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The bankruptcy machine

Assembly line fed by easy credit, eager lawyers and life's misfortunes

05:51 PM EST on Sunday, December 12, 2004

By [PAMELA YIP](#) / The Dallas Morning News

Donald Trump has done it. So have tens of millions of other Americans.

The number of bankruptcy filings nationwide doubled from 1990 to 2002 and has remained firmly above 1.5 million a year since then.

As bankruptcy has become more a part of American life, the stigma around it has lessened.

"There is no social stigma to it anymore," said Craig Jarrell, president of Pulaski Mortgage Co.'s Dallas region. "They just do it and don't look back, and they're ready to rock and roll and get a bunch of debt again."

The lending industry decries the rise in bankruptcies and the decline of the stigma. They're again pushing the 8-year-old effort to tighten the federal laws governing

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personal bankruptcy.

"It's kind of a moral issue — that people who are gaming the system get off scot-free," said Sen. Charles Grassley, R-Iowa, the legislation's main sponsor. "I intend to pursue it just as hard as I have in the past."

But consumer advocates and bankruptcy attorneys say no one who files is happy about it, and most have been driven to it by a job loss, divorce or health problems. They say that aggressive lenders are partly to blame and that bankruptcy laws should continue to protect the weakest members of society from a life of indebted servitude.

After eight years of failure, backers of the tougher bankruptcy legislation are encouraged by the fact that Republicans now hold the White House and predominate in Congress.

The legislation calls for a stricter "means test" that would shift more people from a Chapter 7 bankruptcy, which usually cancels most debts, to a Chapter 13 filing, under which debtors work out a payment plan with creditors.

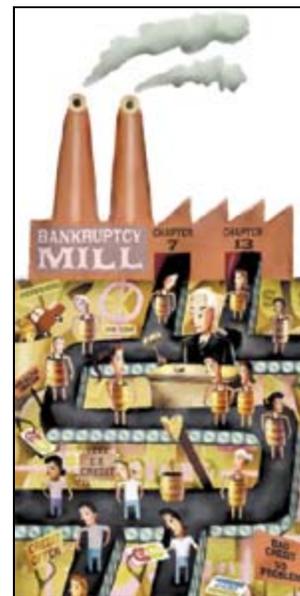
"If it ever has a chance of being resurrected, it will be under this Congress and under this administration," said Richard Venable, a consumer bankruptcy attorney in Bedford, Texas.

Is guilt gone?

Bankruptcy laws were created as a substitute for debtors' prisons. Throwing people in prison for not paying debts helps no one, after all.

Instead, a bankruptcy filing protects a debtor from creditors while a court figures out how much of the debt can reasonably be repaid. The court can declare none, some or even all of the debt forgiven. But usually creditors get something.

That system generally worked well. But as bankruptcies have soared, opinions on the issue have split along the sharp divide in the American political landscape.



Michael Hogue / DMN

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Conservatives tend to see it as a matter of personal responsibility, while liberals see it as a matter of big corporate interests riding on the little guy. They're even divided on whether the stigma is gone.

"The vast majority of Americans say that bankruptcy's more socially acceptable than it was years ago," said Jeffrey Tassey, executive director of the Coalition for Responsible Bankruptcy Laws, a Washington-based lenders group. "Most Americans have seen somebody down the street with two cars, where they go bankrupt and there are no consequences to that, and it really upsets them."

But those who work with bankruptcy filers disagree.

"The stigma is not gone," said Karen Gross, a law professor at New York Law School and president of the Coalition for Consumer Bankruptcy Debtor Education. "Most debtors are very upset that they have failed at America's game. They're living the reverse Horatio Alger story, and there's an enormous sense of failure."

Still others see a generational shift. Carey Ebert of Hurst, Texas, is vice president of the National Association of Consumer Bankruptcy Attorneys:

"My older clients are distraught over what's happened to them, whereas younger people are much more — aaaaaah [whatever]. Part of that is the credit culture has changed."

Stigma vs. strategy

On both sides, it seems, everything these days comes down to strategy: Just as the lending industry offers as much credit to consumers as it's allowed to under the law, many consumers who get in trouble with credit make a strictly financial decision on whether to avail themselves of the protections provided under the bankruptcy laws.

"There's no question people use

Before You File

If you're having trouble paying your bills, consider these possibilities:

First, talk to your creditors. They may be willing to negotiate a modified repayment plan.

Next, contact a credit counseling service. These services work with you and your creditors to develop a debt repayment plan. Some nonprofit organizations charge little or nothing for their services.

If nothing else is working, bankruptcy may be your only option. The first step is to hire a lawyer.

-- *Ieva M. Augstums*

Glossary

bankruptcy as a strategy," said Darrell W. Cook, a collections attorney in Dallas. "What I see are debtors who have not spoken to a bankruptcy attorney, who have not the first idea what bankruptcy entails, telling me, 'If you pursue that debt, I'll file for bankruptcy, and you'll never get it.' "

Mr. Cook, whose job puts him at the center of the debate, points the finger at two groups:

- First, bankruptcy attorneys who push their services.

"This option has been marketed in ways we haven't seen, in my opinion, on TV, on the Internet," he said. "They're aggressively marketing bankruptcy as an option, and people are responding to that."

- Second, lenders who've lowered their standards.

"There's no question that the readily available credit for a person is a big part of the problem," he said. "But there's a competitive marketplace. These lenders are taking risks that I don't think they would normally take, because there's a lot of money around to loan."

Mr. Venable said he and his fellow bankruptcy attorneys are simply addressing a need.

Lenders say they're doing the same thing, just offering their services.

"The same people who are excoriating the industry for easy credit were attacking it for not extending enough credit in the late '80s and early '90s," said Mr. Tasse of the Coalition for Responsible Bankruptcy Laws. "Lenders have been

Chapter 7: A liquidation bankruptcy. For individuals, it involves the sale of a debtor's nonexempt property and the distribution of the proceeds to creditors.

Chapter 11: A reorganization bankruptcy, usually involving a corporation or partnership.

Chapter 12: Bankruptcy for a family farmer.

Chapter 13: Bankruptcy involving the adjustment of debts for someone with regular income.

Creditor: A person or business that the debtor owes money or that claims to be owed money.

Debtor: A person who has filed a petition for bankruptcy.

Exempt property: Property, or value in property, that a debtor is allowed to retain, free from the claims of creditors who do not have liens.

Secured debt: Debt backed by a mortgage, pledge of collateral, or other lien; debt for which the creditor has the right to pursue pledged property upon default.

Unsecured claim: A claim or debt for which a creditor holds no special assurance of payment.

Trustee: A court-appointed official who administers the debtor's bankruptcy estate. A Chapter 7 trustee liquidates property and distributes the proceeds to creditors. A Chapter 13 trustee reviews the debtor's plan and collects and distributes payments.

SOURCE: Bankruptcy Judges Division, Administrative Office of the U.S. Courts

able to extend credit to people who weren't able to get it. I don't see there's any way there's too much credit."

But lenders can't lend to consumers at exorbitant interest rates and then cry for relief from bankruptcy filings, said Ms. Gross of the Coalition for Consumer Bankruptcy Debtor Education.

"Today's there's a reversal of redlining," she said. "We target the poor and vulnerable because that's where you make huge amounts of money. To tighten the bankruptcy system without fixing the predatory lending system is unfair and unwise."

8-year battle

Congress' tortuous attempts to toughen bankruptcy laws bit the dust in 2002 after Democrats inserted language to prohibit abortion clinic protesters from filing for bankruptcy to escape court-imposed financial penalties.

The legislation passed the House twice but died in the Senate.

Under the proposal, creditors may ask a bankruptcy court to dismiss a Chapter 7 case if a debtor's income is above the state median income level.

Bankruptcy will still be an option to people who truly can't afford to pay, said Catherine Pulley, spokeswoman for the American Bankers Association.

"The issue that we have are people with high incomes who stick everyone else with the bill because they don't want to pay some of their debts back," she said. "We believe the courthouse doors need to be kept open for people who truly need it. The bill specifically says that anyone below the median income goes straight to bankruptcy. No means test, nothing."

Still, opponents called the legislation mean-spirited.

"We will lose a significant social safety net," Ms. Gross said. "In an environment of declining consumer protection and declining bankruptcy relief, you will have a group of people who will be living perennially in a form of modern-day peonage — a kind of indentured servitude, where you're going to be working forever to repay your obligations."

There's nothing callous about it, said U.S. Rep. Sam Johnson, R-Plano.

"I don't think it's mean-spirited in any way, shape or form," he said.

"Somehow, we've gotten away from anyone who declares bankruptcy having to pay anything. If there are assets, they ought to be used to help creditors, whoever they might be."

Staff writer Ieva M. Augstums contributed to this report.

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