

## **Are Debtors Abusing Bankruptcy By Repeat Filings?**

Using 20 years of data, this study developed a framework for sorting repeat bankruptcy filers into one of three categories: abusers, non-abusers and possible abusers. Of the 2,194 cases examined, one-third of debtors filed more than once over 20 years in this district. There were 235 (10.7%) debtors who appeared to be abusing bankruptcy by repeat filings. A similar number (N= 231) were classified as possible abusers, resulting in a total of 21.2% of the sample who may be abusers. With one in five debtors in this district filing repeatedly, this study suggests that repeat filers may be a problem in this district.

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### **Introduction**

Since 1980, the number of personal consumer bankruptcy filings in the United States increased from about 300,000 to 1,600,000 in 2003. In the period between 1994 and 2003 personal bankruptcy filings in Utah increased from 6,591 to 22,084 (U.S. Department of Justice, 2004). Among these stark numbers, Utah also leads the nation in the number of bankruptcies filed per household at one filing per 36.7 households (American Bankruptcy Institute, 2004). The rising number of bankruptcy filings is a current concern at the national level as well as in Utah.

A survey of attorneys, accountants, academics, judges, trustees, lenders, and other bankruptcy professionals conducted by the American Bankruptcy Institute reported that serial bankruptcy filings are a significant problem (American Bankruptcy Institute, 2004). Serial filers attempt to use bankruptcy to deliberately thwart creditor's attempts to collect, often with no intention of completing their proposed repayment plan (Weston, 2004). Two-thirds of the creditor representatives and nearly half of the judges also viewed serial filings as a significant problem. United States Senator Jeff Sessions called the attention of Congress to the "deep problem of abusive and repeat" bankruptcy filings (Lewis, n.d.). Debtors who repeatedly file bankruptcy are perhaps doing so in effort to delay foreclosure, avoid paying taxes, or deal with difficult creditors (Nelson, 2000). These debtors may have no intention of completing their bankruptcy plan and thus contribute to the growing number of cases if they file again. Creditors are also finding the bankruptcy process troublesome because foreclosure actions are being delayed for up to five years or more when debtors file bankruptcy repeatedly (Nelson, 2000; Norberg, 1999). The United States Trustee Program identified serial filings and abuse of the system among issues that present significant challenges to the bankruptcy system (Darling & Redmiles, 2002).

### **Bankruptcy Basics**

Bankruptcy law and regulations are governed by the Federal Bankruptcy Code but implementation varies by state or court district. As soon as a debtor files for bankruptcy they are protected by the automatic stay which prohibits collection activity and halts the foreclosure process. Only unsecured debts can be discharged in bankruptcy. A debtor can discharge unsecured debt in a chapter 7 liquidation or propose to repay a portion of their debts in a chapter 13 repayment plan. Debtors are limited to one chapter 7 liquidation every six years. In chapter 7 bankruptcy, equity in property is divided into exempt and nonexempt categories. State and federal bankruptcy law specify which property is exempt. Generally, a certain amount of equity in a home, car, clothes, jewelry, appliances, and furniture is exempt from creditors. Debtors with significant amounts of nonexempt property may choose chapter 13 where they are able to pay the secured debts under court protection. In chapter 13, debtors make monthly payments to the court trustee who distributes the funds to creditors. It generally takes three to five years to complete a chapter 13 repayment plan; there are no restrictions as to how often a debtor can file chapter 13. Those chapter 13 debtors who are not successful in their repayment plan may convert to a chapter 7 or have their case dismissed by the court. Once a case is dismissed the debtor becomes subject to collection efforts. Dismissal may occur for a number of reasons: the debtor did not appear in court, filled out the paper work incorrectly, or stopped making payments on their plan. Dismissed cases are included when counting the total number of bankruptcy filings. Only 26.5% of 1997 chapter 13 filers in Utah completed their plan (Evans, 2004). When debtors' cases are dismissed many file bankruptcy again.

One explanation for abuse of the system, as well as repeat filing, is found in the automatic stay provision. The automatic stay goes into effect at the time of filing and prevents creditors from making further collection actions. The automatic stay prevents the start or continuation of foreclosures, repossessions, garnishments, attachments, utility shut-offs, evictions, and debt collection harassment (National Consumer Law Center, 2002). One problem in trying to determine whether debtors are abusing the system is that it is not clear at initial filing when a bankruptcy petition is abusive or not in good faith. Many debtors who file in good faith fail to complete a repayment plan.

This study will examine debtors who filed for bankruptcy more than once in twenty years. The purpose of this study is to describe the incidence of repeat filers in one district and to assess the extent to which repeat filers are abusing the system. This study developed a methodology for determining the incidence of repeat filers and distinguishing abusive filings from non-abusive filings. Results of this study should enhance our understanding of the growing number of bankruptcy filings and contribute to information about repeat filers that will be useful for guiding bankruptcy policy.

### **Literature Review**

While there is a growing body of research on consumer bankruptcy, very little research has examined repeat bankruptcy and abuse of the system. The first section of the literature review discusses a number of factors that researchers and professionals suggest may lead to consumer bankruptcy filing. Much of the literature merely suggests that there is a problem with repeat bankruptcy filers but little research has actually been conducted. The second section of the literature review focuses on the few studies that report the incidence of repeat bankruptcy filings. No research study has addressed the question of quantifying abusive filings.

When considering what factors contribute to bankruptcy filings, a natural assumption is that people are spending money irresponsibly. Research on consumer bankruptcy has shed some light on what other factors may contribute to bankruptcy. These factors include buying more home than is affordable, home equity loans, abuse of credit cards, inadequate insurance, job loss, and the cost of raising children (Lown & Rowe, 2002; Sullivan, Warren, & Westbrook, 1989). In research conducted by the American Bankruptcy Institute (1996) experts cited some primary causes of bankruptcy: ease of obtaining personal credit, loss of a job, financial mismanagement, medical problems and marital/family problems. The declining social stigma of bankruptcy may also encourage filing (Lewis, n.d.). Other literature suggests macroeconomic factors also contribute to bankruptcy. Strong prosperous economies with low unemployment rates can perhaps increase consumers' willingness to take on more financial risk and demand for credit; subsequent recessions and job losses then trigger bankruptcies (Lewis, n.d.).

A survey by the American Bankruptcy Institute (1996) confirmed that abuse of the bankruptcy system is perceived as a problem, but it is not considered to be rampant. Respondents including attorneys, accountants, academics, judges, trustees, lenders, credit managers, turnaround consultants, and several other types of bankruptcy professionals completed a survey covering a broad spectrum of possible areas in need of reform. About 40% of respondents believed that serial filings are a significant problem. Debtor attorneys downplayed serial filings as a problem while almost two-thirds of creditor attorneys and more than half of the judges, viewed serial filing as a significant concern. Because courts are organized into districts, and some states contain more than one district, it is possible that there is wide variation in the extent of repeat filings among districts although there is no statistical evidence (Williams, 1997).

According to Weston (2004) repeat filers tend to fall into one of three categories, chapter 7 repeat liquidators, chapter 13 repayment plan failures, and serial filers. Repeat liquidators file chapter 7 as often as allowed by law, every six years. Repayment plan failures are those debtors who file chapter 13 and do not complete their repayment plan. When their case is dismissed, repayment plan failures may file chapter 13 again or file chapter 7; each filing is counted as a separate case.

Norberg's (1999) study of Southern Mississippi debtors considered whether multiple filings indicate abuse. Results indicated that 39% (28 of 71) of the debtors had filed one or more previous bankruptcy cases. One-third of all debtors had filed only one previous case. Of those debtors who filed only one previous bankruptcy, two-thirds filed under chapter 13 while the remaining third filed under chapter 7. Chapter 13 debtors who filed only one previous bankruptcy were significantly more likely to achieve a discharge in Norberg's study. Only five debtors had filed more than one previous case. All five of these debtors filed their previous cases in chapter 13 and none received a prior discharge. Norberg (1999) concluded that the filing of a single previous case was not an indicator of abuse, while multiple prior bankruptcies may be a strong indicator.

Sullivan, Warren, and Westbrook (1989) defined a “true repeater” as someone who files bankruptcy, discharges their unsecured debts, runs up more debt, and receives yet another discharge. About 8% of their sample (120 of 1,502) had filed a previous bankruptcy petition. Because the chapter 13 files were incomplete, the researchers were unable to determine the number of true repeaters. They were able to identify only the “potential repeaters” or those who filed previous bankruptcies who may have been discharged. In the Sullivan, et al (1989) study, debtors were categorized into four groups: no-repeat discharges, two bankruptcies in quick succession, two filings but not two discharges, and those not looking for a second discharge. Debtors whose circumstances caused them to file twice in order to complete one discharge were classified as ‘no-repeat discharges.’ There were 23 debtors who made two attempts in order to complete one bankruptcy discharge. Debtors who filed two bankruptcies in quick succession did not receive a second discharge. These debtors filed chapter 7 within two to six years after their first filing, thus barring them from a discharge in chapter 7. Five debtors filed chapter 7 within six years of their previous filing, so either they did not obtain a discharge in their previous case or their second case was dismissed. There were 32 debtors who made their second filing in chapter 13 and were dismissed without a discharge. These debtors filed twice but did not receive two discharges. The last group of debtors were those not seeking a second discharge. These 14 debtors filed chapter 13 a second time trying to pay 100% of their debts. Whether these debtors succeeded or failed, they did not receive two discharges because they were either dismissed from their bankruptcy or paid back 100% of their debts. Finally, 56 debtors out of 1,502 (3.7%) potentially received two discharges and were classified as “potential repeaters” (Sullivan et al., 1989).

Another study compared repeat petitioners to one time petitioners (Strand, Hira, & Carter, 1994). Data were collected in one Canadian province (Manitoba) and one U.S. state (Iowa) from randomly selected bankruptcy records and a survey of debtors. The sample comprised 150 respondents total; 14% of filers at each location were repeat filers. Repeat petitioners had lower mean monthly income, lower monthly expenses, lower mean value of total assets, lower mean value of secured debt, and lower mean values of unsecured debt. While financial characteristics differed between repeat and one time petitioners, sociodemographic characteristics were similar (Strand et al., 1994).

Many bankruptcy professionals (American Bankruptcy Institute, 1996) believe that there is a problem with abusive and repeat filings. Previous research concludes that a relatively small percentage of bankruptcy filers actually file more than once and few of those receive multiple discharges. Sullivan, Warren, and Westbrook (1989) were unable to determine a precise number of true repeaters because the bankruptcy documents were incomplete and the five year time limit for chapter 13 repayment plans left some cases still pending. Although no research quantifies the extent to which repeat filers abuse the bankruptcy system, there is considerable concern in Congress and among bankruptcy professionals.

This study is the first to judge whether repeat filers are abusing the bankruptcy system. The study is groundbreaking because it utilizes a 20 year time frame and a much larger sample than prior studies. This study will take advantage of a court electronic document filing system to track previous bankruptcy filings in this district by the Social Security number of the filer; therefore missing or incomplete information from debtor petitions about previous filings is not a concern unless they are filing under an illegal social security number. The university’s Institutional Review Board approved the study.

### **Purpose**

This study differentiates abusive repeat filings from non-abusive filings. According to a chapter 13 bankruptcy trustee (K. Anderson personal communication, July 8, 2004), three bankruptcy filings in a two year period is considered abusive. This definition is consistent with Darling and Redmiles (2002) who stated that serial (or repeat) filers are those who file bankruptcy numerous times within a short period of time. For purposes of this study, repeat filers are defined as debtors who filed bankruptcy two or more times during the 20 year period (1984-2004). This study will further seek to answer the question: to what extent are repeat filers abusing the bankruptcy system?

### **Methodology**

The sample consisted of 2,194 randomly selected cases from the 12,055 petitions filed in the federal district bankruptcy court in Utah in 1997. The 1997 sample was used because extensive financial, employment, family and socio-demographic data were collected for a previous study using the PACER/Electronic Case Filing System (ECF). This system includes all of the bankruptcy files in the district for 1984 to the present, and can be viewed via the Internet. Free ECF access was granted for this study by the chief bankruptcy judge.

Bankruptcy petitioners are required to report on their petition, or application for bankruptcy, whether they filed for bankruptcy in the previous six years. It is expected that some of this information will be incomplete as petitioners may not report previous filings (Sullivan, Warren, & Westbrook, 1989). Therefore, the ECF system was searched between 1984 and 2004 by social security number for all cases filed by the debtors in the sample. Debtors may have filed in other districts but this study is limited to cases filed in this federal court district. Only debtors who filed as the same filing status across the entire twenty year period were included in the analysis. Filing status refers to whether the debtor filed a joint petition, which is limited to married couples or filed as an individual, regardless of their marital status. Debtors whose filing status changed during the twenty year period were excluded because of the challenge in making judgments about their marital history. Because finances play an important role in marital relationships, assumptions cannot be made about debtors who file repeatedly with a different marital or filing status.

Debtors were sorted into repeaters or one-time filers (Figure 1). Debtors fell into the repeaters category if they filed bankruptcy more than one time in this district between 1984 and 2004. One-time debtors filed bankruptcy only once in this district between 1984 and 2004, this one filing being the 1997 case.

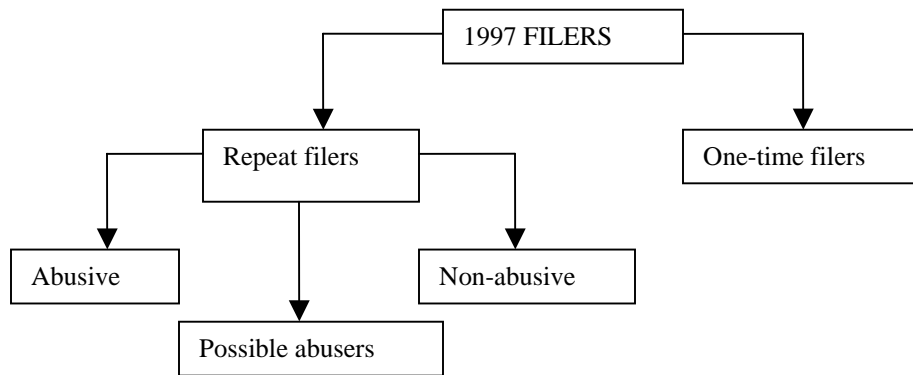


Figure 1 Illustration of framework for sorting filers.

First, debtors who filed more than once during this 20 year period were sorted into three sub-categories: abusers, non-abusers and possible abusers. In general debtors who had at least three filings within any two year period across the twenty year time frame were classified as abusive. The only exception to this definition were cases where a second or third attempt at completing a chapter 13 or converting to a chapter 7 resulted in a third filing within two years. These debtors were classified as non-abusive. Possible combinations of these types of repeat filings are shown in Table 1. Debtors desiring the relief that bankruptcy provides may refile a chapter 13 for another attempt at a repayment plan or file chapter 7 for more expedited liquidation (K. Anderson, Chapter 13 Bankruptcy Trustee, personal communication, July 8, 2004). Debtors may receive up to two chapter 13 dismissals followed by a chapter 13 or chapter 7 discharge and not be considered abusive.

Table 1.  
Possible Combinations of Second or Third Attempts at Chapter 13 Repayment Plan

1 <sup>st</sup> Filing		2 <sup>nd</sup> Filing		3 <sup>rd</sup> Filing	
Chapter	Outcome	Chapter	Outcome	Chapter	Outcome
13	Dismissed	13	Dismissed		
13	Dismissed	13	<i>Discharged</i>		
13	Dismissed	7	<i>Discharged</i>		
13	Dismissed	13	Dismissed	13	<i>Discharged</i>
13	Dismissed	13	Dismissed	7	<i>Discharged</i>

Debtors who filed only twice during the twenty year period were categorized according to the chapter and outcome of their two filings in order to determine to which category they belonged. Two-time filers were sorted according to the combinations shown in Table 2. Judgments regarding abuse were established based on the time frame between the two filings.

Table 2.  
Map of Sorting Two-time Filers by Chapter and Outcome

1 <sup>st</sup> Filing		2 <sup>nd</sup> Filing		Condition	Category
Chapter	Outcome	Chapter	Outcome		
13	Dismissed	13	Dismissed	If < 5 yrs apart If > 5 yrs apart	Possible Abusers Non-abusive
13	Dismissed	13	Discharged	-	Non-abusive
13	Discharged	13	Discharged	If < 10 yrs apart If > 10 yrs apart	Abusive Possible Abusers
13	Discharged	13	Dismissed	-	Possible Abusers
13	Dismissed	7	Dismissed	If < 5 yrs apart If > 5 yrs apart	Possible Abusers Non-abusive
13	Dismissed	7	Discharged	-	Non-abusive
13	Discharged	7	Discharged	If < 10 yrs apart If > 10 yrs apart	Abusive Non-abusive
13	Discharged	7	Dismissed	If < 5 yrs apart If > 5 yrs apart	Possible Abusers Non-abusive
7	Dismissed	7	Dismissed	-	Possible Abusers
7	Dismissed	7	Discharged	-	Non-abusive
7	Discharged	7	Discharged	If < 10 yrs apart If > 10 yrs apart	Abusive Non-abusive
7	Discharged	7	Dismissed	-	Possible Abusers
7	Dismissed	13	Dismissed	If < 5 yrs apart If > 5 yrs apart	Possible Abusers Non-abusive
7	Dismissed	13	Discharged	-	Non-abusive
7	Discharged	13	Discharged	If < 10 yrs apart If > 10 yrs apart	Abusive Non-abusive
7	Discharged	13	Dismissed	If < 5 yrs apart If > 5 yrs apart	Possible Abusers Non-abusive

All filers with three or more filings who did not fit into any of the latter definitions were categorized as possible abusers and analyzed individually to determine whether they were abusive, non-abusive, or possible abusers. It is important to note that one-time filers have the potential to be repeaters. Although age of debtor is often left blank on the petition, younger debtors may be more likely to be one-time filers because they were too young to file in previous years. The data are also limited to one court district. Debtors who moved into or out of the state during this 20-year period could have filed in other districts.

Results of the analysis are reported as frequencies and percentages. The number and percentage of each of the three categories of repeat filers, abusers, non-abusers and possible abusers are reported in the results.

#### Results

Table 3.  
Total Number of Filings for 1997 Debtors Over Two Decades (n=2,194)

Total number of filings 1984-2004	Frequency	Percent
11	1	0.04%
10	1	0.04%
9	3	0.14%
8	8	0.36%
7	13	0.59%
6	15	0.68%
5	38	1.72%
4	85	3.87%
3	192	8.75%
2	387	17.64%
1	1,451	66.13%
Total	2,194	100.0%

Table 3 illustrates frequencies for the total number of filings across the 20-year period. One debtor filed bankruptcy 11 times over two decades. There were 744 (33.9%) debtors who filed two or more times over the 20-year period. Using the criteria for sorting repeat filers as discussed in the methodology, there were 235 (10.7%) debtors who fit the category of abusers and 231 (10.5%) who were possible abusers. If these two groups are combined, 21.2% of the sample could be considered repeat abusers of the bankruptcy system.

Table 4.  
Summary of Filing Status by Frequency of Petitions (n=2,194)

Category	Frequency	Percent
Abusers	235	10.7%
Possible abusers	231	10.5%
Non-abusers	278	12.7%
One-time filers	1451	66.1%

### Conclusions

This is an exploratory study investigating whether or not debtors are abusing bankruptcy by filing repeatedly. No previous research has focused on repeat bankruptcy filers to this extent. According to the method developed for sorting bankruptcy filers, it was found that 10.7% of debtors in the sample appear to be abusing the bankruptcy system. Possible abusers comprise 10.5% of 1997 bankruptcy filers; therefore, up to 21.2% of the 1997 bankruptcy filers may be abusing the bankruptcy system. Bankruptcy professionals have reported that serial bankruptcy filings are a significant problem (American Bankruptcy Institute, 1996). This study, though limited to one district, has provided quantitative support for the concern about repeat bankruptcy filing.

Further research should investigate characteristics of debtors associated with repeat bankruptcy and abuse of the bankruptcy system. Other states or court districts should implement similar studies to investigate the extent that repeat bankruptcy filers are abusing the system within their district. Results of this study are valuable to academics, bankruptcy professionals, and policy makers. Repeat bankruptcy contributes to the growing number of bankruptcy filings and this understanding may be useful for guiding bankruptcy policy.

The results of this study raise questions for the lending community. If creditors lend money to debtors who have filed bankruptcy more than twice, do they realistically expect the borrower to fulfill their obligation to repay? Perhaps some creditors are simply gambling that repeat bankruptcy filers will pay high interest rates for a sufficient period that they will make enough profit to justify the loan even if the borrower defaults. With all the concern in the creditor community about debtors abusing the bankruptcy system, the lenders must acknowledge that they are part of the problem if they loan money to repeat filers. Perhaps lenders no longer examine credit reports but simply rely on a credit score to make lending decisions.

With about 11% of bankruptcy filers in this district apparently abusing the system and potentially one in five debtors falling into this category, the officials in this court district may want to review their procedures for confirming cases. Each bankruptcy petition is reviewed by a trustee. The debtor is subject to questioning at the Section 341 meeting of creditors, and then a few months later, the case is confirmed. With the availability of the electronic case filing system (ECF), each trustee could assign a staff person to search by Social Security number for each new petition. If the search turns up previous filings, the case could be flagged for additional scrutiny. Due to the dramatic growth in case loads over the past decade, less time is available for scrutinizing each petition. Perhaps the addition of the simple step of searching for prior filings might be well worth the while of the court. The court has the right to deny bankruptcy court protection to debtors who are abusing the system. It is not known how often this occurs.

Both lenders and the court administrators have the opportunity to reduce the court case load by identifying and investigating debtors who appear to be abusing the system. The ECF system provides the technology for identifying potential abusers. While debtors with legitimate reasons for repeat filings should be allowed the protection offered by federal law, those who are simply abusing the system should be identified and investigated. It is possible that repeat filers who appear to be abusing the system may have substance abuse, mental health or medical problems and should be referred to appropriate professionals for counseling. At the same time, creditors should be more selective in granting credit to debtors with a history of bankruptcy petitions.

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