



## **BANKRUPTCY: ENACT MEANINGFUL REFORM**

Over the past several years, Congress has worked to enact meaningful reform of our bankruptcy laws. Under current law, bankruptcy protection increasingly is becoming an easy option – a “first stop” rather than a “last resort” – for many borrowers who can afford to meet at least some portion of their financial responsibilities. Abuse of the bankruptcy code undermines the efficiency and effectiveness of our credit markets. Moreover, it raises the cost of credit to millions of responsible borrowers who pay their bills. The California Bankers Association (CBA) believes it is time to reform the system.

### **Background**

Consumer bankruptcies fall under two main categories: Chapter 7 and Chapter 13. Chapter 7 filers have almost their entire debt erased, even when they have the capacity to repay some of it. Under Chapter 13, creditors are repaid, in full or in part, in installments over a three- to five-year period.

The fundamental flaw in the current system is that there are no rules to determine whether Chapter 7 filers have the “means” to repay some of their debt. In fact, many debtors who can meet some of their financial obligations escape such debts by filing for Chapter 7. In a May 2003 speech, Treasury Assistant Secretary for Financial Institutions Wayne Abernathy termed these individuals as “predatory borrowers.” According to Assistant Secretary Abernathy, a predatory borrower is someone who “in a calculated way borrows as much as he can, with little thought of paying it back, or in some cases, with no intention of paying it back – the person who takes advantage of all of the statutes created to protect the truly unfortunate.”

We need legislation that establishes a “needs-based” formula that directs filers into one chapter or another based on their ability to repay. Such legislation would restore greater accountability to our bankruptcy system.

Figures from the Administrative Office of the U.S. Courts show the number of bankruptcy petitions filed in the federal courts rose 2.7 percent in the 12-month period ending March 31, 2004. Bankruptcy filings rose to 1,654,847 from 1,611,268 for the same 12-month period the previous year. While the state of the economy clearly impacts these numbers, it equally is clear that abuses under the current system fueled this growth.

The ever-increasing number of bankruptcy filings demonstrates the need for enactment of needs-based reform. It is important, however, to emphasize that those who cannot afford to pay a portion of their debt – whether due to layoffs or other misfortune – will not be affected by reform efforts.

### **Action**

The CBA strongly urges Congress to enact meaningful bankruptcy reform that will make important improvements in the bankruptcy code while maintaining protections for those truly in need.

House Judiciary Committee Chairman James Sensenbrenner, Jr. (R-WIS) introduced **H.R. 975**, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2003, which passed the House on March 19, 2003, by a vote of 315-113. The bill contains language from the conference report from the 107th Congress, but without the controversial abortion clinic language that prevented enactment of bankruptcy reform last Congress.

The CBA supports **H.R. 975**, which would create a needs-based system. The bill keeps the courthouse doors open for those who need bankruptcy protection and makes the process fair for everyone.

On January 28, 2004, the House incorporated **H.R. 975** into a Senate-passed extension of Chapter 12 farm bankruptcy legislation (S. 1920), and passed the amended legislation by a vote of 265-99. The House also requested a conference with the Senate.

If Congress does not complete action on bankruptcy reform this session, CBA urges Congress to make this a priority item in the next session. Every day Congress delays action is another day that the vast majority of financially responsible Americans bear the cost of those who “game” the system.

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