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STILL CHASING CHIMERAS BUT FINALLY SLAYING SOME DRAGONS IN THE QUEST FOR CONSUMER BANKRUPTCY REFORM

*Jason J. Kilborn**

Consumer bankruptcy systems in Europe and the United States have witnessed especially robust and dynamic development during the past decade. The ever-rising volume of seeking entry to these systems now allows for cross-systemic comparisons of substantially differing “markets” for the relief that these systems offer. In particular, the distinct trend toward greater efficiency seen in other financial markets can be increasingly observed in most consumer bankruptcy regimes, with some notable exceptions. In this context, market performance can be gauged in part by the degree to which systems offer efficient and effective relief as a stimulus to deploying available debtor resources to paying debts while reducing waste in fruitless collections activity and avoiding old and inefficient shibboleths that prevent the efficient allocation of default risk.¹

An evaluation of the performance of consumer bankruptcy reform depends in large part upon one’s perspective. Creditors will likely never be satisfied with the proliferation and refinement

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¹ For a discussion of some of the most salient goals and purposes of modern consumer bankruptcy law, see Jason J. Kilborn et al., *THE WORLD BANK, Draft Report on the Treatment of the Insolvency of Natural Persons* (2012), <http://siteresources.worldbank.org/INTGILD/Resources/WBPersonalInsolvencyReportOct2012DRAFT.pdf>; INSOL INTERNATIONAL, *CONSUMER DEBT REPORT II 1-24* (2011).

of systems that impose a coercive end to debt collections, conclusively robbing creditors of their right to attempt to extract payment from their debtors. Moreover, creditors will likely always complain of rampant “abuse” of these systems by debtors who are perceived as having the means to pay but otherwise lacking the will. But these are among the chimera notions that both developing and developed consumer bankruptcy regimes have chased relentlessly in the past, at significant and often wasted expense to the state and society. Notions of widespread abuse of “debtor-friendly” systems indeed fit the definition of “chimera,” for they are largely if not entirely “unreal creature[s] of the imagination, a mere wild fancy.”²

This paper examines reforms in six prominent consumer bankruptcy systems that have occurred within a little more than a decade, evaluating which of them continue to pursue chimeras of abuse and which have actually begun to slay some real dragons, primarily the twin monsters of inefficiency and waste. It reveals whether these reforms have achieved their stated goals of improving efficiency and effectiveness, as opposed to chasing chimerical abuse. It concentrates on the most salient aspects of recent reforms and their effects, particularly the degree to which reforms have enhanced the risk-shifting efficiency and effectiveness of these systems, developing a more social policy-oriented concentration on, e.g., fighting social exclusion and restraining the anti-social effects of deregulated consumer finance markets. Progressing from worst to best, this examination begins

² THE OXFORD ENGLISH DICTIONARY, VOL. III, 121 (2d ed. 1989) (definition 3(b)). Published evidence of the existence of “abuse” is inevitably sparse, since the concept is difficult at best to measure. Informal evaluation of systems around the world by actors in those systems uniformly suggests that, however abuse might be defined, it infects only a small fraction of cases. Where official system supervisors have gauged the incidence of debtor misbehavior so serious as to represent abuse, they have confirmed the anecdotal accounts. See, e.g., The Insolvency Service, *Annual Report and Accounts 2010-11*, at 33-35 (2012), available at www.bis.gov.uk/assets/insolvency/docs/publication-pdfs/annual2010-11web.pdf; US Department of Justice, US Trustee Program, *Annual Report of Significant Accomplishments 2010*, at 17-19 (2011), available at http://www.justice.gov/ust/eo/public_affairs/annualreport/index.htm. Voluminous academic empirical study has more clearly belied the notion of “fraud” in the broader sense of solvent debtors’ attempts to evade their obligations. See, e.g., Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, *Less Stigma or More Financial Distress: An Empirical Analysis of the Extraordinary Increase in Bankruptcy Filings*, 59 STAN. L. REV. 213 (2006) (citing earlier studies).

with the thoroughly misguided and counterproductive U.S. reform of 2005 and ends with the increasingly impressive series of reforms implemented in France in 1999, 2004, and 2010. Between these poles, the examination progresses through reforms in the Netherlands in 2008, Denmark in 2005, Sweden in 2007, and Germany in 2002, charting a steadily increasing ratio of positive to negative design and result. Overall, the European systems seem to have performed quite well. Broadly speaking, the European reforms have enhanced efficiency by eliminating wasteful formality, targeting appropriate forms of relief to those who clearly need it, and appropriately socializing the burdens of financial distress and assigning financial market risks to sophisticated repeat players better able to gauge and minimize those risks.

I. THE UNMITIGATED DISASTER OF THE U.S. CONSUMER BANKRUPTCY REFORM OF 2005

The mid-1990s saw the first major reform of U.S. consumer bankruptcy law since the adoption of the Bankruptcy Code in 1978.³ Three factors converged to push an ill-conceived and poorly drafted reform bill through the legislative process: (1) the ebb and flow of politics had moved toward a more conservative position, (2) the general economic situation (especially investment asset values, such as home equity and stocks) was at all-time highs, and yet (3) annual personal bankruptcy filings had exceeded the psychologically important one million mark in 1996.⁴ Empirical evidence demonstrated that these filers were overwhelmingly among the exceptional casualties of an otherwise robust economy; they were drowning in debt with no hope of returning any significant dividend to their creditors over a reasonable period. Only the smallest fraction of filers might be said to be “abusing” the privilege of debt relief.⁵ Nonetheless, credit card lenders and their conservative political allies pursued a single-minded campaign of curbing perceived abuse by “can-pay” debtors seeking an easy way out of their debts.

³ See, e.g., Jason J. Kilborn, *The Hidden Life of Consumer Bankruptcy Reform: Danger Signs for the New U.S. Law From Unexpected Parallels in the Netherlands*, 39 VAND J. TRANSNAT'L L. 77 (2006), at 91, n.7.

⁴ *Id.* at 109.

⁵ See, e.g., Sullivan et al., *supra* note 2, and other studies cited therein.

A major credit card issuing bank (MBNA) drafted a reform bill, and a conservative member of Congress ultimately sponsored it. The reform bill sought to reduce the number of bankruptcy filings generally, while identifying “can-pay” debtors, denying them access to an immediate discharge in a Chapter 7 liquidation of their (usually negligible) assets, and offering such debtors relief only through a five-year payment plan under Chapter 13.⁶ After a long process of legislative gestation, the reform law passed and became effective in October 2005 under the misleading name “Bankruptcy Abuse Prevention and Consumer Protection Act” or BAPCPA (often referred to as “bap-see-pah”).⁷

It is difficult to overstate what a spectacular failure the U.S. reform of October 2005 has been, especially in light of the subsequent financial and economic crises. Indeed, at least one authoritative commentator has cogently argued that BAPCPA exacerbated if not contributed directly to the subprime foreclosure crisis and the meltdown of the U.S. housing market, which spread to the rest of the world in 2007.⁸ BAPCPA clearly did not solve the supposed problem of “excessive” consumer bankruptcy filings. Within five years after the effective date of the new law, consumer bankruptcy filings returned to pre-2005 levels.⁹ Likewise, the proportion of filings under the immediate-discharge provisions of Chapter 7 and the payment-plan provisions of Chapter 13 have returned to their pre-reform relation of about 70:30.¹⁰ This data all but conclusively disproves

⁶ See Kilborn *supra* note 3, at 109-110.

⁷ *Id.* at 110.

⁸ See DONALD P. MORGAN, BENJAMIN IVERSON & MATTHEW BOTSCH, SEISMIC EFFECTS OF THE BANKRUPTCY REFORM (Federal Reserve Bank of New York Staff Report, Feb. 2009), available at www.ny.frb.org/research/staff_reports/sr358.pdf.

⁹ Official statistics report nearly 1.6 million filings in calendar year 2010 and over 1.4 million in 2011, the vast majority of which were “consumer” filings. See ADMINISTRATIVE OFFICE OF U.S. COURTS, U.S. BANKRUPTCY COURTS—BANKRUPTCY CASES COMMENCED, TERMINATED AND PENDING DURING THE 12-MONTH PERIODS ENDING DECEMBER 31, 2010 AND 2011, available at www.uscourts.gov/uscourts/Statistics/BankruptcyStatistics/BankruptcyFilings/2011/1211_f.pdf.

¹⁰ See ADMINISTRATIVE OFFICE OF U.S. COURTS, 2010 REPORT OF STATISTICS REQUIRED BY THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2005, available at www.uscourts.gov/uscourts/Statistics/

the hypothesis that any significant number of potential “abusers” have self-selected into Chapter 13 payment plans or out of bankruptcy relief altogether for fear of running afoul of the more rigid entry requirements discussed below.

Most troubling, BAPCPA not only failed to *solve* any problems, it *created* a mass of expensive, burdensome, and distracting challenges for debtors, their lawyers, trustees, and the courts. Three key problems relate to (1) required pre-filing credit counseling, (2) the “means test” for ferreting out “abusive” filers, and (3) poorly drafted provisions of law that have come to dominate the precious time and resources of the courts, including the Supreme Court.¹¹

A. Required Pre-Bankruptcy Credit Counseling

Part of the U.S. reform addressed the perception of lawmakers that debtors were choosing bankruptcy too hastily, without proper consideration of alternatives.¹² All available empirical evidence indicated strongly that debtors were in fact being told about alternatives, but the alternatives were clearly insufficient. For at least 30 years, consumer debtors in the United States had been delaying or avoiding bankruptcy by trying to work things out with their creditors, often with assistance from private credit counselors.¹³ This negotiation and counseling had become all but pointless for most debtors by the mid-1990s, however, in light of a spectacular rise in debt levels, stagnating real incomes for all but the wealthiest Americans, and an increasing unwillingness by institutional creditors (primarily credit card banks) to offer consumers the scope and nature of relief that could stave off a bankruptcy filing.¹⁴

Nonetheless, the 2005 reform bill included an additional obligation for any individual seeking relief under any chapter of the Bankruptcy Code: within 180 days before filing a bankruptcy petition, an individual must attend “an individual or group briefing (including a briefing conducted by telephone or on the Internet) that outlined the opportunities for available credit counseling and assisted such individual in performing a related

BankruptcyStatistics/BAPCPA/2010/2010BAPCPA.pdf.

¹¹ See Kilborn *supra* note 3, at 110, 117-18.

¹² *Id.* at 111.

¹³ *Id.* at 84.

¹⁴ For a more detailed discussion of the rise and fall of credit counseling in the United States, see Kilborn, *supra* note 3, at 84-87.

budget analysis.”¹⁵ Not surprisingly, this search for alternatives to bankruptcy has been an almost complete failure. Credit counseling agencies have reported that only about 3% of these pre-bankruptcy debtors might find solutions to their problems through counseling and budgeting alone, without bankruptcy intervention.¹⁶ The largely ceremonial “counseling” today usually consists of a telephone or internet session in which a counseling provider outlines generalized advice, the debtor inputs financial information that inevitably demonstrates that bankruptcy is the only workable solution to financial trouble spiraling out of control, and the counseling agency produces a certificate of completion in exchange for a \$50 fee. This aspect of the reform thus represents little more than a wholesale transfer of wealth from insolvent debtors to the credit counseling industry, while imposing needless delays on debtors seeking bankruptcy relief.

B. The “Means Test”

The heart of the [2005 U.S.] consumer bankruptcy reforms is the so-called “means test,” the explicit aim of which is to prevent debtors from receiving an immediate discharge under Chapter 7 if they have the “means” to pay a statutorily defined dividend to their creditors over a five-year, Chapter 13 payment plan.¹⁷ This “means test” imposes heavy paperwork burdens on debtors and their lawyers, and the system administrators (panel trustees and the U.S. Trustee’s office) have the onerous task of monitoring compliance with the new restrictions by reviewing these financial disclosures in every case.¹⁸

The substantial compliance and monitoring costs for this hunt for “abuse” have not provided significant benefits, and the entire enterprise of means testing has been revealed as a fool’s errand. In each of the five years since the adoption of the reform, only a miniscule percentage of debtors have been discovered to possess sufficient means to make significant payments to their creditors. Even the most hawkish supporters of consumer

¹⁵ 11 U.S.C. § 109(h)(1) (2010).

¹⁶ See, e.g., NATIONAL FOUNDATION FOR CREDIT COUNSELING, MEETING THE MANDATE: CONSUMER COUNSELING AND EDUCATION UNDER THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT (BAPCPA) 12 (2006); INSTITUTE FOR FINANCIAL LITERACY, FIRST DEMOGRAPHIC ANALYSIS OF POST-BAPCPA DEBTORS 4 & n.9 (2006).

¹⁷ See H.R. REP. NO. 109-31, at 2 (2005).

¹⁸ See Kilborn, *supra* note 3, at 119.

bankruptcy reform originally estimated that only about 10% of debtors might be excluded from Chapter 7 by the means test.¹⁹ In fact, as discussed immediately below, the actual figure has been much smaller than that.

The “means test” was incorporated into an existing Code section that barred Chapter 7 relief for debtors in cases of “abuse.”²⁰ Elaborating on the general notion of abuse of the bankruptcy process, this reformulated test specifically analyzes each debtor’s finances in two steps.²¹ If the debtor “passes” either step of the means test, abuse is *not* presumed based on ability to pay, and the case proceeds under the pre-reform law.²² As reported below, the overwhelming majority of debtors have “passed” one or both steps of this test in each of its first five years.

Debtors pass the first step if their “current monthly income” (“CMI”) falls below a defined threshold.²³ The contrived legalese concept of CMI bears little relation to reality or common sense, however, as that term connotes the average of the debtor’s monthly income over the past six months.²⁴ Not surprisingly, most debtors visiting a bankruptcy lawyer have experienced an income disruption (*e.g.*, unemployment, divorce, medical problem, and so on), so their backward-looking income is generally depressed, even if they do indeed possess the “means” to make future payments. This forces the means test to start on the wrong foot immediately. This fictitious CMI figure is then multiplied by twelve to produce an inaccurate assumed annual income, and this annual income is compared with the inflation-adjusted median family income of a household of the same size as the debtor’s in the debtor’s state.²⁵ Debtors with income at or

¹⁹ See, *e.g.*, Todd Zywicki, *Bankrupt Criticisms: The Bankruptcy Bill Deserves to Pass*, NAT’L REV. ONLINE (Mar. 15, 2005), <http://old.nationalreview.com/comment/zywicki200503150744.asp>.

²⁰ 11 U.S.C. § 707(b) (2010).

²¹ See Kilborn, *supra* note 3, at 117.

²² *Id.* at 118.

²³ *Id.* at 117-118.

²⁴ 11 U.S.C. § 101(10).

²⁵ 11 U.S.C. § 707(b)(6)-(7). The applicable median figures are based on census data and consumer price indices and are available on the U.S. Trustee’s website at <http://www.justice.gov/ust/eo/bapcpa/meanstesting.htm>. For example, as of May 2012, the median gross (pre-tax) income for a family of three in Illinois, a relatively average state, is just under \$70,000 per year. U.S. Dep’t of Justice, *Census Bureau Median Family Income By Family Size (Cases Filed On and After May 1, 2012)*, www.justice.gov/ust/eo/bapcpa/20120501/bci_data/median_

below the applicable median are automatically *not* presumed abusive, and they are allowed into Chapter 7.²⁶ As one would expect of people seeking debt relief, consistently around 90% of all debtors filing under Chapter 7 in the years since the implementation of the means test have passed this median-or-below income test.²⁷

The 10% of debtors who must proceed to step two are required to subtract a series of actual or presumed expenses from their contrived above-average “current monthly income” figure to reveal whether significant “disposable income” remains for distribution to creditors. If so, seeking Chapter 7 relief is “presumed abusive,” and such debtors must convert to Chapter 13 payment plans if they want formal bankruptcy relief.²⁸ After deducting standard monthly allowances for food, clothing, housing and transportation, in addition to amounts contractually due to secured and priority creditors in the next five years, abuse is presumed if the remainder exceeds about \$180 per month (that is, an amount that would allow the debtor to pay creditors at least \$11,725 over an imposed five-year plan).²⁹ Unsurprisingly, given the rising expense of living in the United States, only a small fraction of debtors have failed this second step of the means test. In the first five post-reform years, fewer than 10% of the *above-median income* debtors subjected to the second step of the means test have failed this second step, as well.

That is, only about 1% of all Chapter 7 filers have been revealed as potential “abusers” of the quick relief of Chapter 7 liquidation. Recall, however, that this abuse test is based on an artificial retrospective view of debtors’ incomes. One last safety valve allows the U.S. Trustee the discretion to decline to seek a dismissal or conversion to Chapter 13 in light of “special circumstances.”³⁰ In a final ironic twist, the U.S. Trustee has

income_table.htm.

²⁶ See Kilborn, *supra* note 3, at 118.

²⁷ See, e.g., U.S. DEP’T OF JUSTICE, *UNITED STATES TRUSTEE PROGRAM: ANNUAL REPORT OF SIGNIFICANT ACCOMPLISHMENTS, FISCAL YEAR 2010*, 19 (2011), www.justice.gov/ust/eo/public_affairs/annualreport/docs/ar2010.pdf.

²⁸ See Kilborn, *supra* note 3, at 119.

²⁹ 11 U.S.C. § 707(b)(2)(A)(i). The actual dollar figure is indexed for inflation every three years, and the test is actually more complex than described. Debtors with more than \$28,000 but less than \$47,000 in unsecured debt can be denied access if their “disposable” income exceeds about \$120 per month and over a 60-month plan would pay 25% of their unsecured debt (and at least \$11,725).

³⁰ See Kilborn, *supra* note 3, at 122-23.

exercised this discretion in at least half (in recent years, 60-70%) of the presumptively abusive cases in light of the “special circumstance” of debtors’ unemployment.³¹ If there is any truism in consumer bankruptcy, it is that most cases arise from job loss. The notion that identifying unemployment as a “special circumstance” is necessary to prevent dismissal of a Chapter 7 case starkly reveals the utter disregard for reality in the U.S. bankruptcy reform.

Despite the fact that only a fraction of 1% of Chapter 7 filings are found to be “abusive,” debtors in *every* one of the nearly *one million* Chapter 7 cases filed each year must file a detailed description of how the means test applies to them.³² Further, the case trustee must review *every* Chapter 7 case and file a statement explaining whether the debtor “passes” or “fails” the means test. In the cases in which the debtor fails the means test, but the U.S. Trustee declines to file a motion to dismiss based on “special circumstances,” the U.S. Trustee must explain in a written statement why a dismissal should not be imposed.³³ One might wonder why Congress imposed the time- and resource-intensive review of the complex means test on *every* case when fewer than 10% of cases were ever expected to “fail.” Unfortunately, Congress has not responded and is not expected to respond to the entreaties of overburdened debtors, lawyers, and trustees who face a pointless and unproductive paperwork review burden to weed out what has proven to be less than 1% of possibly abusive filings.

C. Poorly Drafted Provisions Overwhelm the Courts

Compounding the compliance and monitoring costs in the means test, lawyers and the courts have struggled with a massive load of new disputes about poorly drafted provisions of the reform law. Indeed, though the U.S. Supreme Court accepts only a small fraction of all requests for *certiorari* review—generally 100 or fewer cases per year—it has felt obliged to dedicate several precious slots on its docket in recent years to clean up the statutory mess created by BAPCPA. Three disputes illustrate the problem.

³¹ See U.S. Dep’t of Justice, *supra* note 15, at 18.

³² 11 U.S.C. §§ 704(b)(1), 707(b)(1), (2)(C) (2010).

³³ *Id.*

1. Debt Relief Agencies and Free Speech

First, the reform law required bankruptcy lawyers to refer to themselves as “debt relief agencies” and to make required announcements in any advertising that they “help people file for bankruptcy relief under the Bankruptcy Code.”³⁴ One would have thought that this would be entirely clear to anyone coming to a bankruptcy attorney’s office, but the more troublesome aspect of this reform was a restriction on the types of advice that bankruptcy lawyers could offer clients. Debt relief agencies are forbidden to “advise [a bankruptcy client] to incur more debt in contemplation of [the bankruptcy case] or to pay an attorney or bankruptcy petition preparer fee or charge for services performed as part of preparing for or representing a debtor in a [bankruptcy] case.”³⁵

After a law firm challenged these new rules as a violation of the First Amendment free speech rights of lawyers and an undue interference in the client-lawyer relationship, the Supreme Court ultimately took the case to clarify the limited application of this new restriction. In a unanimous decision, the Court held that the superfluous and stigmatizing disclosure requirements were within Congress’s power, but the restriction on advice could be applied only to prevent advice that would be “abusive per se,” such as suggesting that a client take on debt for no other purpose than to take advantage of the discharge (as opposed to an independent, legitimate purpose, such as buying a more reliable car or refinancing a home mortgage).³⁶

All of this was entirely clear before BAPCPA, and any lawyer could and likely would have been sanctioned for offering such “abusive per se” advice in any event. These provisions have imposed significant costs on lawyers in needlessly redrafting their advertising and client communications. Moreover, these rules have caused a dead-weight loss of thousands of dollars and hours by lawyers and courts in litigating over these silly and pointless new rules.

³⁴ 11 U.S.C. § 528.

³⁵ 11 U.S.C. § 526(a)(4).

³⁶ *Milavetz, Gallop & Milavetz, P.A. v. United States*, 130 S. Ct. 1324, 1336 (2010).

2. Projected Disposable Income: Retrospective or Prospective

Second, as discussed above, BAPCPA defines “disposable income” in a contrived, backward-looking way for testing Chapter 7 eligibility. It uses a similar term—“projected disposable income”—for testing the income to be applied to future payments in a Chapter 13 payment plan, however. Courts struggled to apply these two uses of the same statutory words in consistent ways, but many resisted using an artificial view of *past* income to control an evaluation of the debtor’s expected *future* income, especially when the facts clearly suggested a disconnect between the debtor’s income during these two time periods.³⁷

After several appellate courts interpreted these phrases in contradictory ways, the Supreme Court stepped in to fix the drafting mess that Congress had created. It held that “projected” must be interpreted in a way that allowed the court discretion to apply a “forward-looking test” and deviate from the “disposable income” calculation based on past income.³⁸ If the debtor’s income would *clearly* be more or less in the future than it had been in the recent past, then courts could use that *future* projection in calculating the required payments under a Chapter 13 plan, despite the wording of the statute.³⁹ This decision was not unanimous.⁴⁰ As he often does, Justice Scalia favored a “mechanical” test that applied the words that Congress chose in drafting the statute, no matter how absurd the result might be.⁴¹ Once again, a careless drafting error, fueled by conservative politics, wreaked havoc in the courts, wasted countless resources, and damaged the lives of the poor debtors caught in the middle.

3. Deducting the Non-Expense of Vehicle Ownership

Finally, perhaps the most sophistic dispute was the one most recently resolved by the Supreme Court. BAPCPA defined the debtor’s expense deductions for arriving at “disposable income” in terms of the standards used by the IRS (the federal tax service) in negotiating compromise arrangements for tax arrears.⁴² One of these expenses is an “ownership” cost for a vehicle. The

³⁷ *Hamilton v. Lanning*, 130 U.S. 2464, 2467 (2010).

³⁸ *Id.* at 2471.

³⁹ *Id.*

⁴⁰ *Id.* at 2482.

⁴¹ *Id.* at 2471.

⁴² 11 U.S.C. § 707(b)(2)(A)(ii).

IRS allows such an expense deduction, however, only if the debtor actually bears ownership costs; that is, if the debtor owns the car free-and-clear of any loan or lease expenses. No deduction is allowed for “ownership,” separate from a deduction for “operating” expenses, such as gas and maintenance.

But BAPCPA did not clearly adopt the IRS *application* of these expense guidelines; it adopted the “applicable monthly expense amounts specified” in the IRS standards. Debtors’ lawyers argued, and some courts agreed, that this meant that any debtor who owned a vehicle could deduct the “amount specified” in the IRS guideline (that is, about \$500 per car), whether or not the debtor owed any debt related to the car and would incur an *actual* ownership expense.⁴³ Other courts held that the specified deduction was “applicable” only if the debtor actually *had* such an ongoing expense, so debtors who actually anticipated no expenditure for paying back a loan or lease obligation to own a car could take no deduction for this non-expense. In a ruling that came as little surprise to anyone, the Supreme Court adopted the latter position.⁴⁴ This time- and resource-consuming quibbling over the meaning of the word “applicable” arose solely due to the quagmire of poor drafting in BAPCPA, and similar problems continue to plague the ongoing application of the reform law.⁴⁵

The losses from this ill-conceived and poorly implemented reform continue to mount with no end in sight. From the perspective of system efficiency and effective social policy, BAPCPA represents an enormous step backward, a regulatory response that has made treating the casualties of financial market risks all the more inefficient, expensive, and cumbersome. Indeed, as usual, the most financially distressed and socially excluded suffer the most, as one of the greatest tragedies of the U.S. reform

⁴³ See, e.g., *Tate v. Bolen*, 571 F.3d 423, 428 (5th Cir. 2009); *Ross–Tousey v. Neary*, 549 F.3d 1148, 1157 (7th Cir. 2008).

⁴⁴ *Ransom v. FIA Card Services, N.A.*, 131 S. Ct. 716, 723–25 (2011). Once again, Justice Scalia dissented, preferring a “plain meaning” approach to interpreting the word “applicable” as used by Congress in the law.

⁴⁵ For example, a problem similar to that in *Ransom* arises with respect to vehicle ownership deductions for vehicles on which the debtor *does* bear an ownership expense *at the time of filing*, but which the debtor intends to avoid in the future by surrendering the vehicle to the secured creditor. Here again, some courts allow a deduction for an expense that the debtor has at the time of filing but clearly will not incur going forward. Perhaps the resolution of the *Ransom* case in the Supreme Court has implicitly resolved this related dispute, as well, though more likely another round of divided appellate decisions and more uncertainty will ensue.

was a marked rise in the cost of retaining an attorney to guide debtors through this now even more complex thicket of rules and traps. Many debtors who need and deserve relief are now priced out of this “market.” These problems will plague the U.S. system for years to come.

II. CLOSING THE DOORS TO THE DUTCH *WSNP* IN 2008

Though not nearly as problematic as the U.S. debacle of BAPCPA, the reform of the Dutch consumer insolvency regime in 2008 also continued chasing the dual chimeras of perceived “abuse” and a hope that debtors and creditors could simply work things out on their own outside of court. This reform, however, seems to have begun to slay a real dragon by avoiding wasteful, superfluous administrative complexity. These three concepts reflect the three primary goals of the first major reform of the Dutch Law on Debt Adjustment for Natural Persons (*Wet schuldsanering natuurlijke personen*, or *Wsnp*), effective January 1, 2008.

A. *Standardization and Reducing Administrative Complexity*

On the positive side, the Dutch reform pursued one clearly laudable end: to simplify the process and reduce the burden of excessive administrative complexity. Practice had shown that some of the central procedures of the new system were largely or entirely superfluous, especially those that allowed for broader discretion in crafting debt adjustment plans. Very little variation had appeared in the simple problem shared by debtors seeking a solution for a mismatch between limited incomes and burgeoning debts. The reform law thus abandoned the original approach of a flexible *saneringsplan* that relied on judicial discretion to craft “fair and reasonable” adjustment plans. Instead, it essentially codified a unitary model of income and expense allowances that judges and other insolvency professionals had developed in practice.⁴⁶ Another prime example of relegating time-consuming and expensive procedures to virtual desuetude is the former requirement of a formal hearing for verifying creditors’ claims.

⁴⁶ See Raad voor Rechtsbijstand’s Hertogenbosch, Bureau Wsnp, *De Wsnp per 1 januari 2008: Wat wijzigt er?* (October 2007), available at www.mvz.nl/docs_mvz/watverandert_wsnp.pdf; Kamerstukken II, 2004/05, 29 942, nr. 3, pp 6-7, 38 (discussing new article 349a); *Faillissementswet* arts. 295(3), 349a.

Because such hearings were actually held only in the minority of cases where a distribution to creditors was expected, the reform formally ratified this practice. It is difficult to gauge how these aspects of the reform have performed, in part because they represent little more than a legislative ratification of practice under the original law. In any event, these formalized simplifications must have at least maintained if not enhanced the system's efficiency.

B. Restricting Entry To Those Who Are "Ready"

The bigger story in the Dutch reform is at best a mixed success. The goal of avoiding "abuse" was questionable, and the reform's impact here is harder to interpret. To make the system more efficient and effective for those admitted, reformers sought to reduce the number of unstable cases allowed into the system and, consequently, the number of unsuccessful adjustment plans ultimately converted to liquidation bankruptcy. To achieve this goal, the law was reformulated to encourage judges to exercise their discretion to bar the door to debtors who seemed "not ready" to comply with their obligations during the multi-year debt adjustment process. Homeless debtors and those with "psycho-social problems" like drug addiction, for example, were targeted for diversion from the debt adjustment system until their financial situation had stabilized or their non-financial problems are "under control."⁴⁷

The goal of reducing admitted cases seems to have been achieved with a vengeance, though as in the U.S., only temporarily. In 2008 and 2009, filings plummeted 40% from the pre-reform level, from over 18,500 in the several years before 2008 to about 11,000 in 2008 and 12,500 in 2009.⁴⁸ Already by 2010, though, filings had climbed nearly back to their pre-reform level.⁴⁹ Moreover, the rate of admission of filed applications has changed relatively little (about 85% are admitted).⁵⁰ The lower filing figures immediately following the 2008 reform might

⁴⁷ *Faillissementswet* art. 288.

⁴⁸ See Marijke von Bergh et al., Raad voor Rechtsbijstand, *Monitor Wsnp: Zesde meting 7-8* (2010), available at www.wsnprvr.org/pdf/Monitor%20Wsnp%206e%20meting.pdf.

⁴⁹ See Lia Combrink-Kuiters & Vinodh Lalta, Raad voor Rechtsbijstand, *Monitor Wsnp: Zevende meting over het jaar 2010*, at 13 (2011), available at www.wsnprvr.org/pdf/Monitor%20Wsnp%202010_TP.pdf.

⁵⁰ See *id.* at 16 & tbl. 3.2.

indicate that more debtors avoided the system temporarily for fear that their applications would be rejected. If these people would have been, indeed, “not ready” to withstand the rigors of a multi-year payment plan on a strictly controlled budget, perhaps it is better that the system prevent their entry until they are prepared. It is hard to tell, however, exactly why such a sharp drop-off in filings ensued immediately following the effective date of the reform. In any event, as in the U.S., a reform effort designed to depress filing levels has proven to be a decisive failure.

C. Increasing Voluntary Workouts

One potentially brighter explanation for the lower filing figures may lie in the third goal of the reform, diverting more debtors to a voluntary workout with creditors outside the formal system. The constant pursuit of this chimera seems to have been met with success recently, but most likely *not* as a result of the *Wsnp* reform. The Netherlands has a long and impressive history of debt negotiation supported by a well-developed credit counseling infrastructure. The historical success of that extra-judicial system had fallen to disappointing lows after the adoption of the formal *Wsnp*. By 2004, creditors accepted only 9% of proposed out-of-court workout arrangements.⁵¹ The struggle to raise this success rate proceeded on two fronts.

The first front was located within the reform effort of the formal debt adjustment system. The 2008 reform attempted to strengthen the debtor’s hand in negotiating extra-judicial workouts by adding a provision to allow the debtor to request that the court force a creditor to accept the debtor’s proposed out-of-court plan “if the creditor could not reasonably have refused” to accept the debtor’s compromise plan, “in light of the imbalance between the [creditor’s] interest . . . and the interests of the debtor and of the other creditors who will be injured by the rejection.”⁵²

Not surprisingly, this attempt to encourage debtors to seek leverage from the courts has been an all but complete failure, since creditors reject such agreements primarily because debtors are simply unable to make an offer more convincing and attractive than what the *Wsnp* formally extracts from debtors

⁵¹ For a discussion of the development of the unique Dutch credit counseling system and its struggles, see Kilborn, *supra* note 3, at 87-91, 94-97.

⁵² *Faillissementswet* art. 287a.

with court oversight.⁵³ Such a forced compromise has been requested in only about 2000 cases in the first three years of its availability, in contrast to the about 30,000 formal *Wsnp* cases opened during this period.⁵⁴ Indeed, of these 2000 requests, about 40% were withdrawn without a decision from the court, and courts granted only about one-third.⁵⁵

The more successful effort was centered within the extra-judicial counseling and negotiation system. In tandem with the reform of the *Wsnp*, the national coordinating association for credit counseling (*Nederlandse Vereniging voor Volkskrediet* or NVVK) reevaluated its own approach to debt negotiation in two key ways. First, rather than treating every case as a suitable candidate for an out-of-court solution, counseling agencies implemented a sort of triage system.⁵⁶ History had shown that the most financially overwhelmed debtors were clearly destined for the formal debt adjustment system, so counselors stopped resisting that inevitable result. Such debtors were simply prepared for and routed directly to the formal *Wsnp* system, with a certificate attesting that any attempt at a voluntary arrangement would be pointless. With fewer resources diverted to such hopeless cases, counselors could concentrate their efforts and enhance success rates in cases where an extra-judicial workout was a realistic objective. Second, and even more important, the NVVK had observed that one-third of unsuccessful negotiations failed as a result of rejection by one major creditor: the collections bureau for fines and penalties (*Centraal Justitieel Incassobureau*, generally called by its acronym, CJIB).⁵⁷ The NVVK concentrated on convincing this one key creditor to support more out-of-court arrangements, a tactic that seems to have paid off.

The rate of successful NVVK workout negotiations climbed to 22% in 2007, 34% in 2008, and 38% in 2010.⁵⁸ The

⁵³ See Nick Huls, Nadja Jungmann & Bert Niemeijer, *Can Voluntary Debt Settlement and Consumer Bankruptcy Coexist? The Development of Dutch Insolvency Law*, in CONSUMER BANKRUPTCY IN GLOBAL PERSPECTIVE 303 (2003).

⁵⁴ See Combrink-Kuiters & Lalta, *supra* note 49, at 42 & tbl. 5.1.

⁵⁵ See *id.*

⁵⁶ See Nederlandse Vereniging voor Volkskrediet, *Jaarverslag 2010: Schulden, het kan iedereen overkomen* 23 (2011), available at www.nvbk.eu/images/pdfs/NVVK%20jaarverslag%202010.pdf; see generally www.nvbk.eu/ (providing statistics and other information on counseling process).

⁵⁷ *Id.*

⁵⁸ *Id.*

myriad of factors at play in these complex systems makes it impossible to conclude with confidence that one or another of the reform efforts was the silver bullet, but the great weight of available evidence suggests that the NVVK's efforts clearly predominated over the legislative *Wsnp* reform effort in achieving these positive results.

The Dutch reform illustrates a combination of the right and wrong ways to enhance system performance in a socially responsible way. Continuing to chase chimerical notions of "abuse" and creditor cooperation are likely to produce limited success at best, and, at worst, it will undermine the delivery of relief to those who need it. The striking but short-lived post-reform decline of filings in the Dutch system seems likely to be largely a manifestation of this latter, unfavorable result. On the other hand, the Dutch reform is to be admired for engaging real problems and finally slaying the dragon of needlessly formalistic and wasteful administrative complexities and overcoming creditor resistance through direct, targeted negotiation with key creditor interests. This reform has moved the Dutch system in an admirably more effective results-oriented direction.

III. TRANSITION TO MOSTLY SUCCESSFUL: DENMARK (2005) AND SWEDEN (2007)

Two prominent Scandinavian reforms mark the transition toward making real progress without taking significant steps backward. The very first consumer debt adjustment law in Europe has long resisted meaningful reform, and the 2005 revision of the Danish law left in place a significant problem that leaves many debtors to languish in social exclusion, though it did manage to improve the lives of the few debtors this system admits. The Swedish law underwent a more thoroughgoing and effective reform in 2007, finally sloughing off old shibboleths and abandoning a long-standing and widespread quest for one particularly elusive chimera.

A. Local Legal Culture Battles, Humanizing Unified Budgets in Denmark

The persistent problem of "local legal culture" motivated the Danish reform of 2005. That is, substantial regional variation was observed in the ratio of applications to admissions and confirmed debt adjustment plans, as well as in the income and

expense allowances used by courts in arriving at debt adjustment plans.⁵⁹ The reform addressed both areas, though only the latter seems to have enhanced system performance and social responsibility.⁶⁰

Because the Danish law broke new ground in allowing consumers relief from their debts, this system and the others in Scandinavia that it inspired have resisted extending relief beyond a relatively narrow band of particularly needy applicants. Fear of abuse of this extraordinary relief persists in Scandinavia more so than in most other regions, and a complex and bifurcated admissions test prevents most applicants from accessing the system. First, debtors must exhibit “qualified insolvency,” which implies a complete impossibility, free from virtually any doubt, that debtors might right their own financial ships in the foreseeable future by reducing their living standards and applying their best efforts to paying off debt.⁶¹ Second, the court has to be convinced that offering relief in any particular case is appropriate in light of a series of factors, such as the debtor’s efforts to manage debt problems and the composition of the debt load (preferably relatively few fines, penalties, and “irresponsible” debts, such as debts for luxury consumption).⁶²

The variety of inquiries implicit in these complex tests, especially the court’s evaluation of the debtor’s lifestyle and opportunities for belt tightening, have produced very significant regional variations among Danish courts. In 2002, for example, while the court in Odense admitted 66% of its 161 debt adjustment applications, the court in Roskilde admitted only 39% of 139 applicants, and the court in Copenhagen admitted a mere 25% of 828 applications.⁶³ Even beyond the entry point, courts took markedly different approaches to confirming debt adjustment plans for admitted applicants. While the court in Århus closed 41% of its 244 cases with a confirmed plan, the courts in Ålborg and Randers confirmed plans in only 19% and 15%, respectively, of the 136 cases closed by each of those two courts, and as in most years, the Copenhagen court had a miserly

⁵⁹ See Jason J. Kilborn, *Twenty-Five Years of Consumer Bankruptcy in Continental Europe: Internalizing Negative Externalities and Humanizing Justice in Denmark*, 18 INT’L. INSOL. REV. 155, 174 (2009) (giving detailed discussion of the history and operation of the Danish system).

⁶⁰ *Id.* at 172.

⁶¹ *Id.* at 165-67.

⁶² *Id.* at 168.

⁶³ *Id.* at 175 (compiling data from official sources).

success rate of only 13% of its 8,689 closed cases.⁶⁴

These vast admissions and confirmation differentials were left largely unaddressed by the reform. The reform commission all but brushed aside criticisms of non-uniformity, noting ironically that it had no empirical data on the characteristics of admitted or rejected debtors, so it could not conclude that regional variations were *not* based on meaningful, objective variations among cases. It explicitly refused to undertake such studies itself because “the need for the changes in the current law . . . to a significant degree are independent of quantitative considerations.”⁶⁵

The reform law did take one small step away from the historical obsession with abuse, however. The second step of the admissions test originally operated on a presumption that debtors should *not* be admitted into the system unless the court was convinced that the totality of the circumstances militated *in favor* of admission. The reform reversed the presumption, which is now in favor of admission unless consideration of a slightly reformulated list of factors “suggests decisively against” relief.⁶⁶ Unfortunately, this has proven essentially to be a difference without a distinction.

Striking regional variations persist, and while filings are up slightly, overall admission rates in the ensuing years have actually fallen. After a spike in admissions following the 2005 reform, acceptance rates fell back to their former low levels and for many years have remained fairly steady at only about 40-45% (2,000-2,250 of about 5,000 applications annually).⁶⁷ In light of the worldwide recession, in particular, the combination of rising filings and falling admissions suggests a system failing to address a rising incidence of pain; that is, a reform not performing well in reducing growing financial and social exclusion.

⁶⁴ *Id.* at 175 and n.145. The disparities are even greater in smaller districts, though the “small n” problem makes these data less compelling. For example, the court in Sæby admitted 86% of 28 applications, while the court in Ringsted admitted only 15% of 47 applications, and while the court in Nykøbing Mors confirmed a plan in 80% of 15 total closed cases, the courts in Skanderborg and Esbjerg confirmed plans in only about 12% of their 51 and 93 closed cases.

⁶⁵ Konkursrådets Betænkning nr. 1449/2004, at 46.

⁶⁶ *Konkurslov* § 197 (“*taler afgørende imod*”).

⁶⁷ *See*

<http://www.domstol.dk/om/talogfakta/statistik/Pages/skiftesager.aspx>
(author’s calculations based on data from the court administration’s statistics for newly undertaken debt adjustment cases (*insolvensskifter*)).

Turning the corner, however, there is a bit of good news in Denmark on regional variations in treatment of debtors within the system. The Danish law in its original formulation relegated debtors' budgets and expense allowances to the discretionary judgment of courts as to what a "modest" lifestyle entailed. The wide variations in this standard prompted some counselors to suggest that their pre-bankruptcy clients move house from districts with especially miserly judges to nearby areas where relief was available on more livable terms. The 2005 reform achieved greater success in tackling this problem, charging the Justice Ministry with establishing uniform basic budgetary allowances. An unintended consequence of this unification effort was that the Justice Ministry took a substantially more humane approach to debtor support. On the expense side, the ministry's basic budget allowance exceeded the upper range then applied by the courts in most debt adjustment cases by nearly 20%.⁶⁸ On the income side, more types of income were reserved to debtors outright, such as transfer payments for children.⁶⁹ More livable budgets are surely a positive social policy development in many quantifiable and unquantifiable ways.

B. Centralization, Simplification, and Expansion in Sweden

The Swedish reform of 2007 achieved its stated goals of making the debt adjustment process simpler, more efficient, and thus more effective. It reduced a cumbersome three-step process to one step, and it concentrated authority in the actor most suited to administer the process intelligently, sensitively, efficiently, and effectively.⁷⁰ From a quantitative perspective, this overhaul seems to have revved up performance in a very impressive way.

In its original form, the Swedish debt adjustment law required debtors to traverse three distinct stages with different structures of authority.⁷¹ Step one required private negotiation with creditors, supported by budget counselors, much like in the Dutch system discussed above.⁷² Following the inevitable failure

⁶⁸ See Kilborn, *supra* note 59, at 178-79.

⁶⁹ *Id.* at 160 n.22, 172, 174, 176-78.

⁷⁰ See Jason Kilborn, *Out with the New, In with the Old: As Sweden Aggressively Streamlines Its Consumer Bankruptcy System, Have U.S. Reformers Fallen Off the Learning Curve?*, 80 AM. BANKR. L.J. 435 (2007) (providing overview of the history and reform of the Swedish system).

⁷¹ See *id.* at 439.

⁷² See *id.* at 440.

of this search for creditor cooperation and a private solution, debtors would apply for formal relief in step two to the state Enforcement Agency (*Kronofogdemyndigheten* or KFM), who made admissions decisions on criteria quite similar to those described above in the Danish system.⁷³ For those debtors admitted, the KFM was also responsible for drafting the debt adjustment plan for submission to a creditor vote.⁷⁴ Creditors usually rejected this plan, so, in a third step, the Enforcement Agency would engage the courts for a judicial review and an all but inevitable imposition of the plan on creditors.⁷⁵

The 2007 reform slayed two major dragons. First, Sweden became the first state to scrap the required first step of seeking consensual compromise from creditors. Years of criticism of long delays and a fruitless waste of labor finally convinced legislators of the folly of chasing the chimera of cooperation from creditors.⁷⁶ Indeed, even many creditor representatives considered the required step of negotiation “nearly meaningless.”⁷⁷ As the Dutch NVVK had discovered, removing the distraction of negotiation destined for failure would allow already razor-thin Swedish counseling budgets to be concentrated on cases that were good candidates for consensual workouts.⁷⁸

Second, like the other positive aspect of the Dutch reform, the Swedish reform eliminated the hyper-technical requirement of court *imprimatur* on debt adjustment plans. The courts also had complained of wasted time and resources in conscripting them to review cases where creditors objected to the KFM’s proposed plan on such abstract bases as “oppos[ition] to debt adjustment in principle.”⁷⁹ Since the courts upheld the KFM’s proposed plan in the overwhelming majority of cases, court involvement in this process had proven to be little more than a “pure formality.”⁸⁰

The removal of the superfluous court-review process has made the system undeniably more efficient, and there has been no obvious increase in creditor complaints of administrative caprice in the treatment of claims. In the end, debtors’ limited incomes and payment ability constrain the options available to any system

⁷³ *See id.*

⁷⁴ *See id.*

⁷⁵ *See id.*

⁷⁶ *See id.* at 458.

⁷⁷ *See id.*

⁷⁸ *See id.* at 459.

⁷⁹ *See id.* at 460.

⁸⁰ *See id.* at 460-61.

administrator—be it a court or an agency. As the Dutch also acknowledged in their 2008 reform, the role of discretion and the importance of the decision-maker here is limited at best.⁸¹

Having jettisoned the unproductive first and third stages of the process, the newly lubricated Swedish debt adjustment system has been performing at nearly twice its pre-reform level. Filings nearly doubled in 2007 and remained at about that same level in 2008 and 2009 before spiking 20% in 2010 to nearly 8,000.⁸² Moreover, though the Danish-style restrictive entry criteria were left largely unchanged, the percentage of applicants admitted into the Swedish system and offered relief has risen slightly from only about 50% up to and including 2007 to nearly 70% in 2010.⁸³ The Swedish reform of 2007 is among the finest examples of a performance-enhancing re-tooling that has really begun to make larger, lasting gains in the battle against administrative inefficiency as well as social exclusion and financial distress.

IV. OPENING THE FLOODGATES IN GERMANY IN 2002

Though a decade has passed since Germany last reformed its consumer insolvency law, the scope and effect of that reform were so impressive as to merit a brief mention among the real dragon-slayers. Before the December 2001 reform (effective in 2002) of the consumer discharge provisions of the German *Insolvenzordnung*, the overwhelming majority of consumer insolvency cases were dismissed for “lack of estate” (*mangels Masse*⁸⁴) to cover administrative costs.⁸⁵ Not surprisingly, individuals struggling to pay their creditors were unable to scrape together the quite substantial sum required to cover expected costs for official publications, notices to creditors, and administration of the multi-year payment plan.⁸⁶ Concern had also arisen regarding the ability of debtors to remain confined to a

⁸¹ See *id.* at 469-70.

⁸² Kronofogden, *Ärendestatistik: Skuldsaneringsärenden*, available at www.kronofogden.se/20125.html (comparing filings and other statistics from 2007 forward).

⁸³ *Id.*

⁸⁴ *Insolvenzordnung* § 26.

⁸⁵ See Jason Kilborn, *The Innovative German Approach to Consumer Debt Relief: Revolutionary Changes in German Law, and Surprising Lessons for the United States*, 24 NW. J. INT’L L. & BUS. 257, 278-79 (2004).

⁸⁶ See *id.* at 265.

subsistence-level budget for the original seven-year adjustment plan period, especially since the amounts allocated to debtors had not been increased in several years despite rising inflation.⁸⁷

The German legislature's response to these two problems enhanced the performance of this system dramatically, though one's evaluation depends, of course, on one's perspective. As to the problem of financing the costs of administration, the ironic solution was to add another non-dischargeable debt to the debtor's balance sheet. Under the so-called "forbearance model" (*Stundungsmodell*), case opening and administration fees can now be deferred until after the debtor's completion of the multi-year rehabilitation plan, and the debt for these fees is not subject to discharge.⁸⁸

On the one hand, this reform resulted in an explosion of new filings, pushing the system to sustained performance levels that exceed most other similar systems. The mere hope for an impending reform fueled a 23% rise in applications in 2001, and in the first post-reform year, filings tripled to about 45,000 petitions.⁸⁹ Since then, filings by individuals have risen steadily to over 125,000 per year in every year after 2006, a rate of more than 1.5 filings per German resident (among the three highest filing rates in Europe, along with France and England & Wales).⁹⁰ For indigent debtors seeking relief, as well as for a system hoping to eliminate widespread suffering while enhancing debtors' productive energies, this is a spectacular improvement.

In light of the fact that many of these debtors are ultimately unable to repay the delayed filing fees and administration costs, however, these expenses have weighed more and more heavily on the judiciary budgets of the German states (*Länder*).⁹¹ From this perspective, the German system still faces significant performance challenges. Recent reform proposals would require low-income debtors to defray these costs at least

⁸⁷ See *id.* at 282-83.

⁸⁸ *InsO* §§ 4a-4d, 26(1), 298, available at <http://dejure.org/gesetze/InsO>.

⁸⁹ See Kilborn, *supra* note 70, at 287.

⁹⁰ Historical filing data on file with author. See also <https://www.destatis.de/DE/ZahlenFakten/GesamtwirtschaftUmwelt/UnternehmenHandwerk/Insolvenzen/Insolvenzen.html> (providing current filing data).

⁹¹ Sabine Leutheusser-Schnarrenberger, Progress of Insolvency Law Reform, Welcoming Speech at the Eighth German Insolvenztage, available at http://www.bmj.de/SharedDocs/Reden/DE/2011/20110407_Achter_Insolvenztage.html?nn=1356288 (last visited 10 Oct. 2012) (in German, Fortschritte der Insolvenztage-Reform).

mildly during the course of their cases—approximately €20 to €25 per month.⁹²

With respect to the problem of extended rehabilitation periods on depressed incomes, German legislators sensitively improved conditions for debtors by reducing the so-called “good behavior period” (the duration of the debt adjustment plan) from seven to six years and by reforming the general income exemption laws to increase the budgets for most debtors by nearly 50%, indexed bi-annually to keep pace with inflation.⁹³ A shorter rehabilitation period on more livable income clearly represents a performance enhancement from the perspective of debtors and those who hope more debtors will make their way successfully through this arduous process.

As a result of the heightened income protections, an estimated 80% of all cases in Germany today produce no dividend to creditors at all.⁹⁴ If 80% of cases offer no payments to creditors, one might legitimately question the wisdom of expending substantial state revenue to administer this system of six-year “payment” plans if no payments are expected. The latest reform discussions from the Federal Justice Ministry suggest that an even more social policy-oriented proposal may emerge to halve the “good behavior period” to three years,⁹⁵ though even with this further reform, it remains an open question whether the German system is performing well if the great bulk of cases impose an extended period of pain on debtors and an uncompensated administrative burden on the *Länder* with no obvious corresponding benefit (*e.g.*, in terms of payment for creditors). One could deliver relief to debtors in a much more efficient and humane manner if relief and rejuvenation of debtors is the primary system objective.

V. MORE RELIEF, LESS ADMINISTRATIVE BURDEN IN FRANCE, 1999, 2004, 2010

Over its 20-year lifespan, the French consumer insolvency

⁹² See generally *Skuldsanering 2012*, BUNDESMINISTERIUM DER JUSTIZ http://www.bmj.de/DE/Recht/Rechtspflege/Insolvenzrecht/_node.html (last visited Oct. 10, 2012) (providing the latest statements and documents on insolvency law from the German Justice Ministry).

⁹³ See Kilborn, *supra* note 71, at 267-68, 285-86.

⁹⁴ See Kilborn, *supra* note 56, at 293.

⁹⁵ See *supra* note 76.

system has undergone a gradual and impressive evolution toward offering broader and more effective relief to more debtors with less administrative distraction. This is a unique success story, the latest chapters of which are just now being written. This final section will briefly sketch the two-decade progression of reforms in France and the general contours of its spectacular performance shifts over the past few years in particular.⁹⁶

The process of treating what is officially called in France “overindebtedness of individuals” (*surendettement des particuliers*) is commenced with the filing of a petition with a regional “commission on individual overindebtedness,” administered principally under the auspices of the Banque de France.⁹⁷ Because this system arose in the earliest days of Europe’s struggles with consumer debt, it essentially combines what are often two separate mechanisms in other countries: debt counseling and insolvency treatment.

In pursuit of the first, primary goal of the system, the regional commissions offer guidance to debtors in drawing up debt adjustment plans involving only minor concessions from creditors (*e.g.*, reductions of accruing interest, extensions of repayment periods).⁹⁸ In light of the mild modifications that many debtors require, and buttressed by the commissions’ power to “recommend” that a court *impose* these mild concessions on creditors who refuse to agree to the commission’s compromise plan, most situations of financial distress in France are (and always have been) addressed in this earliest and least intrusive stage of the process.⁹⁹ That being said, the first performance indicator here suggests a significant shift: whereas roughly 70% of cases were disposed of with mild consensual workouts from the mid-1990s to 2000, that rate had fallen to just over half by 2008 and 2009.¹⁰⁰

⁹⁶ See Jason Kilborn, *La Responsabilisation de l’Economie: What the United States Can Learn From the New French Law on Consumer Overindebtedness*, 26 MICH. J. INT’L L. 619 (2005) (giving a detailed discussion of the development and operation of the various personal insolvency options in France).

⁹⁷ See *id.* at 637-38.

⁹⁸ See *id.* at 647.

⁹⁹ See *id.* at 650.

¹⁰⁰ See generally *Statistiques mensuelles du surendettement*, BANQUE DE FRANCE, www.banque-france.fr/la-banque-de-france/missions/protection-du-consommateur/surendettement/statistiques-mensuelles-du-surendettement.html (last visited Oct. 2012). The comparative figures discussed here are drawn from the author’s own collection of years of these

One reason for the drop-off is that more effective alternatives to consensual workouts became available in 1999 and 2004.¹⁰¹ Until 1999, the law did not allow either the commissions or the courts to impose a general discharge of unpaid debt.¹⁰² Predictably, a “revolving door” phenomenon developed, with the commissions recommending temporary interest reductions and payment extensions, and debtors returning for more relief when these temporary, limited measures proved insufficient to overcome stubborn difficulties with debt service.¹⁰³

The first major reform of this system introduced a compelled discharge as a form of relief. Beginning in 1999, the commissions could recommend the “extraordinary” measure of a global deferral of all debts for three years (in 2004, reduced to two years).¹⁰⁴ After this period, if the commission’s repeat evaluation revealed that the debtor was still unable to resolve a situation of financial distress using the traditional “ordinary” measures of payment extensions, etc., the commission could recommend that the court impose a partial or total discharge of the unmanageable debt burden.¹⁰⁵

When later surveys revealed that more than a quarter of all debtors had no ability to repay any of their debts, yet few debtors were receiving “extraordinary” discharge relief, the French legislature offered an even more aggressive option. Beginning in 2004, the commissions could recommend a liquidation of non-exempt assets and an *immediate* discharge for debtors in an “irremediably compromised” financial situation through a new “procedure of personal recovery” (*procédure de rétablissement personnel* or PRP).¹⁰⁶ In both process and result, the PRP resembles quite closely a U.S. Chapter 7 consumer bankruptcy proceeding, offering a full and immediate discharge after liquidation of any valuable non-exempt assets (which are generally non-existent), with no rehabilitation plan of any kind.¹⁰⁷

In the past several years, the commissions appear to have comfortably oriented themselves among the variety of relief options, and they seem to be deploying those options aggressively

announcements, no longer available publicly).

¹⁰¹ See Kilborn, *supra* note 96, at 648-50.

¹⁰² See *id.*

¹⁰³ See *id.*

¹⁰⁴ See *id.* at 650.

¹⁰⁵ See *id.* at 650-51.

¹⁰⁶ See *id.* at 654-60.

¹⁰⁷ See *id.* at 656.

to route cases in a way that achieves an optimal balance of relief and administrative efficiency. The commissions have accomplished this by diverting a steadily growing percentage of cases to an immediate PRP discharge, from about 12% of all administered cases in 2004 and 2005 to about 20% in 2007 and 2008, and over 30% in 2009 and after.¹⁰⁸ Before November 1, 2010, the remaining cases had to be forwarded to a court for an all but automatic judicial imposition of the commission's recommended adjustment plan.¹⁰⁹ Approximately two-thirds of these recommendations call for "extraordinary" measures of two-year global debt enforcement moratoria, with about one-third recommending simple "ordinary" measures such as payment extensions and reduced interest.¹¹⁰

With record-breaking filing figures every year (over 230,000 in 2011) and an aggressive sorting system, the French consumer insolvency procedure seems to be firing on all cylinders already, but yet another efficiency-enhancing reform became effective on November 1, 2010.¹¹¹ Two of the latest reforms are of particular interest in terms of performance, and they both promise to make significant contributions.

The first innovative step follows the Swedish model of doing away with recourse to the judiciary for recommended "ordinary" measures. Now, the commissions need not obtain either unanimous creditor assent or court approval for workout plans not involving a discharge of debt; the commissions have their own authority to impose such plans on creditors.¹¹² This will dispose of about 20,000 cases each year, freeing the judiciary from the burden of reviewing the commissions' recommendations in cases that were almost without exception confirmed in due course.¹¹³ Creditors can appeal to the execution court against

¹⁰⁸ See generally *BANQUE DE FRANCE*, *supra* note 100 (percentages based on the total number of cases successfully administered each year, not rejected or closed without a consensual or imposed solution).

¹⁰⁹ See Kilborn, *supra* note 96, at 648-50.

¹¹⁰ See *id.*

¹¹¹ Loi no. 2010-737 du 1 Juillet 2010 [Law 2010-737 of July 1, 2010], *Journal Officiel de la République Française* [J.O.] [Official Gazette of France], July 2, 2010, no. 0150, available at <http://www.legifrance.gouv.fr/affichTexte.do?cidTexte=JORFTEXT000022419094>.

¹¹² *Code de la consommation* art. L331-7, available at www.legifrance.gouv.fr/affichCodeArticle.do?cidTexte=LEGITEXT000006069565&idArticle=LEGIARTI000022423251&dateTexte=20120921 (July 1, 2010).

¹¹³ *Id.*

these commission-imposed measures, but as in Sweden, appeal is the only means of judicial recourse against imposed ordinary measures of relief in France.¹¹⁴

A second innovation is a radical simplification of the PRP route. As originally conceived, a PRP discharge had to be preceded by a court's inventorying the debtor's non-exempt assets (and debts) and conducting a liquidation of valuable non-exempt assets. As has been the case overwhelmingly in Chapter 7 liquidation cases in the United States, however, very few French debtors routed to the PRP had any assets worth liquidating. After November 2010, the commissions can recommend a personal recovery procedure *without liquidation* of assets in cases where the debtor possesses only household items that are necessary, of no market value, or the value of which would be "manifestly disproportionate" to the costs of sale.¹¹⁵ In such cases, which almost by definition will represent the great bulk of PRP cases, unless a creditor objects, the court need only confirm the commission's recommendation and announce an immediate case closure and discharge.¹¹⁶ Given the rising number of cases directed toward an immediate PRP discharge, removing the charade of an inventory and liquidation where no real value is available will seriously lighten the judicial burden in this system.

The French system continues its impressive evolution toward greater efficiency for both debtors and the state budget, permeated by a striking sensitivity to social policy concerns. One would be hard-pressed to find a better example of a consumer insolvency regime that has moved more decisively to expand and refine relief as part of a larger campaign against social exclusion. Over the past decade, relief has become steadily more available, on a broader scale, and in more focused and effective forms. This trend appears to be continuing in the latest round of reforms in France. In light of an impressive record of constant observation, analysis, and policy response to obstacles to effective debt relief, the consumer insolvency regime seems to have become one of the primary tools of modern French social policy.

CONCLUSION

To greater or lesser degrees, European consumer

¹¹⁴ See *id.* art. L332-2.

¹¹⁵ *Id.* arts. 330-1(1), 332-5.

¹¹⁶ *Id.*

bankruptcy regimes have responded well to efficiency concerns and the challenge of achieving social policy goals. The latest reforms have equipped these systems to discipline consumer financial markets more effectively and to administer the new market for relief more efficiently in responding to the casualties of recent financial crises. Also, to varying degrees, each of these systems continues to be distracted by an endless pursuit of the chimerical specter of “abuse,” even though identifiable cases of this problem are vanishingly few and difficult to identify. The United States offers some of the worst examples of the undesirable effects of an infatuation with keeping imagined “hordes of sharpies”¹¹⁷ out of the relief system. Experience reveals that unsupported rhetoric and unchecked conservative political excess is the primary obstacle to meaningful reform. European nations largely seem to be moving past unfounded fears of the mythical monster of bankruptcy abuse, with profoundly beneficial and lasting results. At least in Europe, policymakers appear to have embraced insolvency regimes as an important tool for social policy and are gradually shifting their attention from imaginary threats to real ones.

¹¹⁷ 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, 147 (1994).