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Statement to the *Dickinson Law Review* Bankruptcy Symposium

Congressman George W. Gekas*

As many of you know, this is a homecoming of sorts for me. As an alumnus of Dickinson, I am honored to be addressing you on what I believe will be one of the most crucial pieces of legislation that Congress will address this year: bankruptcy reform. As you probably know, I introduced a bill earlier this week that I hope will stem the epidemic tide of bankruptcy, but I would like to start today by examining some of the history and issues that led up to introduction of the bill.

The greatest, and perhaps most dangerous, irony I have come across in the past decade is that despite economic growth, low inflation, low unemployment, and increasing personal income, our nation has seen an alarming increase in the number of bankruptcy filings—1.3 million in 1997 to be exact. Think about that for a second. That's more than one family per every hundred in the United States. It is also over forty billion dollars of debt that has been erased in a year of strong economic growth. The problem is further illustrated by the fact that the number of filings in the '90s is eight times greater per household than the number of filings made during the Depression.

It hasn't always been this way. The so-called "bankruptcy of convenience" is a new phenomenon, borne out of the loss of stigma the word "bankruptcy" once, but no longer, carried. A sense of responsibility—or perhaps more appropriately, a sense of disgrace and embarrassment—used to discourage Americans from declaring bankruptcy. Deals were cut to make sure that creditors would at least eventually see their money and that debtors paid, rather than legally erased, their debts.

Think about how undesirable bankruptcy was in Pennsylvania during colonial times. Pennsylvania passed one of the first

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bankruptcy laws in our nation's history. The Pennsylvania Bankruptcy Act of 1785 called for consumers convicted of bankruptcy to be nailed to the pillory by the ear and then publicly flogged. After the flogging, the ear would be cut off. By no means do we wish to return to those days.

By the Twentieth Century, penalties for bankruptcy had lessened, but the stigma remained. Harry S. Truman, the thirty-third President of the United States, spent the better part of the 1920s in debt due to the collapse of his clothing business in 1922. Truman was both a man and a President of the highest moral character. His tremendous sense of responsibility was reflected in the motto that sat on his desk in the Oval office: "The buck stops here." Truman eventually paid off all of his creditors by working out deals and payment schedules, thereby keeping himself out of bankruptcy court and ensuring that he lived up to bills he amassed.

As an attorney in practice, I can remember negotiating such a repayment arrangement for a client in the late '60s. With just a few phone calls I was able to appease my client's creditors and arrange for payments to be made on a regular basis until my client's debt could be discharged. While my client's creditors were demanding their pound of flesh, they knew all too well that a deal was in their best interests. The creditors would get paid, albeit not immediately. The other option was for my client to declare bankruptcy which would have erased his debt and left his creditors high and dry. Both parties agreed that an arrangement based on responsibility and good faith was the better alternative.

Today's situation is tremendously difficult to comprehend because times are good. The only reasonable explanation is that the stigma of bankruptcy is all but dead. How do we know? Other than in the last two decades, we have only seen "spikes" in the number of bankruptcy filings during times of recession. That makes sense. During difficult economic times, it is always tougher to make ends meet. But the past six years have been a period of unparalleled economic growth—as any Wall Street broker would be happy to tell us. So, obviously, the growth in the personal bankruptcy market is not a response to the economy.

Nor can we justifiably point an accusing finger at the credit card industry. The popular myth is that the credit card industry is flooding consumers with credit they cannot afford, thereby causing a surge in filings. However, those accusations are misdirected. Credit card debt accounts for only sixteen percent of all bankruptcy

debt. With some quick calculations, you can see that leaves \$33.6 billion of some \$40 billion in debt still unaccounted for. Thus, it is not likely, nor is it fair, to blame the credit card industry for the rapid increase in bankruptcy filings.

The lack of stigma has become a weed infesting the bankruptcy landscape. And the seed that sprouted this condition was Congress, or more correctly, our predecessors in Congress. The Bankruptcy Reform Act of 1978 changed the code dramatically, making the system decidedly pro-debtor. The 1978 reforms were appropriate for the times, but the times have changed. In the twenty years prior to 1978, bankruptcy filings rose from one hundred thousand filings per year to two hundred thousand filings per year. In the twenty years since, filings have gone from 200,000 to 1.3 million.

In his 1997 Economic Report, President Clinton acknowledged that the Bankruptcy Reform Act of 1978 is the primary culprit for the increased filings of the past two decades. The report states that "recent rises in non-business bankruptcy is probably the result of changes in the bankruptcy law and a number of broader social changes [R]esearchers generally attribute much of the increase in bankruptcies since the late 1970s to effects of the Bankruptcy Reform Act of 1978."

The weed has spread as bankruptcy has become viewed more as a financial planning tool, a government debt forgiveness program, and a first choice rather than a last resort. Bankruptcy has even become fashionable—the Hollywood trend-setters do it. People Magazine recently ran a cover story to illustrate the problem. Willie Nelson, Burt Reynolds, Kim Basinger, M.C. Hammer, former Baseball Commissioner Bowie Kuhn, Arizona Governor Fife Symington, former Philadelphia Eagles owner and Pennsylvania trucking magnate Leonard Tose are just a few of the high profile filers lending their help, albeit unconsciously, to bankruptcy en vogue. Just last week, Grammy Award winning singer Toni Braxton, who has sold more than fifteen million records in the past five years, declared bankruptcy.

It is simply too easy to file. I sent my bankruptcy counsel, Dina Ellis, to Bankruptcy Court a few weeks back and what she reported to me was mind boggling. Lawyers who have never met their clients looking like limousine drivers at the airport as they try to identify their clients and get them in front of the judge. Scores of cases are decided over the course of a few hours. Courts spend

an average of one to five minutes deciding each case. Can you imagine? Spend a couple hours filling out some forms and a couple minutes before a judge and you can kiss your debts goodby.

Of course, any remnants of the bankruptcy stigma are easily erased by our daily doses of media. Bankruptcy lawyers have taken to advertising on TV, radio, and in the papers to tout the benefits of stiffing your creditors or to explain how to restore your credit immediately after declaring bankruptcy. The way they make it sound, you would think that you are crazy to responsibly pay your bills or mortgage. It pays to go into debt.

The crux of the problem is that too many consumers are choosing convenience rather than responsibility for the debts that they have accrued and can afford to pay. This is why you and I should care about stemming the tidal wave of bankruptcies.

When irresponsible spenders who can afford to pay all of their debt declare bankruptcy, you and I get stuck with the bill. It is a forty billion dollar bill that we share this year, or four hundred dollars per household. I do not know about you, but four hundred dollars is five weeks' worth of groceries or twenty-plus fill-ups at the gas pump to me. It has also been estimated that it takes fifteen responsible borrowers to cover the cost of one bankruptcy of convenience.

When consumers file for bankruptcy, retailers pass on the costs in the form of higher prices, layoffs, and/or buying less from suppliers. Lenders redistribute bankruptcy debt by charging you and me higher interest rates and insurance premiums.

Now, my colleagues, I have a decision to make: plow new ground or let the weeds grow. Mr. McCollum, Mr. Boucher, Mr. Moran and I have decided to plow. The bill we introduced here is a conglomeration of ideas, strategies, and solutions that, when enacted, will put an end to the abuse, protect the downtrodden, and keep you and I from footing the bill for someone else's irresponsibility.

The genesis of this reform was the Bankruptcy Reform Act of 1994 and its major tenet: the formation of the National Bankruptcy Review Commission. The Commission was charged with the duty of studying the Bankruptcy Code and submitting a report in two years suggesting proposed reforms. Last October, the Commission released its report and recommendations to Congress. To put it lightly, the report was disappointing—even by several commissioners' own admissions, for it failed to identify the source of the

problem of increased consumer bankruptcies or offer adequate solutions. However, in its defense, it did provide a starting point.

Our bill is comprehensive—tackling both consumer and business bankruptcy. Let me highlight some of the fine points of our bill:

- Our bill emphasizes responsibility and cuts down on abuse by implementing a needs-based system. Our plan mirrors previous legislation introduced by Congressmen McCollum and Boucher.
- A unique portion of our legislation is what I call the “Debtor’s Bill of Rights,” which outlines protection for those who legitimately require bankruptcy’s safety net and would save them from becoming victims of the “bankruptcy mills.”
- There is also language included in the bill that provides a pilot program for consumer education to help debtors better manage their finances.
- We have addressed the exemption issue, making it more difficult for those who are dodging their debts to hide their wealth in exempted assets.
- Our bill also permanently extends Chapter 12 bankruptcy to protect family farmers under the Code.

What you see before you is a tremendous accomplishment. It re-establishes the link between bankruptcy and the ability to pay one’s debts. Yet, it still preserves the foundation of bankruptcy—providing a safety net to support those who suffer a major life crisis.

To paraphrase my former colleague and former Treasury Secretary Lloyd Bentsen: while there is nothing wrong in legitimately admitting financial defeat by filing bankruptcy when it becomes impossible to repay one’s debts, we must make an effort to restore the justifiable sense of embarrassment Americans once felt asking their neighbors to shoulder their burden.

Another concern is that the current system—which breeds financial irresponsibility—is not the cure-all imagined by those who live beyond their means. By allowing people to escape from their financial obligations, we are doing those individuals a disservice by not encouraging them to manage their finances and control their debt. The end result is a citizenry caught in a never-ending cycle of debt. With bankruptcy filings expected to reach historic levels this year, I have grave concerns for the stability—economic and emotional—of the American family.

The time is now, while our economy is robust, to reform. Waiting until the dawn of the next recession or economic downturn will allow this outbreak of bankruptcy to turn into an uncontrollable epidemic. Historically, bankruptcy was intended as a last resort pursued only under the most dire of situations. We are committed to ensuring that the code will help those in dire circumstances get back onto their feet while protecting responsible consumers who are unfairly bearing the costs.

Your assignment, should you choose to accept it, is to help to promote these reforms. That means contacting your hometown congressperson and senators and encouraging them to work with me to pass this vital legislation this year. It also means that I want to hear from you. This bill is a work in progress, and further reforms may be necessary. I have already had dialogues with interested citizens and members of Congress, and I want to add your voice to the debate.