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Bankruptcy Abuse Prevention and Consumer Protection Act of 2005: How the Credit Card Industry's Perseverance Paid Off

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Enacted on October 17, 2005, *The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* (BAPCPA) marked the most significant change in United States' bankruptcy legislation since 1978. An important aspect of BAPCPA is that it makes fewer people eligible to file Chapter 7 bankruptcy. Until BAPCPA, Chapter 7 was the most popular form of personal bankruptcy because it eliminated non-secured debt — mostly, credit card debt. BAPCPA was passed at a time when the United States was experiencing significant annual increases in personal bankruptcy filings. While some researchers (e.g. Posner 1975; Michelle White 1991) have claimed that bankruptcy is a fault of moral character, there is another suspect: namely, the credit card companies that profit from increasing consumer indebtedness, but were losing $4 billion a year due to bankruptcy filings before BAPCPA (Waller 2001, 874). This paper presents research showing how the credit card industry developed, how credit card companies helped implement BAPCPA, and the new law's effects on the economy and individuals.

William Waller's article "Kick'em While They're Down: Anti-Consumer Bankruptcy Reform" (2001) is the best presentation to date of the institutionalist view of personal bankruptcy. But Waller's paper was published before BAPCPA was enacted. There are important implications associated with BAPCPA that Waller did not (could not) foretell. This analysis builds upon the work of Waller and other institutional economists (Adkisson and McFerrin 2005; Dolfsma and McMaster 2007; Redmond 2001; Veblen [1899] 1994; Watkins 2000) by presenting an institutionalist interpretation and analysis of BAPCPA. Specifically, this paper isolates the credit card industry as the main driving force behind BAPCPA.

This paper draws on research conducted in the year since BAPCPA's enactment that study its many effects. On October 16, 2006 the independent

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nonprofit bankruptcy research organization, American Bankruptcy Institute (ABI), organized a program entitled “A Year After BAPCPA” at Georgetown University Law School.[1] The program included practitioners, lawyers, judges, academics, and policy specialists from all sides of the BAPCPA debate. The program’s transcript (247 pages) provides detailed insight into BAPCPA’s influence on consumers, lawyers, and the economy in the first year of its existence.

The following sections present: (1) the nuances of bankruptcy types; (2) the highlights of BAPCPA; (3) some different perspectives on personal bankruptcy; (4) empirical findings that identify characteristics of bankruptcy filers; (5) policy prescriptions to help reduce the overall number of personal bankruptcies and minimize negative effects of BAPCPA; and (6) concluding remarks.

Nuances of Bankruptcy Types

The Bankruptcy Act of 1898 is the foundation of today’s modern bankruptcy laws. Before this act, bankruptcy laws were not permanent; they were enacted only during times of economic crisis. It was the Chandler Act of 1938 (a New Deal reform) that first made bankruptcy legislation more debtor-friendly (Adkisson and McFerrin 2005, 450). One important change made was to include the option to file Chapter 13 bankruptcy, which allowed people with considerable assets to file bankruptcy and pay off a portion of their debt over a number of years. Until this time, Chapter 7 bankruptcy was the only personal bankruptcy option available (Nader 2005; Skeel 2001).

The two most common types of personal bankruptcy are Chapter 7 and Chapter 13.[2] Chapter 7 bankruptcy allows a debtor to dissolve eligible debt obligations. Before BAPCPA’s enactment, Chapter 7 bankruptcy filings accounted for an average of 70 percent of all personal bankruptcies. Just after BAPCPA, the number of Chapter 7 filings fell below 30 percent (www.abiworld.org).[3] It is a common misperception that Chapter 7 bankruptcy discharges all personal debt. In fact, Chapter 7 bankruptcy only eliminates unsecured high interest debt, financial company loans, and some medical debts. It does not expunge mortgage loans (or any associated penalty fees, taxes, etc.), education loans, outstanding tax debts, child support, or alimony. So instituting a policy that reduces the number of Chapter 7 filings helps one industry most: the consumer credit lending industry (read: credit card companies) (Michelle White 2006; Manning 2000, 344; Nader 2005).

If a bankruptcy filer has significant assets, a judge will typically have him or her file Chapter 13 bankruptcy. Chapter 13 bankruptcy requires debtors to repay their debts over a three to five year period as specified by the court. Roughly two-thirds of people who file Chapter 13 bankruptcy never make it entirely through their debt repayment plan outlined by the court. These people typically exit the bankruptcy system, never getting their debts discharged (Michaela White 2006, 171; Manning 2000, 345; Sullivan 2006, 31). They must then establish new debt repayment schedules with their creditors, which gives debtors more flexibility with when payments are made and how much is paid each time. Court ordered repayment plans fail for many reasons: job loss, unexpected expenses, or the plan organized by the court was unrealistic. And, if someone who files under Chapter 13 misses even one payment at anytime for any reason — in the debt repayment schedule outlined by the court — their case is automatically dismissed. This is one reason politicians in the 1970s argued that "forced participation in a [Chapter 13 plan] has so little prospect for success that it should not be adopted as a feature of the bankruptcy system" (Skeel 2001, 154).

BAPCPA Highlighted

On March 11, 2005 the Senate passed BAPCPA (Senate Bill 256), a bill that drastically reformed United States' bankruptcy laws. Then on April 14, 2005, the House passed BAPCPA by a vote of 302 to 126. It was officially enacted on October 17, 2005 — six months after President Bush signed it.

Between 1999 and 2005, credit card companies contributed almost $25 million to politicians and political parties in an effort to reform personal bankruptcy legislation. MBNA (one of the country's largest issuers of credit cards) spent more than $17 million lobbying Congress from January 1999 to June 2004 for reform. BAPCPA has existed in a number of different forms since the late 1990s when credit card companies started pursuing legislative reform. Congress came close to passing an Act in 2001, but were thwarted by the 9/11 terrorist attacks.[4] Up to this point the top twenty-five credit card companies had spent at least $3.6 million on political contributions directly related to their support of personal bankruptcy reform, but they were not discouraged (Waller 2001, 874). They ramped up spending after 2001 and were eventually rewarded (www.opensecrets.com).

Credit card companies are estimated to recoup four billion dollars a year due to BAPCPA. This translates into a 7.5 percent increase in revenue each year. Credit card companies gain from BAPCPA because it allows them more time to collect fees and interest rates from debtors. It also gives them more opportunity to garnish the wages of debtors (House Report 2005; Leach 2005).

Charles Tabb's (2006b) research shows a strong correlation between bankruptcy filings and credit card debt (his conclusions are further supported by the empirical analysis conducted below). His research also shows that while consumer debt in general is correlated with personal bankruptcy, it is actually people's rising credit card debt that is significantly correlated with the increased number of bankruptcies. According to Michelle White (2006), credit card lenders have noticeably increased their offerings to risky borrowers and will continue to do so now that BAPCPA exists. She states:

> Late charges, over-limit charges, and penalty interest rates have been going up and up. . . . The credit card pricing pattern makes consumption more risky, which makes bankruptcy more valuable. . . . But, the adoption of BAPCPA has made it more difficult for debtors to file bankruptcy. That means that many debtors will delay

> filing, which means they are more likely to have their wages garnished, and they will pay the high credit card fees longer. So the social cost of debt is likely to rise. (Michelle White 2006, 26-7)

The BAPCPA changes the structure of the bankruptcy law in a number of ways — some are severe, others minor. According to bankruptcy attorneys Paul Hoffmann and Jerald Enslein (2006), "BAPCPA is more than 500 pages long, changes 83 sections of the Bankruptcy Code, and adds 17 new sections and one new chapter to the Bankruptcy Code. Many of the provisions raise more questions than they answer" (300). The following presents only the most relevant changes to bankruptcy legislation.

Credit Counseling

People who file for bankruptcy (regardless which Chapter) must now undergo credit counseling. Counseling is supposed to help consumers perform budget analyses. It also helps them better understand their options for paying back debts using various methods such as debt consolidation and prioritizing debts based on interest rates.

Some people are able to avoid filing for bankruptcy using counseling, but in most cases, people's financial situations are in such a state of disrepair that counseling is ineffective (Sullivan 2006). Since BAPCPA's inception, credit-counseling companies have found that the number of people filing bankruptcy has not fallen significantly due to debt management plans. Money Management International Inc. (MMI) — largest credit counseling company in the United States — found that by the time debtors get to their organization, their financial situation is too far gone for a debt management plan (www.moneymanagement.org). According to Sullivan (2006, 31), since BAPCPA, only 3.2 percent of people choose debt management plans over filing bankruptcy.[5] She also reports that "only about 10 percent of those who got certificates of credit counseling did not follow through with bankruptcy" (32).

The credit agency someone uses must be one already approved by the court, and courts usually pick credit agencies that are the largest in the industry, which are often heavily funded by credit card companies. These companies do not want people to file bankruptcy, so they use credit counseling agencies to encourage debt restructuring any way necessary so as to avoid bankruptcy (especially Chapter 7), even when it is clearly not in a consumer's best interest. Furthermore, credit counselors do not ask why these people are in financial trouble so they can help educate them about avoiding future problems. In general, the type of credit counseling outlined by BAPCPA is inadequate to solve most people's bankruptcy problems (House Report 2005).

Means Test

The means test is a method for evaluating one's eligibility to file Chapter 7 bankruptcy. This test is supposed to be an objective method of analyzing one's need to file Chapter 7 bankruptcy. If someone's income is below the median income of a similarly sized family in the state where they live (are registered), then they may be able to file Chapter 7. But if a debtor's income is above the state's median then the law becomes ambiguous. The court usually takes the debtor's income, subtracts living expenses, and multiplies the difference by 60. If this product is greater then $10,000 then the debtor cannot file Chapter 7. Even if someone passes the means test, the judge makes the final decision (Brown and Ahern 2005, 25). This is supposed to stop many opportunists from filing Chapter 7 bankruptcy when they should file Chapter 13. Michelle White (2006) states, "debtors can . . . pass the means test by spending more on categories that are exempt under the means test, for example, mortgage loans, car loans, and current charitable trust contributions" (24). She estimates that a knowledgeable opportunist whose income is in the 90th percentile can still pass the means test (24). An opportunist could also avoid the means test by opening a business, accumulating some business related debt, then filing bankruptcy because their debt is no longer primarily consumer debt and is therefore exempt (Michelle White 2006, 25; Brown and Ahern 2005).

In the means test, monthly income is the debtor's income for the six months preceding the date of filing for bankruptcy. If the debtor is filing jointly then both spouses' incomes are included; otherwise, a spouse's income may or may not be included depending upon circumstances. Included in a debtor's income is any contribution to household expenses by other people. It is unclear in the BAPCPA definition of income whether it refers to net income or gross income (an important distinction). Further, the means test follows guidelines set up by the Internal Revenue Service (IRS) for tax evaders and imposes severe limits for allowable expenses; for example, about $200 a month for food and less than $800 for housing and utilities.[6] In addition, the test subjects consumers to lengthy hearings in court and much higher attorney's fees, no matter which type of bankruptcy one files under (Brown and Ahern 2005; House Report 2005). The means test is complex, and not well understood by many people, including practicing bankruptcy attorneys, which is why it is characterized by many as over-exclusive and fallible (Brown and Ahern 2005; Hoffmann and Enslein 2006).

Attorney Regulations

Under the stricter requirements of BAPCPA, attorneys take on greater risk representing clients in Chapter 7 cases. It is stated in BAPCPA that "debt relief agencies" (attorneys) are regulated with greater scrutiny — requiring them to disclose clearly in a contract what they intend to do for their clients and all associated costs. These contracts are flexible and loosely designed, so it is questionable whether anyone actually gains from this arrangement (Hoffmann and Enslein 2006, 300).

If a lawyer represents someone in a Chapter 7 bankruptcy case and it is found later by the court that the person filing bankruptcy is not, in fact, eligible, for whatever reason (hidden assets are discovered or an accounting error), the lawyer is expected to pay back all expenses accrued by her client in the case to that point. And, more importantly, a civil penalty may be assessed against the attorney (Hoffman and Enslein 2006, 302). This rule is known as "reasonable investigation" (Section 102 BAPCPA) — meaning lawyers are supposed to perform financial background checks on their clients. Some lawyers have stopped offering Chapter 7 bankruptcy because of the increased risk. A National Association of Consumer Bankruptcy Attorneys (NACBA) survey released October 2006 noted that a quarter of bankruptcy attorneys saw the costs of filing bankruptcy rise over 100 percent; and 92 percent of attorneys said the costs had significantly increased (Sullivan 2006, 30-1). According to the Congressional Budget Office (CBO 2005), reasonable investigation will raise legal fees between $240 million and $800 million in 2007. CBO also predicts that these costs will be passed directly on to bankruptcy filers (House Report 2005). In the year since BAPCPA, attorney's fees for filing Chapter 7 and 13 bankruptcies have risen 43 percent and 41 percent, respectively (Hammes 2006, 7).

Filing Advice Restriction

Attorneys are now kept from giving advice regarding how to organize a debtor's debts. For example, if it is in a filer's best interest to sell an expensive automobile, payoff the loan, and use the remainder for buying a less expensive car the filer will have to get this information from sources other than their attorney because attorneys are disallowed from giving such advice. This regulation was put in place because it is believed that attorneys often times told clients to incur debt that will be written off when they file for bankruptcy. However, in most cases these debts are not dischargeable (i.e., credit cards) because the judge is careful to see when debts were incurred and what the money was spent on (Brown and Ahern 2005; Hoffmann and Enslein 2006, 300-1).

These attorney regulations have brought on a maelstrom of controversy. To date, three courts (U.S. District Courts of Connecticut, Oregon, and Texas) have ruled that filing advice restrictions (11 U. S. C. Section 526(a)(4)) on attorneys are unconstitutional because they limit attorneys' right to free speech (First Amendment of the U.S. Constitution).

Support Creditors

One of the few generally supported changes made by BAPCPA was the new rule that was supposed to make debtors more responsible for child support, alimony, or other similar debt. But so far BAPCPA has not lived up to expectations. According to Bryan Leach (2005, 245), the new law makes access to creditors' assets, wage garnishment, and so forth a competitive endeavor. For example, a woman who is owed child support will have to compete against credit card companies to collect.

And, of course, credit card companies are well positioned to use their asymmetrical advantage of ready-and-waiting collection agencies to pounce on newly declared bankrupts (Leach 2005). Usually this leaves the new bankruptcy filer financially drained limiting his ability to pay back child support and even future child support.

Automatic Stay

Under the automatic stay section, if someone has had a previous bankruptcy case discharged, and they file for bankruptcy again within one to two years, their creditors may not be dispelled. In other words, creditors are legally able to continue collecting payments owed. Furthermore, according to BAPCPA, by filing bankruptcy one can no longer avoid eviction from their home/apartment (Benoit 2006, 311; Brown and Ahern 2005).

Home Protection

There is a limit placed on the amount of assets one can protect from creditors ($125,000). This cap is in place for three years after filing for bankruptcy. Home improvements that might be seen as adding to the value of a home with the intent of hiding the money from creditors are also not allowed for 10 years. In addition, a filer cannot move to another state with more lenient rules regarding asset protection for 730 days after filing bankruptcy (Brown and Ahern 2005; Hoffmann and Enslein 2006, 303).

Perspectives on Personal Bankruptcy

According to Michelle White (1991), neoclassical economists believe the theory of consumer behavior is the theoretical foundation of personal bankruptcy. Consumers are believed to maximize their utility rationally in planning consumer spending on goods and services given a budget constraint (686). She also states that if bankruptcy laws are too lenient, then many consumers will take on considerable debt only to discharge it at the expense of society (687-90). This approach makes individuals the catalyst for bankruptcy, and disregards the impact of institutions, society, or government (Adkisson and McFerrin 2005, 448-9; Michelle White 1991, 697). It also avoids recognizing inappropriate lending practices of credit card companies as an impetus for bankruptcy. Furthermore, it fails to recognize that credit card companies exploit economic weaknesses (growing inequality, chronically low minimum wages) and human ones (emulative consumption). As Veblen wrote in the *Theory of the Leisure Class* ([1899] 1994, 103), people want to live one stratum above where they are currently. Today, credit cards give people the power to live above their means; but this typically results in heavy debt burdens. An element of truth exists that bankruptcy is, in part, people's fault; so increasing financial literacy is a reasonable goal that is a logical extension of neoclassical theory (Adkisson and McFerrin 2005, 448-9). However, this is not enough. Even armed with solid personal finance skills people are still susceptible to emulation, which Veblen ([1899] 1994, 109) wrote is a "pervading trait of human nature," and unanticipated disasters; therefore, bankruptcy is still necessary.

Research conducted by Teresa Sullivan, Elizabeth Warren, and Lawrence Westbrook (1999; 2000) show that consumers do not file bankruptcy by rationally calculating anticipated gains/losses due to filing. Instead, they found that a majority of consumers file for bankruptcy only when they became overwhelmed by debt. They further found that this, not the neoclassical theory of consumer behavior, best explains personal bankruptcy. Lawrence Ausubel (1997) came to the same conclusions and additionally posited that lack of understanding by consumers regarding interest rates, fees, and penalties placed them in a vulnerable position that credit card companies could abuse (see also Government Accountability Office 2006).

For institutional economists, personal bankruptcy is a complex matter. It results from many economic, social, and psychological factors. In particular, important institutional failures have allowed credit card companies to promote consumerism and enjoy profits generated from exploitation. One important institutional failure was the U.S. Supreme Court's 1978 Marquette Decision (Marquette National Bank of Minneapolis vs. First Omaha Service Corp.), which states that banks must obey the usury law in the state where they are located and not the state where their customers live. Because credit card operations are done mostly by mail, banks established credit card companies in states that allowed them to charge high interest rates (Ausubel 1997; Watkins 2000, 921-2). At this point, credit card companies began rapidly supplying consumers with cards, and this trend has not stopped. This occurred at a time of generally stagnant (or decreasing) real wages, record low savings rates, and rising costs for housing, education, and medical expenses (Manning 2000; 2001; Williams 2004, 43-5). People have to meet present needs/ wants with expensive credit, which they must repay with future income. This can create surplus profits for businesses, but poses a serious threat to consumer stability now that BAPCPA is enacted (Watkins 2000, 911). Waller (2001, 879-81) emphasizes this point by using Hyman Minsky's Financial Instability Hypothesis to show how many consumers are easily led into Ponzi schemes that are often difficult to escape.

John Kenneth Galbraith wrote in *The Affluent Society* ([1958] 1970, 169-70) that there exists significant danger in expanding debt for consumption. He argues people become reliant on a steady source of credit, and if there is a disruption in a borrower's income stream or the debt repayment costs become too high then this can lead to "painful consequences." He further states in *The New Industrial State* (1967 that it is not consumers who control the market, but rather producers (212-3). He then explains that producers actually dictate what and how much is bought and sold in the market. They are able, therefore, to manipulate consumer psychology (213-5). Waller (2001) echoed Galbraith's point well when he wrote:

> Since much of these banks' credit card marketing is done through unsolicited mailings, and since consumers often miscalculate the consequences of credit card debt . . . , in many ways these

> companies knowingly create the defaults and discharges. Thought of in this way it suggests that the public policy issue may reside in much more stringent regulation of this industry (875).

Empirical Findings

In order to make policy suggestions it is necessary to identify the important factors that lead people into bankruptcy. In a recent article, Charles Tabb (2006a) notes that little new research is available that analyzes this question empirically. This section provides empirical insights into the determinants of personal bankruptcy. The proceeding empirical results were calculated using three datasets: (1) Panel Study Income Dynamics (PSID) 1996 (8,511 observations); (2) Survey of Consumer Finances (SCF) 2004 (22,595 observations); and (3) Gallup Poll Survey conducted in 1997 of people who filed bankruptcy in 1996 (425 observations).

Neoclassical economists have argued in recent years that too many people take unfair advantage of the bankruptcy system (Adkisson and McFerrin 2005, 452-3; Michelle White 1991). While a small group of people may exist who abuse the system, this number is far outweighed by those who genuinely need to file bankruptcy. In the PSID dataset only 5.9 percent of the sample had ever filed bankruptcy, and of those, only 0.3 percent reported filing bankruptcy two times. Not one person in the survey recorded having filed for bankruptcy more than twice. Using the SCF dataset, 9.34 percent of the sample had declared bankruptcy at some point.[7] This number is still low when we consider that annual poverty rates in the United States are consistently over 12 percent (Census Bureau 2006). As John Watkins wrote: “Given the burden of debt, the question is not why there are so many bankruptcies . . . , but so few” (Watkins 2000, 924).

Many contemporary personal bankruptcy studies focus on medical expenses as a significant cause of personal bankruptcy (Buckley and Brinig 1998; Domowitz and Sartain 1999; Fay, Hurst and White 2000; Gross and Souleles 2002; Manning 2000; 2001; Stavins 2000; Sullivan, Warren and Westbrook 1999; 2000). But PSID data shows that only 12 percent of respondents gave medical/health care bills as the primary reason they filed bankruptcy (the fourth most popular answer). The most common reason given for having to file was that personal debts were too high/credit card misuse (over 34 percent). Credit card debt is the debt that shows up most consistently when people file bankruptcy — roughly 60 percent of all bankruptcy filers have significant amounts of credit card debt (Sullivan, Warren and Westbrook 2000, 119-20). Interestingly, the American Medical Association (AMA) — the United States’ second largest lobbying group — spent no money supporting BAPCPA; yet they stood to receive a financial gain from its passing.

A 1997 Gallup Poll Survey of people who filed for bankruptcy the previous year provides further evidence that credit cards are the primary determinant of personal bankruptcy. Of the 425 bankruptcy filers surveyed, 62.12 percent claimed credit card bills as a major reason they had to file bankruptcy, which is consistent with previous literature (Lawless 2006, 1-3; Sullivan, Warren and Westbrook 1999; 2000;

Waller 2001). The second most common reason people gave for having to file personal bankruptcy was job loss (38.59 percent). The third major reason was medical expenses (26.35 percent). This survey also showed that 95.06 percent of people stated that filing for bankruptcy was their last resort — they were left with no good alternatives for managing their debt. In this survey, bankruptcy filers were asked if they currently receive credit card offers in the mail and 89.18 percent responded that they do even though some of them had filed for bankruptcy less than a year ago (Gallup Poll 1997).

Many studies show that credit card debt is a primary determinant of personal bankruptcy. The following model, therefore, tests what factors determine the liklihood someone has revolving credit card debt, which has been previously identified (Lawless 2006; Manning 2000; Stavins 2000; Sullivan, Warren and Westbrook 1999; Waller 2001; Williams 2004) as an important predictor of bankruptcy. This way we can identify policy solutions that minimize revolving credit card debt thereby reducing bankruptcy rates, generally.

Using the 2004 Survey of Consumer Finances, a model was developed to analyze characteristics of people who carry revolving credit card balances. The Survey of Consumer Finances is a triennial survey that the Federal Reserve Board started administering in 1983. Data for the 2004 survey was collected in roughly six months' time from the middle of 2004 to the end of the year. In the following model, revolving credit card balances (CCBALAN) is the dependent variable and is coded as a binary variable (1 if someone has revolving credit card balances; 0 if not).[8] Because the model has a limited dependent binary variable, it was sensible to use the logit method of regression. A logit regression (a) allows for easy estimation "due to the functional form of the logistic distribution," (b) is estimable as a model of "choice between alternatives with random utilities," and (c) leads to simple interpretation because of the log-odds ratios (Kemp 2000, 3; Long 1997 79-83). An odds ratio larger than one means the coefficient is positive; the higher above one it is the greater its number associated with the dependent variable coded as 1 versus the alternative (coded as 0). Conversely, odds ratios below one reflect a negative coefficient; the lower below one it is the lower its number associated with the dependent variable coded as 1 versus the alternative.

Only two iterations of this model were tested. The first iteration included a variable for family size. It was collinear with another variable(s) in the model, however, so it was removed. The second iteration (equation 1) displays no multicollinearity (determined by observing each variable's low standard error, below). Table 1 contains definitions of all variables used in the model and Table 2 presents the second iteration's results.

$$
\begin{aligned}
CCBALAN_i = {} & \beta_0 + \beta_1 AGE_i + \beta_2 AGESQ_i + \beta_3 INCOME_i + \beta_4 JOB_i + \\
& \beta_5 SEX_i + \beta_6 MARR_i + \beta_7 BANKRUPT_i + \beta_8 HEALTH_i + \\
& \beta_m \sum_{m=1}^{5} EDUC_{mi} + b_i \sum_{j=1}^{4} RACE_{ji} + \varepsilon_I
\end{aligned}
\tag{1}
$$

Table 1. Definitions of Logit Model Variables

Variable	Definition
Ccbalan	Binary dependent variable—coded as 1 if respondent had a balance on her credit cards after last credit card payment (i.e. revolving credit card debt); 0 otherwise
Age	Age of respondent
Agesq	Age of respondent squared—accounts for decrease in bankruptcy probability in older people
Income	Household income—measured in thousands of dollars
Job	Binary variable—coded as 1 if respondent is employed, retired, or not in the labor force; 0 if unemployed
Sex	Binary variable—coded as 1 if male; 0 if female
Marr	Binary variable—coded as 1 if married; 0 if unmarried
Bankrupt	Binary variable—coded as 1 if respondent has ever filed bankruptcy; 0 otherwise
Health	Binary variable—coded as 1 if respondent has medical insurance; 0 otherwise
Educ	Vector of binary education variables; where people with a high school diploma serve as the base
Race	Vector of binary race variables; where white people serve as the base

Looking at the results presented in Table 2 we see that all variables are significant at the one percent level except BLACK and RACES OTHER (neither of which are significant at any accepted level of significance). The variables with the greatest statistical significance and telling odds-ratios are (1) bankruptcy, (2) marriage, (3) sex, and (4) Hispanic.[9]

More people who have ever filed bankruptcy (1.326 times) carry revolving credit card balances compared to people who have never filed bankruptcy.[10] This result suggests that people who have filed bankruptcy are more likely to continue taking on credit card debt and that credit card companies are not discouraged by people's previous bankruptcy status in issuing them credit or letting them keep (even increase) the lines of credit they already have. The 2004 Survey of Consumer Finances shows that 52 percent of people who have filed bankruptcy have revolving credit card balances compared to 36 percent of people who have never filed. So, people who file bankruptcy do not necessarily learn their lesson; furthermore, bankruptcy for many people may only be a short-term solution to their chronic financial problems. It is apparent that previous bankruptcy filers are more likely to take on credit card debt, which is something Manning (2000) has identified in his research, which indicates credit card companies intentionally target recent and past bankruptcy filers because they have demonstrated a predilection toward accumulating debt (Williams 2004).

Table 2. Logit Regression Results

Variable	Standard Error	Odds Ratio
Age	0.0059	1.063*
Age squared	<0.0001	0.999*
Income	<0.0001	0.999*
Job (1 employed; 0 unemployed)	0.0750	1.249*
Sex (1 male; 0 female)	0.0502	0.620*
Marr (1 married; 0 not married)	0.0447	1.514*
Bankrupt	0.0491	1.326*
Health	0.0402	1.756*
No high school diploma	0.0546	0.564*
Some college	0.0429	1.136*
College degree	0.0439	0.734*
Post college education	0.0480	0.531*
Black	0.0486	1.063
Hispanic	0.0574	1.388*
Races other	0.0754	1.081

*Statistically significant at the 1 percent level.

The results above also show that as someone gets older (AGE) their likelihood of having revolving credit card debt increases, but only up to some maximum age (AGESQ) then the likelihood of her carrying revolving credit card debt decreases (albeit slightly). This probably occurs because as people get older their expenses rise, which increases their reliance on credit cards; but after they get over this expensive period their need for credit diminishes. Married people are more likely than single people to have revolving debt (51.4%). This result is not too surprising because married people tend to have more expenses (children, houses, etc.), which significantly raise their debt burden. Women are 38.4 percent more likely to have credit card balances versus men. We can likely attribute this finding to the fact that women today make only $0.77 of every dollar a man makes, ceteris paribus (Census Bureau 2006). The only significant race variable is Hispanic: more Hispanics (1.388 times) have credit card balances versus whites. This discovery probably results from the fact that Hispanics have the second lowest median earnings of all race groups (the group with the lowest income are classified by the Census Bureau as "some other race") (Census Bureau 2006, 10). Having a college degree or post-college education decreases the probability of having credit card debt compared to high school graduates. This finding gives credence to initiatives aimed toward increasing financial literacy, and education, in general (more below).

Policy Prescriptions

A combination of factors has contributed to the rise in personal bankruptcy filing rates in recent years. But, as is argued here, institutional failures specifically with regard to credit cards have contributed most to the recent surge in filings. Unfortunately, BAPCPA does not address credit card debt's influence on personal bankruptcies. In fact, BAPCPA actually makes it easier for credit card companies to collect from debtors, thus making it harder for debtors to discharge credit card debt. University of Illinois Law Professor Robert Lawless (2006) summed up the above analysis well when he accurately stated: "Although the new law was called the Bankruptcy Abuse Prevention and Consumer Protection Act . . . it addressed abuses that did not exist and protected the credit industry instead of consumers" (1).

Due to credit card companies' loose underwriting practices with few standards for issuing credit some debtors become overwhelmed with credit card debt (GAO 2006, 5-7). This can translate into an overextension of consumer credit to households with no concern given to whether those households can reasonably manage the amount of credit issued. For example, over six billion credit card offers were mass mailed to U.S. households in 2006.[11] This technique is known as *carpet bombing* and is intended to inundate people with credit cards and checks so that if temptation (or need) arise they will have easy access to anonymous credit (GAO 2006, 90-1).[12] This technique must be tempered, and only a federal regulatory agency has the power to control this behavior.

Mitigating bankruptcy pressures brought on by the credit card industry (and consumer credit industries, in general) will best come from the Treasury's Office of the Comptroller of the Currency (OCC). OCC is responsible for regulating banks and credit card companies. They can establish more practical underwriting standards for credit card companies and consumer lending agencies. For example, by setting a limit on the interest rates credit card companies can charge. Since the Marquette Decision, credit card companies have had *carte blanche* with the rates they charge and no standards for when interest rates should increase. Therefore, a reversal of the Marquette Decision may well eliminate many problems associated with companies charging high interest rates. In addition, credit card companies have few restrictions when setting credit limits. Factors such as income, credit history, and bankruptcy history are rarely, if ever, used to set credit lending parameters. Carefully monitoring who credit card companies give credit to, and how much, will raise industry standards. It may also prove useful to charge a penalty to companies that give too much credit to risky borrowers.

Recently, OCC required some credit card companies to raise the minimum balance due on credit card bills to four percent, but most companies are exempt. Moreover, a minimum payment of four percent is still probably too low to keep people from accumulating excessive revolving debt — the industry standard of five percent several years ago did not discourage people from accumulating revolving debt. A more significant increase in minimum payments, one that affects all credit card companies, must be passed. They should experiment with different minimum payment percentages to see what is most reasonable. Before the Marquette Decision, many credit cards required borrowers to pay their balances in full every month. While this is probably unnecessary today, it may be sensible to raise minimum payments to as high as 10-25 percent so people avoid paying much more for their credit card debt than is prudent (Manning 2000; Sullivan 2006).

According to the Census Bureau (2006), 46.6 million people (15.9 percent) do not have health insurance, and many more have insufficient coverage. It is widely accepted that medical expenses are a determinant of bankruptcy. While it is beyond the scope of this paper, it is practical to state that this problem requires attention. There should be more provisions in the bankruptcy legislation that allow certain medical expenses to be dischargeable.

BAPCPA's version of credit counseling has proven inadequate. In principle, it is still a good idea. However, credit-counseling agencies should be independent from credit card companies and any other organization that might benefit from their work. Establishing non-profit credit counseling agencies funded by the government would secure their independence and ensure debtors have access to unbiased recommendations.

Furthermore, it is necessary to begin the education process before consumers are in bankruptcy-level financial trouble. Recently, while working with the Jersey Shore Council of the Boy Scouts of America to assess financial literacy rates of New Jersey students, we together developed and implemented a financial literacy program for students in grades two to five (which later developed into an analysis of high school students' financial literacy) in several local schools. In our study, we found little student interest about money until grade five. But once students reached fifth grade they had a complex understanding of money and were eager to learn more about it and its many nuances. Therefore, based on these preliminary empirical findings, it seems sensible to consider starting formal financial literacy training around fifth grade and continuing through high school.[13]

Adopting a personal finance curriculum as part of social studies, math, or elective courses will give students a better understanding of the risks associated with poor money management. An increasing number of today's high school students work; and many take on expensive education loans (Manning 2001; Schor 1991, 26-7). Their understanding the distinction between good debt and bad is important. It will take little time and effort to show students that improper credit card use can lead to "painful consequences."

Conclusion

Credit card companies fought long and hard to ensure the passing of BAPCPA. More than a year after its enactment, it is becoming clear that BAPCPA is incapable of deterring opportunists from abusing the bankruptcy system (Michelle White 2006). Instead, it has had unadvertised ancillary effects such as raising bankruptcy filing costs, limiting people's access to bankruptcy, making it easier for credit card companies to collect past debts, and complicating the bankruptcy system further in favor of creditors. In short, it has hurt that portion of the population who genuinely need (now or in the future) a more debtor-friendly bankruptcy system and who use it only as a last resort (evidenced in the empirical findings section above).

Credit card companies argue that they lose substantial profits due to consumers filing bankruptcy. They also argue, however, that they charge exorbitantly high interest rates and fees to control for their increased risk when issuing credit to risky borrowers; yet since BAPCPA was ratified, interest rates have increased not decreased (Board of Governors 2006). Credit card companies have double profit indemnity: (a) they have freedom to issue risky borrowers significant amounts of credit without considering their ability to manage the credit given; and (b) they can charge borrowers arbitrarily selected interest rates and fees, which leave many borrowers little chance of escaping their debt except by slowly paying it off over a long period or now by filing under Chapter 13, which is more expensive today, time consuming, and rarely completed. The OCC needs to tighten credit card companies' lending practices so consumers avoid becoming unnecessarily overburdened with debt — they can do this by setting pragmatic usury and underwriting standards. This need not limit people's access to credit, but rather ensure they are allowed a practical level of credit given factors such as credit history and income.

Due to BAPCPA, credit card companies will likely relax further their already loose lending policies and extend debt to even riskier borrowers thus raising the probability that those people will accumulate revolving debt (Michelle White 2006). Therefore, people have to take greater responsibility and show more resourcefulness regarding their personal finances. The way to aid this process is to promote that a larger percentage of schools' curriculums be dedicated to raising students' financial literacy. This policy is a long-run initiative with many measurable benefits beyond those outlined in this paper. This approach completes a two-sided solution to the rise in credit card debt — and the subsequent rise in personal bankruptcies — in which institutions (credit card companies, government regulators) and individuals (borrowers) take greater accountability for securing people's financial stability.

Notes

1. "ABI is a nonprofit, nonpartisan professional association with 11,000 members involved in the bankruptcy process — lawyers, accountants, financial and restructuring professionals, judges, academics, lenders, and others in the insolvency community" (Gerdano 2006, 1).
2. There is also Chapter 12 personal bankruptcy, which is a special case for family farmers.
3. Since the invention of Chapter 13 bankruptcy in 1938, Chapter 7 bankruptcies have consistently made up 70 percent of all bankruptcies. Since many people anticipated BAPCPA they filed for Chapter 7 early, which probably accounts for the slow down in bankruptcy filings since October 2005 (Skeel 2001).
4. Also, creative legislative blocking by anti-bankruptcy reform advocate New York Senator Chuck Schumer helped extinguish the 2001 Act.
5. Typically, these credit agencies are members of the National Foundation for Credit Counseling (NFCC). Despite NFCC's positive reputation, a majority of their funding comes from financial organizations such as credit card companies.

6. The Internal Revenue Service Standard Guidelines (both national and local) for repayment are available on the IRS website (www.irs.gov).
7. This number includes all forms of bankruptcy: Chapter 7, 11, 12, and 13. The SCF does not distinguish between the different types of bankruptcy.
8. We are most interested in studying the differences in people who carry revolving credit card balances versus those that do not; therefore, measuring this variable as a binary variable (1 if they have revolving credit card debt; and 0 if not) is the most effective way to identify what characteristics most likely lead to revolving credit card debt.
9. Because the Survey of Consumer Finances is survey data, no goodness-of-fit testing procedures are available (Bertolini et al. 2000, 251-2).
10. Log-odds-ratios indicate the probability of an event's occurrence relative to an event not occurring. An odds ratio greater than one means there is a higher probability of an event occurring (in this case revolving credit card debt); while an odds ratio smaller than one means there is a lower probability of an event occurring. For example, looking at the variable JOB, there are 1.249 higher numbers of people who filed bankruptcy that have jobs compared to unemployed people.
11. This makes up an estimated seven percent of all mail volume in the United States.
12. Carpet-bombing is a term borrowed from the military. It refers to the use of gravity or incendiary bombs to destroy an area.
13. The Jump$tart Coalition for Personal Financial Literacy is a Washington D.C. based non-profit organization created in 1995. They conduct a biennial survey of high school seniors across the United States to assess their level of financial literacy. Jump$tart is actively engaged in furthering the goal of greater, and better, financial education in school systems nationwide (www.jumpstart.org).

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