J. 121, 145 (1989) (referring to bankruptcy for the elderly as a "vortex of impoverishment that can engulf decent, self-sufficient and largely blameless persons in the final phases of the life cycle").

Because of notable increases in the number of older Americans who experience hardship,[201] it is increasingly important that policymakers consider the limits of bankruptcy's power to help older or retired Americans in financial distress.

Although sample size limits the scope of analysis, we consider several explanations for older debtors' overrepresentation among the financially vulnerable after bankruptcy. First, it is exceedingly unlikely that older debtors can increase their earnings, and, as we have demonstrated, improved income is most closely associated with improved postbankruptcy financial status.[202] The job market is not kind to older Americans. Even though older debtors may have more years of job experience, they generally take longer than younger debtors do to find employment.[203] These additional months of unemployment or underemployment cause stagnant or declining incomes. Age discrimination may also lead older Americans to accept lower-paying jobs.[204] Older families, particularly retired ones, are also more likely to live on fixed incomes and must therefore rely entirely or in part on Social Security or pensions. These stable yet fixed sources of income may prove inadequate to keep up with increases in the cost of living. If a family could not make ends meet before bankruptcy, they are likely to face similar problems after bankruptcy and wind up back in debt.

The second reason for older debtors' postbankruptcy financial fragility is that older Americans are much more likely to be plagued by medical problems and therefore are hampered by issues relating to chronic illness and high prescription drug costs.[205] The situation of Max, a 70-year-old military veteran, shows how multiple income-reducing factors can pile up on an older American.[206] Max, who has diabetes and HIV, explained that he lost all of his investments in the stock market in the late 1990s.[207] Consequently, his only steady source of income was now Social Security.[208] As Max explained:

> My financial situation is worse because I have no cushion to fall back on. My four children are going to contribute and send money each month but that's a spit in the ocean. But I'd rather be work-

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201 *See* McGhee & Draut, *supra* note 195.

202 *See supra* Part III.A.

203 *See* Kim Clark, *A Fondness for Gray Hair*, U.S. News & World Rep., Mar. 8, 2004, at 56 (noting that it takes an unemployed 60-year-old on average eight weeks longer to find a new job than it does a 30-year-old).

204 *See id.* at 56–57 ("Studies show that workers in their mid-60s earn at least 10 percent less than those in their mid-50s with similar qualifications and work hours.").

205 *See* U.S. Dep't of Health & Human Servs., Health, United States, 2005 with Chartbook on Trends in the Health of Americans 382 tbl.124, *available at* http://www.cdc.gov/nchs/data/hus/hus05.pdf.

206 *See* Porter & Thorne, *supra* note 91, at 3–4 (survey respondent CA-07-187).

207 *See id.* at 3.

208 *See id.* at 4.

> ing. This is really a crucial period because my Social Security check only fundamentally covers my rent.[209]

Because these income, job, and medical problems become more prevalent and potent as a person ages, we anticipate that further research will reveal that older families are particularly likely to remain in financial distress well beyond the one-year postbankruptcy period that we examined, whereas some of the worse-off and unchanged younger families may eventually rebound. For the oldest cohort of debtors, financial recovery is particularly elusive. Their economic trajectory may ultimately be one of continued decline. The relationship between age and income change needs to be closely examined to generate solutions for helping older Americans reestablish their financial health.

The significance of our determination that age and postbankruptcy recovery are correlated is highlighted by the fact that age was the only demographic variable that appears to be relevant to how families fare. Our data did not identify education level,[210] marital sta-

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[209] *See id.*

[210] The strongly predictive relationship between educational attainment and income is well documented. *See, e.g.*, JENNIFER CHEESEMAN DAY & ERIC C. NEWBURGER, U.S. CENSUS BUREAU, THE Big Payoff: Educational Attainment and Synthetic Estimates of Work-Life Earnings 2 (2002), *available at* http://www.census.gov/prod/2002pubs/p23-210.pdf (reporting that, of adults who were employed at any time from 1997 to 1999, those with higher educational levels earned notably higher salaries than their less educated counterparts). Therefore, we posited that debtors with more education would be more likely to achieve improved postbankruptcy financial situations. Better educated people could also be better equipped to evaluate the consequences and benefits of bankruptcy and file only if bankruptcy is likely to produce a meaningful and lasting financial improvement. The questionnaire that we distributed to the debtors at the time of their bankruptcies asked them to indicate their highest level of education. For our analysis, we used the educational level of the first petitioner and collapsed responses into three categories: (1) less than a high school diploma, (2) high school diploma or some college, and (3) college degree or graduate education. The data failed to show that level of education significantly affected a debtor's postbankruptcy financial status. Debtors are approximately equally likely to sustain an improved financial situation one year postbankruptcy regardless of educational achievement.

tus,[211] race,[212] or financial responsibility for a dependent child[213] as

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211 Scholars have documented that divorced people are overrepresented among bankruptcy filers. *See* SULLIVAN, WARREN & WESTBROOK, *supra* note 22, at 183–84 (finding that in their study, "[a]bout 23 percent of the bankruptcy sample was divorced, compared with about 10 percent of the general population in 1991"). This finding may suggest that single individuals, particularly single women, are at greater risk for financial ruin than the general population. *See* Elizabeth Warren, *What Is a Women's Issue? Bankruptcy, Commercial Law, and Other Gender-Neutral Topics*, 25 HARV. WOMEN'S L.J. 19, 25 (2002) ("[T]he real problem is that women, particularly divorced and separated women with children, are facing a rapidly growing risk of economic collapse."). We posited that this trend may continue postbankruptcy, with divorced people more likely to be represented among the worse-off families. The data refute this hypothesis. We did not find a statistically significant relationship between marital status and debtors' postbankruptcy financial situations. In fact, when compared to their married counterparts, single debtors are slightly more likely to report that they are better off one year after filing—67% compared to 62%. Although divorce may heighten one's risk of financial failure, it does not seem to impair the chances that one experiences improved postbankruptcy financial health. This conclusion was substantiated by the stories that women told us during interviews conducted one year after their bankruptcies. Many women described how following their divorces they were saddled with monthly obligations from old debts that were unmanageable without their husbands' incomes. Alternatively, they described being unable to meet the share of debts that they were allotted in the divorce decrees. Still other women reported that their ex-husbands filed bankruptcies, causing their joint creditors to turn on them for collection. Our data suggest that bankruptcy effectively helps divorced women deal with these problems. By erasing their past debts, these women exit bankruptcy on an equal footing with other former debtors. They are equally likely to be part of the two-thirds of families that find themselves better off after bankruptcy.

212 Scholarship on the intersection of race and bankruptcy is nascent and inconclusive. *See* A. Mechele Dickerson, *Race Matters in Bankruptcy*, 61 WASH. & LEE L. REV. 1725, 1775 (2004); *see also* SULLIVAN, WARREN & WESTBROOK, *supra* note 22, at 42 (discussing the presence of both overrepresentation and underrepresentation hypotheses about minority group members in bankruptcy). We were unsure whether and how postbankruptcy financial status would correlate with the race of debtors. Using the race of the first petitioner as self-reported on the debtor questionnaires, we categorized respondents in a binary fashion as either Caucasian or minority. Debtors who reported their race as Black, Asian, Hispanic, or "other" were grouped together as minorities, as were those debtors who indicated that they were both Caucasian *and* minority, or were members of multiple minority groups. Our relatively small sample size required us to construct the minority-nonminority category. If our sample size had been larger, we would have rejected the binary category and explored possible differences between the numerous racial and ethnic groups. Using these criteria, 40% of first petitioners in our sample identified themselves as minority; 60% self-identified as Caucasian. We did not find a statistically meaningful correlation between race and families' postbankruptcy financial status. Caucasians and minorities were essentially equally likely to have worse, unchanged, or better postbankruptcy financial situations.

213 Previous research has demonstrated that dependent children increase the likelihood that families will file bankruptcy. *See* Elizabeth Warren, *Bankrupt Children*, 86 MINN. L. REV. 1003, 1019 (2002) ("Once again, households and individuals with no children face the least risk of financial collapse, while families with children are at more than double the risk."). Other research has determined that "a woman decreases her chances of going bankrupt by 66 percent" if she does not reproduce. *See* WARREN & TYAGI, *supra* note 72, at 173 (stressing that if families, and women in particular, avoid having children, they will face a dramatically reduced risk of bankruptcy). Being childless may seem like a drastic measure to prevent financial collapse, but the data do demonstrate the costs and uncertainties that accompany having children. In light of these findings, we expected to find that families with children would be less likely to recover financially and more likely to continue to struggle with their bills after bankruptcy. Interestingly, this was not the case.

significant in determining postbankruptcy financial experiences. Although these data are the first of their kind,[214] and we believe further study would be beneficial, we tentatively conclude that most prebankruptcy demographic characteristics do not determine postbankruptcy financial recovery.

The data on demographic qualities suggest that bankruptcy works equally well—or poorly—for people of different levels of educational achievement, races, and marital statuses. This finding is consistent with our main conclusion that income change is the determinative factor of how a family fares after bankruptcy. Although better educated families do earn higher prebankruptcy incomes,[215] it is the direction of income change—not the amount of income, as we have previously established[216]—that is crucial to a family's ability to maintain its financial health in the year after bankruptcy. The same explanation applies to race. White families may earn higher incomes,[217] but race itself appears not to be predictive of declining income over time. Focusing on income change also explains why marital status and the presence of dependent children do not correlate with how people fare after bankruptcy. Unlike job or medical problems, divorce or a family breakup normally has a definite end. It is not a chronic condition and is not necessarily linked to a continuing income problem. Similarly, the presence of dependent children in a household may make a family more financially vulnerable to failure,[218] but children do not cause a downward employment spiral of reduced earnings or underemployment in the way that age does. Age was the only demographic quality that we identified as related to a family's financial recovery. The correlation between prebankruptcy

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In fact, when households with at least one minor dependent were compared with those without any minors, those with minors were not significantly more likely to report being in worse financial shape or to report problems paying their debts. We stress, however, that the relationship between financial problems and children should be examined for a period of more than just one year.

214 Stanley and Girth could not consider these questions. *See* STANLEY & GIRTH, *supra* note 16, at 6–8, 219–29. They did not gather demographic information beyond what is available on the bankruptcy petition and therefore lacked information regarding race, education, and marital status. *See id.* Additionally, because they could not reach most of their initial sample for interviews two years postbankruptcy, they had to draw an essentially new sample of interview respondents. *See id.* at 224–25.

215 According to our data, the median annual income of families wherein the primary petitioner reported earning less than a high school diploma was $15,510. For households in which the primary petitioner had a high school diploma or some college, the median income was $21,174. In the most-educated families, those families with primary petitioners who had a college degree or graduate education, the median income was $26,682.

216 *See supra* Part III.A (analyzing income data).

217 *See* U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE U.S., 443 tbl.666 (2004); U.S. Census Bureau, Income – Frequently Asked Questions, http://www.census.gov/hhes/www/income/faq.html (last modified Dec. 20, 2005).

218 *See* WARREN & TYAGI, *supra* note 72, at 173–79.

demographic characteristics and postbankruptcy financial condition did not yield simple findings that can easily predict who will thrive after Chapter 7 bankruptcy. Practitioners, scholars, and policymakers probably cannot accomplish the task of improving the efficacy of the fresh start merely by changing bankruptcy policy to aid particular demographic groups.

The data revealed a much more complex picture about how families experience life after bankruptcy. Income is the single critical factor. A bankruptcy filing that is followed by continued income decline or interruption will likely result in a family facing financial distress again after discharge. Stable or increasing income is the key to a family's ability to meet ongoing expenses and weather new financial pressures after bankruptcy.[219] Because job problems, medical problems, and age often hinder income growth or result in a declining income, these factors correlate with an increased likelihood of financial hardship in the year following bankruptcy.[220] The implications of our findings, which we discuss in the next section of the Article, reflect both the primacy of income to financial recovery and the complexity of how income intersects with postbankruptcy experiences.

IV
Policy Implications

Jean Braucher recently called for studies to explore the "long-term financial picture for debtors after they file in bankruptcy."[221]

> We know little about the financial situations of debtors after bankruptcy. Who does well and who does not? What are the key factors in the success stories? Are increased income and good health insurance most crucial to staying out of debt and beginning to save? Or is it learning to budget? . . . . We also do not know who gets into trouble again after a bankruptcy and why (other than that many debtors reaffirm debts in Chapter 7, impairing their fresh starts, or fail to complete plans in Chapter 13). The gaping holes in our knowledge make it hard to evaluate how successful bankruptcy is in providing a fresh start.[222]

This Article makes a vital step toward filling these empirical voids. The data that we report herein provide a key way to measure post-bankruptcy financial success by providing information regarding debts and expenses following bankruptcy and comparing financial situations before and after bankruptcy. Other measures of postbankruptcy financial well-being are possible and could yield similarly rich

219 *See supra* Part III.A fig.6.
220 *See supra* Parts III.B–D.
221 Braucher, *supra* note 50, at 1068.
222 *Id.* at 1090–91.

results.[223] Armed with the best available data to date, we provide a first glimpse into the previously unstudied realities of life after discharge.

For many families, the postbankruptcy prognosis is good. Approximately two-thirds of families who file Chapter 7 report that they are better off one year after bankruptcy. These families experienced the proverbial fresh start, evidencing that the Chapter 7 system has potentially positive transformative power. To the extent that these families achieve lasting financial success, the bankruptcy system deserves praise for its ability to restore families to economic security. Nevertheless, the critical and unanswered question that remains is whether these changes continue beyond the first year.

Equally notable, however, is the fact that nearly one in three families remains gripped by financial distress a year after they filed bankruptcy. These debtors' personal stories of their experiences provide humanizing insights into the types of problems that hinder the discharge's promise of a fresh start. One year after they were willing to declare themselves bankrupt, these families reported that their financial situations are the same as or worse than when they sought legal relief and a fresh start under Chapter 7. For these families, bankruptcy may have provided immediate short-term relief, but it does not appear to translate into sustainable financial improvement. Bankruptcy and its concomitant discharge of most debts merely temporarily mask underlying problems that exceed the current bankruptcy system's ability to resolve. The major factor behind these families' continuing financial struggles is stagnant or declining income in the period following their bankruptcies. As we demonstrate, any factor that leads to reduced postbankruptcy income will severely handicap a family's prospects for a meaningful fresh start. Many of these families have chronic, crippling job and health issues. Hampered by the continuation of problems that led to their initial overindebtedness or struck with new crises, these families are unable to use bankruptcy successfully as a launching point for future economic security. Positive wage growth and consistent good health appear to be vital for financial rehabilitation. Because these factors correlate negatively with age, older families are also less likely to enjoy improved financial health after bankruptcy.[224]

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[223] For example, a follow-up study could ask families who filed bankruptcy to complete forms similar to bankruptcy schedules that provide a detailed picture of debt, assets, income, and expenses. Another possibility is to query debtors at the time of filing as to how they would rate their financial health in the month before their bankruptcies on a numerical scale—say, one to ten—and then to repeat this procedure in later interviews.

[224] *See supra* Part III.D.

Bankruptcy offers a discharge of most unsecured debt and a way to restructure or reduce most other remaining debts. This provides powerful relief, and for most victims of one-time hardship, the bankruptcy system appears to work well. However, the bankruptcy process fails to provide a family with a certain and stable income stream, an economically viable employer, or a guarantee of good health. Without these benefits, bankruptcy remains a limited remedy for the financial disasters that drive more than a million families to seek bankruptcy relief each year.[225]

Our findings on the postbankruptcy financial experiences of debtors call for a reevaluation of the consumer bankruptcy system. New amendments to the Bankruptcy Code limit who may file Chapter 7 bankruptcy through application of a complex means test.[226] This legislation can be interpreted as reflecting an assumption in Congress that Chapter 7 bankruptcy is too generous, and that families are too eager to reap the "easy" benefits of bankruptcy instead of struggling to pay their debts.[227] This conception of bankruptcy relief is difficult to reconcile with our key finding that one year after bankruptcy, more than one in three families finds itself in the same or worse financial condition as when it sought Chapter 7 relief.

Our data suggest that Congress should redirect its attention. Reducing the number of bankruptcy filings is an admirable goal, but bankruptcy filings tend to serve as merely a proxy for the number of Americans in financial distress. Restricting access to Chapter 7 relief will do nothing to solve the underlying problems that continue to plague families after they file bankruptcy. Instead, such a restriction will strip debtors of even a temporary reprieve from hardship. Our findings indicate that the dynamics of job loss, declining incomes, illness or chronic health problems, and reduced life prospects for the elderly underlie both the financial crises that precipitate bankruptcy and the continuing hardships that many families face after a bankruptcy discharge.[228] Concern for the economic situations of low-income Americans must take us beyond the bankruptcy system. Resolving the underlying causes of reduced and unstable income—for example, wage declines and illness or injury—will not be simple.

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225 *See* News Release, Admin. Office of the U.S. Courts, Bankruptcy Filings Fell in March 2005 12-Month Period (June 10, 2005), *available at* http://www.uscourts.gov/Press_Releases/news61005.html (reporting the total number of filings in 2004 as 1,654,847 and in 2005 as 1,590,975).

226 *See* 11 U.S.C.A. § 707(b)(2) (West 2005); *see also* Tabb, *supra* note 32, at 34–35 (explaining how the reform bill will create entry barriers to the consumer bankruptcy system).

227 *See* Tabb, *supra* note 32, at 13 (positing that reform advocates assume "that *debtors* are causing the [bankruptcy] crisis—that debtors are abusing the law by taking out too much credit, living the high life, and sliding down the easy path of discharge when they could repay a significant portion of their debts").

228 *See supra* Part III.

Economists and social scientists concerned with job instability and wage growth have documented the extent of this problem.[229] As Jean Braucher posited, "[i]f more income is the key [to who does well after bankruptcy], job training would be a more effective strategy than financial management education."[230] Broadening unemployment benefits to cover those who suffer even a modest reduction in hours or wages, not just those who lose their jobs, may also mitigate the consequences of decreased income on a family's financial prospects. Our research suggests that job problems do not have a dichotomous relationship with financial health. Rather than a binary employed-versus-unemployed split, the interaction between job problems and financial crisis is multilayered. More focus is needed on ensuring stable and adequate income despite temporary layoffs, unpaid leaves of absence for family or medical reasons, or changes in employers, and the concomitant loss or reduction in benefits. The postbankruptcy data show that for many families, one job problem often leads to another, creating a downward income spiral that a bankruptcy discharge alone cannot reverse.[231]

Other scholars have tackled more directly the relationship between medical problems and financial distress.[232] These scholars' focus on the reasons for bankruptcy caused them to identify the need for comprehensive medical insurance to help prevent families from becoming saddled with large medical bills.[233] Ensuring postbankruptcy financial health requires providing forms of income support to those debtors facing chronic medical conditions. Social programs of this sort cannot prevent all injuries or heal all illnesses, but they can help to both prevent medical bankruptcies and ensure postbankruptcy recovery for the chronically ill. Income-replacement and disability insurance could help families meet their ongoing expenses during periods of wage loss due to illness or injury. However, unless these forms of income support are affordable and widely available, they will do little to help families who file bankruptcy because these

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229 *See, e.g.*, BARBARA EHRENREICH, NICKEL AND DIMED: ON (NOT) GETTING BY IN AMERICA (2001); NEWMAN, *supra* note 72; Emil E. Malizia & Shanzi Ke, *The Influence of Economic Diversity on Unemployment and Stability*, 33 J. REGIONAL SCI. 221 (1993).

230 Braucher, *supra* note 50, at 1090. As part of the 2005 amendments to the Bankruptcy Code, Congress mandated that debtors attend a financial education course as a prerequisite to receiving a discharge of their debts. *See* 11 U.S.C.A. § 727(a)(11) (West 2005).

231 *See, e.g.*, Porter & Thorne, *supra* note 91, at 1 (survey respondent CA-07-055).

232 *See, e.g.*, Himmelstein et al., *supra* note 117 (analyzing the relationship between illness or injury and bankruptcy and noting in particular the impact of the lack of health insurance on bankruptcy); Jacoby, Sullivan & Warren, *supra* note 190.

233 *See* Himmelstein et al., *supra* note 117, at W5-72 (asserting the need for universal health coverage but stressing that unless this coverage is considerably more comprehensive than many current health policies, it may still prove inadequate to prevent the risk of massive medical debt striking a family).

families' meager incomes leave few or no dollars available for such expenses. Our data on the substantial number of families struggling to pay insurance premiums after bankruptcy serve as a reminder of how escalating insurance costs contribute to the financial vulnerability of American families.[234]

Our findings also demonstrate the importance of establishing savings accounts after bankruptcy, although this may be terribly difficult and possibly even unrealistic. We recognize that these families are trying to live on incomes that, at best, can be characterized as extremely modest,[235] and that meeting basic expenses is already challenging.[236] Nevertheless, the data are clear. Job problems and medical problems are likely to resurface in the postbankruptcy period, which will cause the incomes of a substantial fraction of families to decline. Saving money in the aftermath of bankruptcy could, to some degree, help insulate families from future financial shocks. Bankruptcy law could offer incentives for such savings. For example, a family could be eligible for a future bankruptcy discharge sooner than the statutory eight-year period[237] if it can demonstrate that it made substantial efforts to save money but faced a crisis that overwhelmed those savings. Without the assistance of social programs or a different structure to bankruptcy relief, these families must, in the postbankruptcy period, choose between suffering even more severe privations in order to cut expenses and save, or continuing to risk another financial collapse.

We are skeptical about the role of financial education in helping families avoid future financial trouble.[238] Although financial education is now a prerequisite for a bankruptcy discharge,[239] the stories that the debtors in our sample shared indicate that the heartaches and headaches of going bankrupt have taught them more powerfully than any financial management course ever could. Financial education should occur before families get into trouble, and it should be available to all Americans, possibly as a central component of a high

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234 *See supra* Part I.C.

235 *See supra* Part III.A (providing the median incomes of debtors).

236 *See supra* Part II.C (reporting the special difficulty of debtors in paying bills).

237 *See* 11 U.S.C.A. § 727(a)(8) (West 2005) (denying discharge to a debtor who has been granted discharge within eight years before the current bankruptcy case).

238 *Cf.* Susan Block-Lieb, Corinne Baron-Donovan, Karen Gross & Richard Wiener, *The Coalition for Consumer Bankruptcy Debtor Education: A Report on Its Pilot Program*, 21 EMORY BANKR. DEV. J. 233, 235, 257 (2004) (suggesting that there are too few studies on the effects of financial education for debtors but concluding, based on their own limited studies, that "with careful planning and thought, such programs are not only possible, but also affordable and valuable"); Susan Block-Lieb, Karen Gross & Richard L. Wiener, *Lessons from the Trenches: Debtor Education in Theory and Practice*, 7 FORDHAM J. CORP. & FIN. L. 503, 518–19 (2002) (expressing concern for "the possibility of the development of predatory educational practices").

239 *See* 11 U.S.C.A. § 727(a)(11) (West 2005).

school curriculum. Given the volatility of the modern economy and the weakening social safety net, individuals need to be more proactive than ever to insulate themselves from financial collapse. Our research demonstrates the critical importance of building a postbankruptcy savings cushion to ensure ready access to money to pay expenses during times of renewed financial stress. A steady income will elude many Americans, and the current bankruptcy scheme does not provide any mechanism to assist in obtaining income stability or growth—the key building block to financial recovery.

The isolation of income as the primary factor in determining how a family fares after bankruptcy has important practical implications for bankruptcy attorneys and law professors. Effective counseling of clients about whether to file bankruptcy should include a discussion of whether they anticipate future declines in income. We speculate that some of the worse-off and unchanged families could have benefited from postponing filing bankruptcy. The amended bankruptcy law now bars these families from seeking relief again for eight years,[240] and yet a substantial fraction of families continue to struggle to pay debts and experience renewed or continuing financial hardship. To the extent that the bankruptcy discharge is a "get out of jail free" card for most debt, families should be cautious in playing this card before the circumstances surrounding their distress have stabilized.[241] As a general matter, we believe that unemployed debtors should try not to file bankruptcy until they have found new employment, that sick people should try to recover their health before they file bankruptcy, and that all debtors, particularly those nearing retirement age, should be work to ensure that their incomes will increase or that they can reduce monthly expenses to meet their current incomes before filing bankruptcy.

Interviews with hundreds of families show that this advice is easier to dispense than to implement. Creditors are persistent, worry compounds existing health problems, and optimism springs eternal. Bankruptcy relief is far from foolproof, but it does offer certain immediate benefits, such as the protection of the automatic stay and a halt to the accumulating mountain of interest on debt.

The odds on an effective fresh start after Chapter 7 are slim—one in three—and the short- and long-term costs of bankruptcy are substantial. Our findings should remind attorneys who counsel families in financial crisis and those who write the bankruptcy laws of an im-

240 *See* 11 U.S.C.A. § 727(a)(8) (West 2005).
241 *See* WARREN & TYAGI, *supra* note 72, at 163–80.

portant fact—bankruptcy relief is not free.[242] Bankruptcy imposes both direct and indirect costs.[243] With a median annual income of less than $22,000, the direct expenses of filing a Chapter 7 case are quite burdensome. The Chapter 7 filing fee is approximately $220,[244] while median attorneys' fees for Chapter 7 bankruptcy exceed $700.[245]

Having a bankruptcy on their credit reports may very well cause these families to become victims of additional unexpected hardships.[246] For instance, many families will be required to pay much higher interest rates for future mortgages, car loans, or credit cards.[247] Some families will be turned down for apartment rentals and be required to pay in advance rent deposits that are three or four times higher than the local average.[248] Some debtors will be denied employment because a bankruptcy is on their credit reports.[249] Others will be fired from existing jobs,[250] despite the fact that doing so is unlawful.[251] Vulnerable and lacking legal recourse, these families are cause for serious concern. Indeed, further longitudinal study could determine whether they end up refiling bankruptcy or explore how these households cope with their financial problems during the period when they are ineligible for bankruptcy.

Despite the charge that it provides a "painless way" to maintain extravagant lifestyles,[252] bankruptcy is an expensive solution. The immediate and future costs of bankruptcy ensure that families pay dearly for their decision to seek legal relief from their debts. Thus, before

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242 1 STEWART MACAULAY ET AL., CONTRACTS: LAW IN ACTION 264 (1995). We borrow this phrase from Stewart Macaulay, who frequently studied how the expense of legal action deters pursuit of legal remedies.

243 *See* Melissa B. Jacoby, *Ripple or Revolution? The Indeterminacy of Statutory Bankruptcy Reform*, 79 AM. BANKR. L.J. 169, 186 (2005) (noting that bankruptcy filers bear a wide array of immediate and long-term costs).

244 *See* 28 U.S.C.A. § 1930(a)(1) (West 2005) (requiring a $220 filing fee for a Chapter 7 filing). The filing fee under the version of the Bankruptcy Code in effect in 2001 was $155. *See* 28 U.S.C. § 1930(a)(1) (2000).

245 The mean cost of an attorney for those in our sample was $738. Attorneys for fifteen families provided their services *pro bono*. The maximum amount paid for an attorney for Chapter 7 was $2,700. At the 25th, 50th, and 75th percentiles, families paid their attorneys $450, $700, and $1,000 respectively.

246 *See, e.g.*, Thorne, *supra* note 166, at 1.

247 *See id.* at 1.

248 *See id.* at 8.

249 The Bankruptcy Code makes it illegal for private employers to "discriminate with respect to employment against" an individual "solely" because he or she has filed bankruptcy. 11 U.S.C. § 525(b) (2000); *see* MERRICK T. ROSSEIN, EMP. L. DESKBOOK HUM. RESOURCES PROF. § 2:21 (2005) ("If an employer obtains an applicant's credit report that reflects a bankruptcy filing, the employer will need to have an independent basis for any adverse employment decision."), *available at* EMPDESK § 2:21 (Westlaw).

250 *See id.* at 5.

251 *See* 11 U.S.C. §525(b) (2000).

252 Jones & Zywicki, *supra* note 100, at 218.

families spend approximately one-twentieth of their income to file bankruptcy and risk future housing, transportation, and employment opportunities, they should consider other alternatives, including negotiating with creditors, using the Fair Debt Collections Practices Act to stop abusive collection agents,[253] or working with a reputable debt counseling service.[254] Although these solutions are piecemeal and have their own transaction costs, the data on families' postbankruptcy financial health suggest that greater caution is necessary when counseling them to file Chapter 7 bankruptcy.

In reaching the above conclusions, we emphasize that even for the worse-off families, bankruptcy was likely beneficial in many critical ways. The automatic stay halted collection efforts.[255] The stress, fear, and shame that accompany threats of repossession and constant dunning calls temporarily receded when these families came under the protection of the bankruptcy court. The discharge of debts gave these families a critical reprieve from watching their debt spiral higher through late fees, over-limit charges, and penalty rates. These families may accumulate new bills in the years after their bankruptcies, but without any bankruptcy discharge, they surely would be buried under an insurmountable mountain of debt. Month after month, these families suffer depression and humiliation because they know that repayment is impossible. To appreciate the futility of the average family's financial situation, consider the following: Our average debtor had $27,573 in unsecured debt. If she made a minimum monthly payment of 3%, it would take her more than twenty-eight years and cost her an additional $27,351 in interest to repay that debt.[256] This assumes, of course, that she never accumulates any additional debt that must be serviced.

We cannot overlook, and unfortunately cannot easily estimate, the peace of mind that families find when they seek bankruptcy relief.

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253 *See* 15 U.S.C. §§ 1692–1693 (2000).

254 Credit counseling services are one of the various options recommended to help consumers in financial trouble. *See* FED. TRADE COMM'N, KNEE DEEP IN DEBT, FTC FACTS FOR CONSUMERS (Dec. 2005) (offering detailed information to consumers in financial trouble), *available at* http://www.ftc.gov/bcp/conline/pubs/credit/kneedeep.pdf. Many of these credit counseling services are under investigation for deceptive practices. *See* News Release, Internal Revenue Service, IRS, FTC and State Regulators Urge Care When Seeking Help from Credit Counseling Organizations (Oct. 14, 2003), *available at* http://www.irs.gov/newsroom/article/0,,id=114574,00.html.

255 *See* 11 U.S.C. § 362 (2000).

256 Minimum monthly payments vary depending on debtors' credit scores. For example, those with excellent credit ratings are generally required to pay 2% of the balance; those with lower scores must pay 3%. For the program used to make this calculation, see Bankrate.com Home Page, http://www.bankrate.com. The calculation assumed an 18% interest rate, which is conservative, especially for people who are likely in default on one or all of their debts and are being charged rates of 29%. At this higher rate, it would take the debtor more than fifty years and over $110,750 in interest to pay off the $27,553 debt.

From reading interviews with hundreds of families, we know that bankruptcy offers them a way to take control of their financial problems. In this way, families who seek bankruptcy relief are acknowledging the realities of their debts and may view the decision to file bankruptcy as a responsible financial step rather than a financial mishap. In filing bankruptcy, however, these families are playing the odds that their incomes, employment opportunities, and health will improve, and that they will be one of the families for whom Chapter 7 brings lasting financial benefits.

Conclusion

During the recent bankruptcy law reforms, Congress and scholars alike used the fresh start as a rhetorical weapon to argue opposing sides—that access to Chapter 7 bankruptcy should be maintained and that it should be restricted. Our findings reveal that, contrary to popular belief, the fresh start may be more myth than magic bullet. Instead of being a panacea for consumer financial distress, Chapter 7 bankruptcy relief is insufficient to ensure lasting financial well-being for one in three households. After bankruptcy, these families experience income declines often related to job or medical problems that limit their abilities to turn bankruptcy's fresh start into sustainable financial health. Determining how to reduce the number of families in financial distress requires developing an appreciation of the primacy of income as a factor in financial well-being. Stable and sufficient income not only helps insulate families from the underlying problems that lead to bankruptcy, it is also critical to preventing these debtors from experiencing a subsequent economic collapse. Armed with insight about the postbankruptcy realities facing former debtors, we can consider how to design a bankruptcy system and alternative structures to foster financial stability, allowing families to capture and sustain the benefits of bankruptcy's fresh start.

APPENDIX

Methods and Additional Data

The data for this Article were gathered over a two-year period, from 2001 to 2003, during Phase III of the Consumer Bankruptcy Project.[257] The Project, which has existed for over two decades, is a collaborative effort of over a dozen academics at seven research institutions.[258] Phase III collected data using three types of instruments: debtor questionnaires, public court records, and telephone interviews.

In the first half of 2001, questionnaires were distributed to every debtor at the mandatory meeting with the panel bankruptcy trustee called section 341 meetings.[259] The five judicial districts in the study were the Eastern District of Pennsylvania (Philadelphia), the Northern District of Illinois (Chicago), the Middle District of Tennessee (Nashville), the Northern District of Texas (Dallas), and the Central District of California (Los Angeles).[260] A letter accompanying the questionnaire informed debtors that their participation in the study was voluntary and would not affect their bankruptcy cases. The institutional review boards of Harvard University and the University of Texas approved the study's research protocols with regard to human subjects protections. All researchers who had access to respondents' names or identifying data signed confidentiality agreements.

The Consumer Bankruptcy Project research sample included only debtors who filed Chapter 7 or 13 bankruptcy. Married couples filing jointly completed a single questionnaire. The questionnaires were available in both English and Spanish. In each of the five districts, we collected questionnaires from 250 debtors, which created a total core sample of 1,250 bankruptcy cases. Each district's sample reflected the proportion of Chapter 7 and Chapter 13 cases that occurred in that district.[261] Thus, the core sample consisted of 780 Chapter 7 cases and 470 Chapter 13 cases.[262]

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257 Phase III builds on previous empirical studies of consumer bankruptcy conducted by Dr. Teresa Sullivan, Professor Jay Lawrence Westbrook, and Professor Elizabeth Warren. *See* Sullivan, Warren & Westbrook, *supra* note 22; Sullivan, Warren & Westbrook, *supra* note 58.

258 *See* Warren & Tyagi, *supra* note 72, at 181–88 (listing contributors and their institutions and providing a detailed methodology for the Consumer Bankruptcy Project.).

259 11 U.S.C. § 341 (2000) (meetings of creditors and equity holders).

260 A single city dominated the bankruptcy filings in each of the five judicial districts.

261 If, for example, 80% of nonbusiness petitions in a district in the preceding year were Chapter 7 filings and 20% were Chapter 13 filings, we mirrored that proportion in our sample. Thus, of 250 petitions in that district, we would have collected 200 Chapter 7 petitions and 50 Chapter 13 petitions.

262 We also collected supplementary questionnaires of debtors who met certain criteria, such as being a homeowner or living in a rural area, but we did not present any data from the supplemental questionnaires in this Article.

A copy of the questionnaire is publicly available.[263] The questionnaire solicited general demographic data, including age, sex, race, marital status, number of children, employment status, and highest level of education. The questionnaire also asked debtors about their reasons for filing bankruptcy and the strategies they used to manage their financial problems before bankruptcy. Most of the questions were close-ended and required debtors to check a box. The back of the questionnaire invited debtors to share the story of their bankruptcies in their own words. The final part of the questionnaire asked debtors if they would be willing to complete three telephone interviews in the three years following their bankruptcies, with fifty dollars compensation per interview.

The second data instrument used during Phase III was a copy of the court records corresponding to each questionnaire that was completed. Approximately 160 pieces of information from each debtor's court records were coded. The data were principally drawn from each debtor's schedules, which are filed under penalty of perjury and include information about assets, liabilities, income, and expenses.

The third data instrument was telephone interviews. From the core sample of 1,250 cases, 875 debtors volunteered to complete telephone interviews. Of these debtors, 630 were eventually contacted and interviewed. The telephone interviews began approximately a year after each debtor's filing and were completed by February 2002.[264] Although the questions were tightly structured, researchers were trained to follow up on interesting points and to take extensive verbatim notes. The average interview lasted approximately forty minutes and had four foci. One set of questions was asked only of debtors who owned their homes before or during their bankruptcies. Another group of questions was posed to debtors who indicated a medical reason for their bankruptcies. A third set was directed to small-business owners. All debtors were asked a final, general set of questions. All data presented here come from this set of questions, which had a sociological bent toward issues of reduced life chances, effects of bankruptcy on spousal or partner relationships, and the stigma associated with filing.

This Article uses only data provided by the 359 Chapter 7 debtors in the core sample who completed a telephone interview. We excluded Chapter 13 debtors because we wanted to study the final resolution of bankruptcy in debtors' lives, and debtors cannot normally obtain a discharge in a Chapter 13 case until three to five years after

263 *See* Warren, *supra* note 213, at 1028–32.

264 The interviews were conducted using a computer-assisted program designed in Microsoft Access.

filing bankruptcy. We included only the core sample in order to reduce sample bias to the maximum extent possible.

Trained individuals who followed written coding protocols coded the data from all three instruments into specially designed Microsoft Access databases. To ensure accuracy, we blindly recoded a random sample of 15% of the court records and 10% of the questionnaires. We then compared the results with the first coding and corrected any errors. The accuracy rate exceeded 99% as there was less than one error per data instrument and each instrument collected approximately 150 data points. For analysis, we imported the data into SPSS, a statistical software package. We performed each data run twice, once by each author, and we compared our results.

Because Phase III's data from postbankruptcy telephone interviews are the first of their kind, we were sensitive to any potential bias that could have resulted from using data only from debtors who self-selected when they agreed to a telephone interview. To determine the presence of any potential bias, we compared the samples of telephone interview participants and nonparticipants across several variables including income, total assets, total liabilities, total unsecured debt, employment status, homeownership, age, marital status, and race. The table below shows the results of these analyses. With the exception of marital status and race, no significant differences exist between participants and nonparticipants.

Appendix Table: Participant and Nonparticipant Demographics

	Participants	Nonparticipants
Mean annual income at time of filing	$24,300	$24,690
Mean total assets at time of filing	$52,268	$54,627
Mean total liabilities at time of filing	$84,458	$89,258
Mean total unsecured debt at time of filing	$44,130	$46,973
Employment status (percent employed)	75%	79%
Homeownership (percent who owned home)	32%	34%
Mean age (years)	42.7	40.9
Marital status (percent married)*	38%	46%
Race*		
Caucasian	60%	51%
Minority	40%	49%

* Differences between participants and nonparticipants were statistically significant ($p<0.05$).

Individuals who completed the telephone interview were significantly less likely to be married (38%) than individuals who did not complete the telephone interview (46%). Prior research has found that single individuals are less likely to file bankruptcy.[265] Because we have fewer married people in our subsample of telephone interview participants, the findings we present in this Article may understate the postbankruptcy financial difficulties that people experience.

Further, telephone interview participants were more likely to be Caucasian than minority, which also may have contributed to an underestimation of the prevalence and severity of postbankruptcy financial problems. Minorities are much more likely to be victims of predatory lending practices.[266] Recently, a scholar has suggested that the consumer bankruptcy system may be biased against minority debtors.[267] Based on these findings, it is possible that if the interview participant sample included a higher percentage of minorities, the number of those in financial distress could be greater. Because the subsample of interview participants contains a lower percentage of married people and minorities than does the core sample of the Consumer Bankruptcy Project, our findings may underestimate the extent to which postbankruptcy financial problems occur. These sampling issues are inherent in participatory research, and we believe that our data remain the best available at the present time and provide a base for further longitudinal studies.

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265 *See id.* at 1015 ("Unmarried men who have no children in their homes have the least risk [of bankruptcy], with a filing rate of 5.3 per thousand . . . . Unmarried women have slightly higher rates at 6.1 per thousand.").

266 *See* Elizabeth Warren, *The Economics of Race: When Making It to the Middle Is Not Enough*, 61 WASH. & LEE L. REV. 1777, 1794 (2004) (asserting a relationship between predatory lending and race).

267 *See* Dickerson, *supra* note 212, at 1743–71, 1775–76 (arguing that bankruptcy law is "raced" despite being facially neutral, because the conception of the "Ideal Debtor" most likely describes a Caucasian American).