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BANKRUPTCY AND THE INDIVIDUAL DEBTOR—AND A MODEST PROPOSAL TO RETURN TO THE SEVENTEENTH CENTURY*

*Vern Countryman***

As most lawyers and a few nonlawyers know only vaguely, we have a federal bankruptcy law under which debtors may obtain relief from most of their debts. Although relief is available to most debtors, whether they are individuals, corporations, partnerships, other business entities, labor unions, or nonprofit institutions, this article will focus on the relief available to individual debtors. To understand modern day treatment of individual debtors in bankruptcy, some understanding of the history of bankruptcy is necessary.

The origin of bankruptcy law has been traced to the Roman Law in existence in 118 B.C. and its subsequent development in Italian medieval cities in the thirteenth and fourteenth centuries.¹ To understand the treatment of debtors under the early bankruptcy laws, however, it is necessary to have some understanding of their treatment prior to the adoption of such laws—a treatment under which the debtor who could not pay “was either killed, made a slave, imprisoned, or exiled.”² Thus, under the Twelve Tables of Roman law (circa 450 B.C.):

When a defendant [against whom a judgment has been rendered], after thirty days have elapsed, is brought into court a second time by the plaintiff, and does not satisfy the judgment . . .

* Since the above was written, the Senate has enacted S. 445, amended to adopt the shotgun approach of H.R. 1800 (referred to in note 101) by authorizing the court, on its own motion, to dismiss an individual debtor's petition for liquidation under Chapter 7 if the court finds it to be “a substantial abuse” of Chapter 7. The quoted language seems to be cosmetic, designed to enable the consumer credit industry to make the same arguments in the courts as it has been making in the Congress.

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1. I. ROSS, EUROPEAN BANKRUPTCY LAWS 4, 13-18 (1974); Riesenfeld, *The Evolution of Modern Bankruptcy Law*, 31 MINN. L. REV. 401 (1947).

2. I. ROSS, *supra* note 1, at 3.

the plaintiff, after the debtor has been delivered up to him, can take the latter with him or bind him or place him in fetters; provided his chains are not of more than fifteen pounds weight; he can, however, place him in others which are lighter, if he desires to do so.

If . . . [the debtor] desires to obtain food . . . he shall be permitted to support himself out of his own property. But if he has nothing on which to live, his creditor, who holds him in chains, shall give him a pound of grain every day, or he can give him more than a pound, if he wishes to do so. . . .

After [the debtor] has been kept in chains for sixty days, and the sum for which he is liable has been three times publicly proclaimed in the Forum [in the hope that friends or relatives would pay it], he shall be condemned to be reduced to slavery by him to whom he was delivered up; or, if the latter prefers, he can be sold beyond the Tiber.

Where a party is delivered up to several persons, on account of a debt, after he has been exposed in the Forum on three market days, they shall be permitted to divide up their debtor into different parts, if they desire to do so; and if anyone of them should, by the division, obtain more or less than he is entitled to, he shall not be held responsible.³

There were also "abundant traces in Rome, as in Europe until recent times, of an ancient custom of seizing the corpse of a defaulting debtor as a means of enforcing payment from his heirs"⁴—which may explain why there are still statutes on the books of some of our states specifically forbidding that practice.⁵

The early Italian bankruptcy laws, applicable to merchant debtors only, were not designed for the relief of the debtor, who was treated as an outlaw, but were designed almost entirely as an additional remedy to enable his creditors to reach his property for the collection of their claims. Although there was a voluntary type of bankruptcy which would enable debtors adjudged honest to escape imprisonment for debt, fraudulent debtors were punished severely and subjected to the destruction of their benches or trading places—the *banca rotta* of Italian law and the *banqueroute* of French law that led to the English word "bankrupt."⁶

Debtor dissection, detention of deceased debtors, and, originally, debt slavery were not sanctioned in England, from which we took most of our

3. I S. SCOTT, *THE CIVIL LAW* 63-64 (1932).

4. Radin, *Debt*, 5 *ENCY. SOC. SCI.* 32, 34 (1931).

5. CAL. HEALTH & SAFETY CODE § 7053 (1970); R.I. GEN. LAWS § 9-26-3 (1969).

6. Radin, *The Nature of Bankruptcy*, 89 *U. PA. L. REV.* 1 (1940).

law of debtor and creditor. But methods were early developed by which the creditor could have his debtor imprisoned and, in effect, held for ransom until the debt was paid.⁷ In 1283 the statute of Acton Burnell authorized a special procedure for evidencing debt by a bond that entitled the creditor immediately on default to levy on and sell the debtor's personal property and, if it did not produce enough to pay the debt, to imprison the debtor; the creditor was obliged to supply the debtor with bread and water.⁸ Two years later, the Statute of Merchants simplified matters by authorizing immediate imprisonment of the debtor on default. If after three months' incarceration the debtor had not paid his debt, his personal property was to be delivered to the creditor and his lands transferred to the creditor until the debt was discharged from the profits. The debtor was to languish in prison until the debt was paid.⁹

For the creditors of those who would not agree to such treatment, there were developed, during the thirteenth, fourteenth, and fifteenth centuries, writs of body attachment before judgment (*capias ad respondendum*) and body execution after judgment (*capias ad satisfaciendum*) for imprisoning the debtor until payment. The creditor could invoke these writs without becoming liable for the debtor's support. As an English court wrote in mid-seventeenth century:

If a man be taken in execution and lies in prison for debt, neither the plaintiff at whose suit he is arrested, nor the sheriff who took him, is bound to find him meat, drink, or clothes; but he must live on his own, or on the charity of others; and if no man will relieve him, let him die in the name of God¹⁰

Early English bankruptcy laws, two enacted in the sixteenth and two in the early seventeenth centuries,¹¹ enlarged the ranks of imprisoned debtors. Save for the first, they were confined to merchant debtors, could be invoked only by creditors on involuntary petitions, provided both for the

7. Sometimes the debtor was incarcerated for a longer period. In England, from 1772 to 1792, the Thatched House Society

released from prison 12,390 honest and unfortunate debtors; and so trifling were the debts for which these prisoners had suffered confinement, that their freedom was obtained at the expense of 45s. a head. Many were discharged merely on payment of the gaol fees, for which alone they were detained in prison; others on payment of costs, the original debts having long since been discharged.

2 T. MAY, CONSTITUTIONAL HISTORY OF ENGLAND 145-46 (Holland ed. 1912).

8. 11 Edw. (1283).

9. 13 Edw., stat. 3 (1285).

10. *Manby v. Scott*, 1 Mod. 124, 132, 86 Eng. Rep. 781, 786 (ex. 1659).

11. 34 & 35 Henry 8, ch. 4 (1543); 13 Eliz., ch. 7 (1571); 1 James, ch. 15 (1604); 21 James, ch. 19 (1623).

seizure and distribution of the debtor's property and for his imprisonment, and provided no discharge for the unpaid balance of his debts.

During the latter half of the seventeenth century a variety of English insolvency laws were enacted which were designed to enable some debtors to secure release from prison, but not discharge their debts, by surrendering their assets and taking a poor debtor's oath. Further, the creditor who had the debtor incarcerated could by his objection prevent the release, but if he did so he was obligated to pay a weekly sum for the debtor's subsistence. However, these laws were of limited application and were not very effectual.¹²

Finally, in an English bankruptcy law of 1705,¹³ some concessions were made to the debtor. He was allowed to keep, as exempt property, necessary family wearing apparel and an additional exemption of 5% of the estate, not to exceed 200 pounds, in a case where the estate paid a dividend of at least eight shillings on the pound to creditors—if the dividend was less, the commissioner who administered the law was to determine the amount of any additional exemption. If the debtor honestly surrendered up his estate and made a full disclosure of his affairs, he was granted a discharge of the unpaid balances of his debts. This would release him from imprisonment on such debts—a feature that still distinguishes bankruptcy in English-speaking countries from bankruptcy on the continent. But no “privilege, benefit or advantage” under the law was to extend to any bankrupt who had made a marriage settlement on a child of more than 100 pounds which left him insolvent, or who had gambling losses of five pounds in one day or 100 pounds in the aggregate in the year preceding bankruptcy. Moreover, the bankrupt who did not honestly surrender his property and disclose his affairs was to be adjudged a “fraudulent bankrupt” and a felon.

By another statute of 1732,¹⁴ the bankrupt's discharge was restricted to those cases in which four-fifths of his creditors consented thereto.

Not only did the English practice of imprisonment for debt apply to the American colonies, but debt slavery received sanction in the settlement of those colonies. Prospective employers of colonial labor adopted the indentured servant device by which impecunious Europeans as well as Englishmen bound themselves for a period of four or five years' labor in exchange for passage money and subsistence. When the labor force thus acquired

12. Cohen, *The History of Imprisonment for Debt and its Relation to the Development of Discharge in Bankruptcy*, 3 J. LEG. HIST. 153, 158-59 (1982); 8 W. HOLDSWORTH, A HISTORY OF ENGLISH LAW 234-36 (2d ed. 1937).

13. 4 Anne, ch. 17 (1705).

14. 5 Geo. 2, ch. 30 (1732).

proved insufficient, English convicts were shipped to America under involuntary indentures of somewhat longer term. It is estimated that nearly half of our total white immigration came over under indenture. In some colonies indentured service became an alternative to imprisonment for debt, but its use, unlike that of imprisonment for debt, rapidly diminished after the Revolution.¹⁵

There matters stood when our Constitution was framed, authorizing Congress to establish "uniform laws on the subject of bankruptcies throughout the United States",¹⁶ and when our first Bankruptcy Act of 1800¹⁷ was enacted. This Act, like the two that followed it, was enacted in response to a financial panic, was of short duration, and was repealed in 1803.¹⁸ It also followed the English model of the time. Confined to merchant debtors, it provided for involuntary proceedings on creditors' petitions only, and allowed the debtor to retain as exempt necessary wearing apparel and bedding for himself and family. The debtor who honestly surrendered his other property and disclosed his affairs could also receive an additional exemption at a graduated percentage depending on the percentage of dividend to creditors, and a discharge of his debts if two-thirds in number and value of his creditors consented. The debtor who did not honestly surrender and disclose was adjudged a "fraudulent bankrupt" and imprisoned not less than one nor more than ten years. Among those who obtained a discharge, entitling him to release from debtor's prison in Pennsylvania after nearly three years of incarceration, was Robert Morris, the financier of our Revolution and a member of the Constitutional Convention.¹⁹

In the interim between repeal of the first and enactment of our second Bankruptcy Act, there were substantial changes in the English practice. The Court for Relief of Insolvent Debtors was created in 1813²⁰ and empowered to give jail release, but not a full discharge of debts, to all insolvents who surrendered their property to their creditors. It set free more

15. Goodrich, *Indenture*, 7 ENCY. SOC. SCI. 644 (1932).

16. U.S. CONST., art. I, § 8, cl. 4 (1787).

17. 2 Stat. 19 (1800).

18. 2 Stat. 348 (1803).

19. C. WARREN, BANKRUPTCY IN UNITED STATES HISTORY 13, 20 (1935). Bankruptcy proceedings were initiated against Morris in July 1801, and he received his discharge in December. Thereafter, his creditors abandoned the proceedings and they were vacated on the petition of his heirs 36 years later and 25 years after his death. See *In re Morris*, 17 F. Cas. 785 (E.D. Pa. 1837) (No. 9,825). Another member of the Constitutional Convention, Supreme Court Justice James Wilson, fled to North Carolina shortly before his death in 1798 to avoid imprisonment for debt in Pennsylvania. C. WARREN, *supra* at 13.

20. 53 Geo. 3, ch. 6 (1813).

than 50,000 debtors in the next thirteen years.²¹ Body attachment was abolished in 1838,²² although the use of body execution was not restricted for another thirty years.²³

A step toward voluntary bankruptcy proceedings was made in 1825 when it became the basis for an involuntary creditors' petition for the debtor to publish a statement that he was insolvent.²⁴ And in 1840, a Parliamentary Commission reported that the requirement of creditor consent to a discharge should be abolished because "it is sometimes attended with a very heavy and useless expense to the bankrupt, and he is tempted, by knowledge of such expense, and the probability of being obliged to purchase the assent of some creditors, to secrete property."²⁵

There was also one significant, although not complete, change in American practice in the interim between our first and second Bankruptcy Acts. Imprisonment for debt had been widely employed in this country in the early nineteenth century. Thus, in 1830, there were in Massachusetts, Maryland, New York, and Pennsylvania three to five times as many persons imprisoned for debt as for crime.²⁶ The Suffolk County Jail in Boston alone for the decade 1820-1830 contained 11,818 imprisoned debtors from a total population ranging from 43,000 to 63,000.²⁷ A wave of reform in the 1830's, however, led to state constitutional provisions forbidding imprisonment for debt. Today, such prohibitions appear in the constitutions of most states and in the statutes of several where the constitutions are silent.²⁸ But many of these provisions are limited to contract debtors, and many that are so limited contain exceptions for absconding debtors or those guilty of fraud; and in the fraud cases "evidence may be conclusive which would be far from sufficient in a criminal prosecution."²⁹ Other provisions, not confined to contract debtors, contain exceptions for specific kinds of torts.³⁰

Our Bankruptcy Act of 1841,³¹ effective in 1842 and repealed in 1843,³²

21. T. MAY, *supra* note 7, at 146.

22. 1 & 2 Vict., ch. 110 (1838).

23. 32 & 33 Vict., ch. 62 (1869).

24. 6 Geo. 4, ch. 16 (1825).

25. Report of the Commissioners for Inquiring into Bankruptcy and Insolvency xix-xx (1840).

26. Ford, *Imprisonment for Debt*, 25 MICH. L. REV. 24, 29 (1926).

27. Nehemkis, *The Boston Poor Debtor Court*, 42 YALE L.J. 561, 576 (1933).

28. See Note, 80 YALE L.J. 1679 (1971); Note, 42 IOWA L. REV. 306 (1957); Note, 26 N.Y.U. L. Rev. 172 (1951).

29. Hamilton, *In re the Small Debtor*, 42 YALE L.J. 473, 480 (1933).

30. Note, 1970 LAW & SOC. ORDER 658; Note, 42 IOWA L. REV. 306 (1957).

31. 5 Stat. 440 (1841).

32. 5 Stat. 614 (1843).

went beyond then current English practice in substantial respects. While preserving involuntary proceedings against merchants owing debts of \$2,000 or more, it also provided for voluntary proceedings open to merchants and nonmerchants alike; England did not extend voluntary proceedings to merchants until 1844³³ and to nonmerchants until 1861.³⁴ Exemptions covered not only wearing apparel, but furniture and other "necessaries" not to exceed \$300 in value, all without regard to the size of the dividend paid to creditors. Although Congress was advised of the recommendation of the British Parliamentary Commission against conditioning discharge on creditor consent,³⁵ a recommendation followed in England in 1849.³⁶ It compromised the issue by providing for discharge unless a majority of creditors took affirmative action by filing written dissents.³⁷

The economic crisis following the Civil War produced our third Bankruptcy Act of 1867,³⁸ which was not repealed until 1878,³⁹ and which provided for voluntary and involuntary proceedings for merchants and nonmerchants owing debts of more than \$300 and extended both proceedings to corporations for the first time. Like the earlier Acts, this one specified exemptions for wearing apparel and other necessities. Unlike the earlier Acts, it also provided that the debtor could keep such other property as was exempt by federal nonbankruptcy law and by the law of the state of his domicile in the year 1864 (extended, in 1872, to the year 1871).⁴⁰ Thus Congress incorporated existing state law partially to define the bankruptcy exemption policy. But it did so in such a way that state laws were given effect in bankruptcy only if they were also effective as between the debtor and his creditors outside of bankruptcy, and states were not free to change the bankruptcy policy prospectively by amending the state exemption laws.

The 1867 Act also provided that all debtors who had not committed one of a long list of dishonest or otherwise reprehensible acts should receive a

33. 7 & 8 Vict., ch. 96 (1844). The voluntary petition was abolished by 32 & 33 Vict., ch. 71 (1869), but restored by 46 & 47 Vict., ch. 52 (1883).

34. 24 & 25 Vict., ch. 134 (1861).

35. 9 CONG. GLOBE 134-44 (1841).

36. 12 & 13 Vict., ch. 106 (1849). Creditor consent to discharge was reinstated for any case where the dividend did not equal 10 shillings per pound by 32 & 33 Vict., ch. 71 (1869), but was eliminated again by 46 & 47 Vict., ch. 52 (1883).

37. A voluntary bankrupt who had made a preferential transfer could not obtain a discharge without the consent of a majority in interest of creditors not preferred.

38. 14 Stat. 517 (1867).

39. 20 Stat. 99 (1878).

40. 17 Stat. 334 (1872). *See also* 17 Stat. 577 (1873).

discharge without the necessity of creditor consent for the first year after enactment (extended by subsequent amendments through the year 1869).⁴¹ Thereafter, consent of a majority of creditors was required if the debtor's assets did not equal 50% of his debts, but in 1874 the requirement of creditor consent was dropped for involuntary cases and was reduced to a requirement of consent of one-fourth in number and one-third in amount where assets did not equal 30% of debts for voluntary cases.⁴²

The Civil War also produced the thirteenth amendment, providing that, "Neither slavery nor involuntary servitude, except as a punishment for crime whereof the party shall have been duly convicted, shall exist within the United States," and authorizing Congress to enforce that prohibition by appropriate legislation.⁴³ After this abolition of slavery, resort was again had to a variation of the old indentured servant device, which came to be known as peonage. In one form, it was based on sharecropper or labor contracts. In another, it arose when an employer of labor was allowed to pay fines imposed for vagrancy and other petty offenses and thus to secure the service of the offender until his fine, and additional debts to his employer incurred for subsistence, were paid. Peonage, at one time widespread in the United States, was sanctioned by the law of many states, particularly in the South.⁴⁴ Congress in 1867 abolished peonage, declared state laws sanctioning it void, and made it a crime to hold anyone in "a condition of peonage."⁴⁵ In sustaining and enforcing these congressional enactments, the Supreme Court defined peonage as "a status or condition of compulsory service based upon the indebtedness of the peon to the master. The basal fact is indebtedness . . . [whether] the debtor voluntarily contracts to enter the service of his creditor" or the servitude is "forced upon the debtor by some provision of law. . . . [P]eonage, however created, is compulsory service, involuntary servitude."⁴⁶ "The essence of the thing is compulsory service in payment of a debt. A peon is one who is compelled to work for his creditor until his debt is paid."⁴⁷ The Supreme Court has applied the thirteenth amendment and the federal statutes to invalidate state laws making it a crime for an employee who is paid in advance to fail to perform the labor for which he was paid.⁴⁸

41. 15 Stat. 228 (1868); 16 Stat. 276 (1870).

42. 18 Stat. 180 (1874).

43. U.S. CONST., amend. XIII.

44. McBride, *Peonage*, 12 ENCY. SOC. SCI. 69 (1934).

45. 14 Stat. 546 (1867) (codified in 18 U.S.C. § 1581 (1976 & Supp. V 1981) & 42 U.S.C. § 1994 (1976 & Supp. IV 1980)).

46. *Clyatt v. United States*, 197 U.S. 207, 215 (1905).

47. *Bailey v. Alabama*, 219 U.S. 219, 242 (1911).

48. *Id.*; *Taylor v. Georgia*, 315 U.S. 25 (1942).

Since the enactment of our fourth Bankruptcy Act in 1898,⁴⁹ we have not been without a federal bankruptcy law, although the Bankruptcy Reform Act of 1978 repealed the 1898 Act and replaced it with an entirely new Bankruptcy Code effective October 1, 1979. Under the 1898 Act, which governed bankruptcy proceedings in this country for eighty years, any individual could file a voluntary petition, and all individuals save wage earners and farmers were subject to creditors' involuntary petitions. Again, there was a list of dishonest or otherwise reprehensible acts which would bar a discharge, and by later amendments this list proliferated over the years. If the debtor survived scrutiny under that list, however, he was entitled to his discharge without the necessity of obtaining consents from any of his creditors and without regard to the size of dividends paid. In another departure from the 1867 Act, the 1898 Act provided that the debtor was entitled to any exemptions specified by federal nonbankruptcy law and by the laws of the state of his domicile at the time the petition was filed. Thus, states were left free to amend the bankruptcy policy prospectively, although they could do so only by also amending their exemption laws as between the debtor and his creditors outside of bankruptcy.

This feature of the 1898 exemption policy was challenged as violative of the constitutional requirement that federal bankruptcy laws be uniform and as an invalid delegation of congressional power to the states. In a 1902 decision that did not adequately explain its ruling on either point, the Supreme Court rejected both challenges.⁵⁰ The Court, in a later decision, also held that, quite apart from any exemption law, a creditor whose claim was discharged in bankruptcy could not thereafter collect it out of the debtor's postbankruptcy wages even though he had taken before bankruptcy an assignment of future wages that was valid and enforceable under state law. To allow the creditor to enforce that assignment would be contrary to the bankruptcy policy to "relieve the honest debtor from the weight of oppressive indebtedness and permit him to start afresh" so that "the honest but unfortunate debtor who surrenders for distribution the property which he owns *at the time of bankruptcy*," is given "a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt."⁵¹

That aspect of the debtor's "fresh start," the preservation of his future earnings against discharged debts, has always been a feature of our bankruptcy laws although the enactment in 1938 of a new, alternative proce-

49. 30 Stat. 544 (1898).

50. *Hanover Nat'l Bank v. Moyses*, 186 U.S. 181 (1902).

51. *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934) (emphasis in original).

ture—a chapter 13 Wage Earner's Plan—allowed the debtor, whose principal income was from wages, salary, or commissions, to retain also any nonexempt assets he owned by substituting for liquidation of those assets a plan to pay all or a part of his existing debts from future income, after which he received a discharge of any unpaid balances of his debts. But the choice was the debtor's; a chapter 13 case could be initiated only on the debtor's voluntary petition.⁵²

Obviously, the debtor's future wages were essential to his "fresh start" but the exemptions he was allowed to retain from his existing estate were also a significant element in the measurement of the extent of that fresh start. And there was considerable dissatisfaction with the 1898 Act's incorporation of state exemption laws, not only because this element of the fresh start was different in each state but also because in many states the exemption laws are both parsimonious and grievously obsolete.⁵³ Debtors in financial difficulty do not enjoy effective lobbies in state legislatures. In Connecticut, for instance, a sparse list of exemptions included from 1821⁵⁴ to 1977⁵⁵ "two cords of wood, two tons of hay, five bushels each of potatoes and turnips, ten bushels each of Indian corn and rye or the meal or flour manufactured therefrom." Hence, the federal Commission that Congress created in 1970 to revise the bankruptcy law recommended, in view of "the unfairness of existing state exemption laws, most of which are archaic, some of which are unduly generous, and some of which are exceedingly niggardly,"⁵⁶ that the new Bankruptcy Code itself spell out a uniform list of exemptions for bankruptcy cases. That recommendation was not followed. In the Code that passed the House, the debtor was given a choice between exemptions specified in the Code or those in other federal law and in the law of the state of the debtor's domicile at the time the petition was filed.⁵⁷ In the version that passed the Senate, however, there was no bankruptcy list of exemptions and the debtor was given no choice. As under the old Bankruptcy Act, the debtor was confined to exemptions specified in other federal law and in the law of the state of his domicile.⁵⁸

52. 52 Stat. 930 (1938). Originally, ch. 13 was limited to those whose income did not exceed \$3,600 per year. By a 1950 amendment, the limitation was raised to \$5,000, and in 1959 it was eliminated (73 Stat. 24).

53. See Countryman, *For a New Exemption Policy in Bankruptcy*, 14 RUTGERS L. REV. 678, 681-84 (1960).

54. CONN. GEN. STAT. tit. 2, Act 74, at 56 (1821).

55. 1977 Conn. Pub. Acts 77-466 § 4.

56. *Report of the Commission on the Bankruptcy Laws of the United States*, H.R. DOC. NO. 137, 82d Cong., 1st Sess. pt. I, at 17 (1973) [hereinafter cited as *Commission Report*].

57. H.R. 8200, 95th Cong., 2d Sess. § 522 (1978).

58. S. 2266, 95th Cong., 2d Sess., § 522 (1978).

In a last-minute compromise between the two Houses, the House version, giving the debtor a choice, was retained but with an important qualification: the legislature of each state was empowered to "opt out" of the choice by providing that the state's domiciliaries could not elect to take the bankruptcy list of exemptions specified in the Bankruptcy Code.⁵⁹

If debtors in financial distress do not have an effective lobby in state legislatures, the same cannot be said for the consumer finance industry. In the four and one-half years since enactment of the new Bankruptcy Code, no fewer than thirty-five states have "opted out" of the bankruptcy exemption choice for the debtor and confined their domiciliaries to exemptions prescribed by other federal and state law.⁶⁰ While some of them have taken the occasion also to update obsolete state exemption laws somewhat, many of them have not.⁶¹

In the new Bankruptcy Code, Congress has abdicated its bankruptcy power to the states more than ever before. Not only has it empowered the states by the enactment and amendment of exemption laws applicable in nonbankruptcy contexts to define the content of the federal bankruptcy policy for the present and in the future, but it has also empowered the states, solely for the purpose of defining the content of the federal bankruptcy exemption policy, to do no more than enact a law which says to their domiciliaries: you shall not have the choice of the bankruptcy exemptions specified in the Bankruptcy Code. This feature of the new Bankruptcy Code has been challenged as both a violation of the uniformity requirement of the Constitution and as an unlawful delegation of congressional power to the states. The United States Court of Appeals for the Seventh Circuit, in an opinion which reflects little if any appreciation of the difference between the federal abdication involved in the new Code and that involved in the 1898 Act's incorporation of state exemption laws, treated the Supreme Court's 1902 decision on the constitutionality of the 1898 Act⁶² as controlling, and the Supreme Court denied review of the case.⁶³ So we are left with a new Bankruptcy Code in which the important

59. 11 U.S.C. § 522(b)(1) (1976 & Supp. IV 1980).

60. It is easiest to list the 15 states where the debtor has not yet been deprived of the choice: California, Connecticut, Hawaii, Massachusetts, Michigan, Minnesota, Mississippi, New Jersey, New Mexico, Pennsylvania, Rhode Island, Texas, Vermont, Washington, and Wisconsin.

61. State exemption laws are collected in 7 COLLIER ON BANKRUPTCY (15 ed. 1982).

62. *Hanover Nat'l Bank v. Moyses*, 186 U.S. 181 (1902).

63. *In re Sullivan*, 680 F.2d 1131 (7th Cir.), *cert. denied*, 103 S. Ct. 349 (1982). It should not be viewed as advertising, whether constitutionally protected or otherwise, for me to reveal that I made the unsuccessful argument in the Court of Appeals and wrote the unsuccessful petition for certiorari.

exemption ingredient of the fresh start policy is completely nonuniform. Because thirty-five state legislatures have decided that this should be so, it is different in each of the thirty-five states from any of the other forty-nine. In the remaining fifteen states it is the same, unless the debtor decides that this shall not be so, in which event it is also different in that state from any of the other forty-nine. Congress has participated in the shaping of this exemption policy only to the extent of abdicating to state legislatures and debtors the power to decide what that policy shall be.

The lobbying efforts of the consumer finance industry have not been confined to state legislatures. That industry is concerned also with that part of the fresh start policy of American bankruptcy law which has said to the individual debtor in this country since 1898: you may file a voluntary bankruptcy petition and, if you honestly surrender your nonexempt existing assets and have not committed any of the other acts that will bar a discharge, you will receive a discharge that will free your future earnings from the claims of most of your prepetition creditors.⁶⁴ It is true that in the vast majority of cases of individual bankrupts there are no nonexempt assets of significant value to be surrendered.⁶⁵ This has not seemed to Congress in modern times to be a reason to deny the honest debtor his fresh start. It is true also that in the new Bankruptcy Code Congress has given the debtor an alternative chapter 13 plan under which he can retain any nonexempt assets and instead pay off all or a part of his debts out of future earnings and receive a discharge of unpaid balances, and that this alternative is no longer confined to wage earners but extends to most individuals with earnings sufficiently stable and regular to support such a plan.⁶⁶ But, as under the old Act, this alternative is strictly the debtor's choice; a chapter 13 case can be initiated only on the debtor's voluntary petition.⁶⁷

It has been a matter of regret to some creditors that American bankruptcy law did not pick up a feature adopted in England in 1883⁶⁸ which

64. That feature of the 1898 Act is fully preserved in the new Code. 11 U.S.C. § 727 (1976 & Supp. IV 1980). The discharge is of "most" prepetition debts because under the Code, as under the 1898 Act, there is a specification of certain debts that are not dischargeable. 11 U.S.C. § 523 (1976 & Supp. IV 1980).

65. Statistics on bankruptcy do not enjoy a high priority on the government computer and there are no statistics available yet on this point under the new Code. But, year in and year out under the old Act, nothing was available for distribution to creditors in 85% of the cases, V. COUNTRYMAN, *CASES AND MATERIALS ON DEBTOR AND CREDITOR*, 264 (2d ed. 1974), and there is no reason to believe that the experience will be significantly different under the Code.

66. 11 U.S.C. §§ 101(27), 109(e) (1976 & Supp. IV 1980).

67. 11 U.S.C. §§ 301, 303 (1976 & Supp. IV 1980).

68. 46 & 47 Vict., ch. 52 (1883).

still characterizes the English practice today.⁶⁹ the conditional or suspended discharge. Under that practice, the debtor will frequently not get a fresh start, or it will be long delayed. The court is given broad discretion to grant or deny discharge, to condition it on the making of payments to creditors from future earnings or other post-bankruptcy acquisitions, or to suspend the discharge while such payments are being made. There was, a half-century ago, a proposal that we adopt this English feature. It provoked vehement opposition in congressional hearings—it is, to my knowledge, the only proposed bankruptcy legislation in this country to be characterized by witnesses as “UnAmerican”⁷⁰—and it did not emerge from committee.

But the consumer credit industry has, since 1964, been pushing a proposal that amounts to the same thing.⁷¹ Under that proposal, an individual debtor seeking relief under the liquidation provisions of the bankruptcy law would be denied that relief if the court concluded that he could pay substantial amounts of debts out of his future earnings under a chapter 13 plan. Hearings were held on this proposal and on some questionable economic studies designed to support it in 1967⁷² and it also did not emerge from committee. A Brookings Institute study of the bankruptcy system that preceded the federal Commission’s study considered the proposal and the economic studies on which it was based and rejected it.⁷³ So did the federal Commission a few years later⁷⁴ and Congress in 1978.⁷⁵

But then there were the 1980 elections and a change in political climate which obviously suggested to the industry that the time was propitious for a renewed try. A campaign was mounted that dwarfed all earlier efforts. Members of the industry—banks, consumer finance companies, and credit unions—banded together as the National Coalition for Bankruptcy Reform and began to beat the drums for the Bankruptcy Improvement Act (a

69. R. WILLIAMS & M. HUNTER, *THE LAW AND PRACTICE IN BANKRUPTCY*, 121-36 (19th ed. 1979); Bashkloff, *Limited, Conditional and Suspended Discharges in Anglo-American Bankruptcy Proceedings*, 131 U. PA. L. REV. 69 (1982).

70. *Joint Hearings before Subcomms. of House and Senate Judiciary Comms. on S. 3863*, 73d Cong., 1st Sess., 546, 743 (1932).

71. The earlier proposals were embodied in H.R. 12,784, 88th Cong., 2d Sess. (1964); H.R. 292, 89th Cong., 1st Sess. (1965); S. 613, 89th Cong., 1st Sess. (1965); H.R. 1057 & H.R. 5771, 90th Cong., 1st Sess. (1967).

72. *Hearings before Subcomm. No. 4 of House Judiciary Comm. on H.R. 1057 & H.R. 5771*, 90th Cong., 1st Sess. (1967).

73. D. STANLEY & M. GIRTH, *BANKRUPTCY: PROBLEM—PROCESS—REFORM*, 38-39, 210-12 (1971).

74. *Commission Report*, *supra* note 56, at 158-59.

75. H.R. REP. NO. 595, 95th Cong., 1st Sess. 120-21 (1977). *See also* S. REP. NO. 989, 95th Cong., 2d Sess. 12-13 (1978).

gross piece of mislabelling). Suddenly the newspapers and other news media were featuring stories about how unfair the new Bankruptcy Code was to the extenders of consumer credit. These stories stated, that it was so generous to consumers that they were unable to resist the lure of the bankruptcy court whether bankruptcy relief was needed or not. For months the industry's representatives inundated the halls of Congress, wining and dining as many Congressmen and Senators as they could and, when they could not, wining and dining their legislative aides and their secretaries. They were lavish in their monetary political contributions. According to a July 1982 study by Ralph Nader's Congress Watch, the industry contributed \$987,000 to individual Congressmen. In consequence of all this effort, when their bill was introduced by Senator Dole of Kansas in S. 2000, in the 97th Congress, it bore the names of twenty-four senators. When it was introduced in the House as H.R. 4786 by now ex-Congressman Billie Lee Evans of Georgia (who received \$9,800 in contributions from the industry)⁷⁶, it bore the names of 65 Congressmen, a number that later grew to 269 (95% of whom had received industry contributions).⁷⁷

The industry also contributed \$300,000 for another supporting economic study directed by Professor Robert W. Johnson of Purdue University's Credit Research Center. (If Professor Johnson's name or that of his Research Center are familiar to you, it may be because you read in 1976 that Senator William Proxmire had given the Golden Fleece Award to the National Science Foundation for paying Professor Johnson and his Center to do an "unbiased and scientific study of consumer legislation and services." Since Senator Proxmire found that Johnson and his Center had "an overwhelming bias in favor of the credit industry," he concluded that asking them to do the study was "like asking the Air Force to study the need for the B-1 bomber or the oil and gas industry to evaluate the depletion allowance.")

Professor Johnson produced a two-volume study⁷⁸ based on interviews with about a thousand debtors filing for bankruptcy liquidation and examination of the petitions and accompanying papers of another thousand debtors. It begins with a fascinating preface. Perhaps recalling Senator Proxmire's award and realizing that a study funded by the industry might be suspected of bias, Professor Johnson and his associates assure the reader

76. CONGRESS WATCH, TAKING CREDIT FOR BANKRUPTCY: CAMPAIGN CONTRIBUTIONS FROM THE CREDIT INDUSTRY TO CO-SPONSORS OF THE BANKRUPTCY "REFORM" BILL, 6-7 (1982).

77. *Id.* at 2.

78. Purdue University Credit Research Center, *Consumer Bankruptcy Study* (1982) [hereinafter cited as the *Johnson Study*].

that such a suspicion would be “based on a false premise that what is good for the industry is bad for consumers and vice versa,” whereas, in the competitive consumer credit industry, all that is involved is a trade-off between one group of consumers and another, so that a study biased in favor of the industry would be impossible.⁷⁹ This does not quite achieve the hubris of the General Motors Corporation president who assured us some time ago that what was good for General Motors was good for the country, but it comes close.

Johnson’s job was to predict how many of his sampled bankrupts could have paid off all or a substantial part of their existing debts out of future earnings. Obviously, what he needed was information about probable future income, living expenses, and present debt loads. What he produced does not inspire great confidence in his study.

Twenty-five percent of those filing a single petition in his study were unemployed at the time of filing and only 22% of both spouses filing a joint petition were employed at the time of filing.⁸⁰ But over 75% of those who were employed had been employed continuously for the previous year and most of them expected, when interviewed in early 1981, that their income would remain the same or increase for the balance of 1981.⁸¹ Johnson’s study assumes that their income would remain at the present level for the next five years. Facts have not borne out that assumption. Unemployment had risen from 7.2%, when Johnson’s interviewing was completed, to a peak of 10.8% in December 1982, and there is dispute among the experts as to whether a slight decline to 10.3% in March 1983⁸² is due only to more people dropping out of the labor force or means that the “recession” is ended. But many would agree that if unemployment rises to 12% we will have moved from “recession” to “depression.”⁸³ It is estimated that most of the 11.4 million unemployed and their families—as many as 25 million people—have also lost their health insurance,⁸⁴ and, for many of the unemployed, unemployment insurance is running out. For those still employed, many major labor unions are making financial concessions on compensation for financially distressed employers whose profits have been on an almost steady decline from 16% on capital in 1964 to 9.5% in 1982, and whose factories are operating at an average of 69.8% of capacity, the

79. *Id.*, vol. 1, at vi.

80. *Id.* at 33.

81. *Id.* at 34.

82. Wall St. J., Mar. 7, 1983, at 4, col. 1; *id.*, Mar. 7, 1983, at 1, col. 6; *id.*, Mar. 11, 1983, at 3, col. 1; *id.*, Apr. 4, 1983, at 4, col. 2.

83. *Id.*, Dec. 31, 1982, at 1, col. 1.

84. N.Y. Times, Mar. 7, 1983, at 1, col. 2.

lowest annual rate in the thirty-four years that such statistics have been kept.⁸⁵ Home mortgage foreclosures hit a thirty year high in the fourth quarter of 1982.⁸⁶ Many of the foreclosures are on the properties of farmers, whose debt has nearly doubled in the last four years and whose income is down.⁸⁷ No one knows how many of Johnson's sample are covered by these statistics, but no matter: he has assumed that they will enjoy into 1986 the income they were receiving in early 1981.⁸⁸

As for living expenses, Johnson turned to a standard fixed by the Census Bureau in 1979 for identifying those whom we normally regard as needing help: those living at the poverty level, which was \$9,159 for a family of four. With some slight adjustments for child care expense, child support, and current medical expenses, Johnson assumed also that, for the next five years, those in his sample would live at that level.⁸⁹

Finally, in measuring existing debt levels of those in his sample, all debts secured by real estate other than homes were excluded entirely. This was on the assumption that the debtors needed no bankruptcy relief for such debt; they could simply default on the mortgage and allow the mortgagee to foreclose, which "generally should provide adequate funds to repay those debts."⁹⁰ No matter that this real estate may be property in which the debtor is entitled to an exemption as part of this fresh start; the mortgage debt is still to be liquidated by foreclosure. Similarly excluded for the same reason were all business debts "which typically are secured by the assets of the business"⁹¹ although, as any bankruptcy judge or practitioner can tell us, business debts are typically *under*secured by business assets at the time of bankruptcy, leaving the debtor with an excess personal liability. In any event, the debts that Johnson tells us the debtors can repay are only consumer debts, not including those consumer debts secured by real estate unless the real estate is the debtor's home.

How much of this selected list of debts could Johnson's sample of debtors have paid if held to the poverty level for five years but bolstered by his assumption that they would suffer no decline in income during that time? Twenty-nine percent of them could pay 100% of those debts, and another 8% could pay over 50%.⁹²

85. *Id.*, Mar. 28, 1983, at 1, col. 3; Wall St. J., Jan. 18, 1983, at 3, col. 1.

86. Wall St. J., Feb. 24, 1983, at 2, col. 3.

87. N.Y. Times, Mar. 4, 1983, at D1, col. 3.

88. *Johnson Study*, *supra* note 78, vol. 1, at 45-46.

89. *Id.* at 51-54.

90. *Id.* at 55.

91. *Id.*

92. *Id.* at 59.

But, in each of its important calculations and projections—future income, living expenses, and debts to be repaid—Johnson's study contains distortions, each of which seems "good" for the consumer credit industry and "bad" for the consumer. It is difficult to extract the comfort Johnson does⁹³ from the fact that, since 52% of his sample were already at the poverty level or below it, they would pass the "threshold test," leaving only 48% who, if reduced to the poverty level for five years, could pay all or some part of their debts.

Despite the defects of his study, Johnson could have learned more from it than he apparently did. He asked his interviewees about the causes of their resort to bankruptcy and reported that the most important reported causes were use of too much credit, marital problems, and loss of employment. But he takes no note of the fact that 28% of his interviewees reported that "credit was too easy to get."⁹⁴ That observation is borne out by a recent study of 260 federal credit unions by the National Credit Union Administration which reports that for over one-half of all charged-off loans, the credit unions had not even bothered to obtain a credit report on the borrower before making the loan.⁹⁵ Consumer credit is too easy to get. Like the federal credit unions, too many private consumer credit extenders make no decent credit check, relying instead on volume and tax deductions for credit losses.⁹⁶ These improvident credit extenders not only get unsophisticated debtors into trouble by overloading them with debt, but also jeopardize the loans made earlier to the same debtors by prudent credit extenders. That is why I tried, but without success, to persuade Congress to include in the new Bankruptcy Code provisions for disallowance of improvident credit extensions.⁹⁷

The Johnson study and the Credit Union study share one more distortion that is a part of the consumer credit industry's campaign in the halls of Congress. They treat debts discharged in bankruptcy as "bankruptcy losses"⁹⁸ on the assumption that it was the bankruptcy discharge that caused the loss. But the real cause of the loss was the financial difficulty that led the debtor to resort to bankruptcy. If the debtor had been com-

93. *Id.* at 59, 65.

94. *Id.*, vol. 2, at 35-36.

95. National Credit Union Administration, *The Report on the Special Bankruptcy Profile Survey*, 5, 27 (Sept. 1981) [hereinafter cited as *Credit Union Study*].

96. See Countryman, *Improvident Credit Extension: A Legal Concept Aborning?*, 27 ME. L. REV. 1 (1975); Countryman, *The Diminishing Right of Privacy: The Personal Dossier and the Computer*, 49 TEX. L. REV. 837, 839-46 (1971).

97. *Hearings Before the Subcomm. on Improvements in Judicial Machinery of Senate Judiciary Comm. on S. 235, S. 236, S. 582 & S. 2957*, 94th Cong., 2d Sess. 4 (1975).

98. *Johnson Study*, *supra* note 78, vol. 1, at 93; *Credit Union Study*, *supra* note 95, at 18.

pletely barred from bankruptcy and had received no discharge, although his or her own life would have been made much more miserable, the industry would still have suffered most of the same loss. Indeed, since the Johnson study estimates that, even if Congress were to adopt the industry's proposal to sequester the debtor's income and pin him or her to the poverty level for five years, the industry would collect only 25% of its claims,⁹⁹ it is obvious that most of the losses are not "bankruptcy losses."

In any event, what the industry offers by way of amendment to the Bankruptcy Code was embodied in H.R. 4786 and S. 2000 in the 97th Congress, where S. 2000 was reported out by the Senate Judiciary Committee.¹⁰⁰ In the 98th Congress, the industry proposal is embodied in H.R. 1169, introduced by Congresswoman Marilyn Lloyd of Tennessee, and S.445, introduced again by Senator Dole. Essentially, the proposal is the same proposal the industry was pushing in the early 1960s.¹⁰¹ That is the basis of one of the principal arguments behind the proposal: that the new Bankruptcy Code is so overly generous to consumers with exemptions, discharges, and other features that consumer filings are skyrocketing.¹⁰² Total bankruptcy filings are skyrocketing and consumer filings account for more than 80% of the total. From a former peak of 254,484 filings in 1975, total cases filed were 331,098 in 1980, 363,847 in 1981, and 380,212 in 1982.¹⁰³ But, while consumer filings increased 10% in 1981 and decreased by 1.5% in 1982, business filings increased by 10% and 43%. It is the state of the economy, and not the coddling of consumers, that has caused the increase in bankruptcy filings.

Many of us, perhaps most of us, who have considered the problem, believe that our treatment of financially distressed debtors has grown more humane in the past three centuries and that the change in their treatment is an improvement. But not the consumer credit industry. That industry is

99. *Johnson Study*, *supra* note 78, vol. 1, at 90.

100. S. REP. NO. 446, 97th Cong., 2d Sess. (1982).

101. There is also H.R. 1800, introduced by Congressman Michael Synar of Oklahoma and endorsed by, among others, Congressman Barney Frank of Massachusetts, one of my erstwhile favorite Congressmen. This bill would take the shotgun approach and authorize the bankruptcy court, on its own motion, to dismiss a consumer's petition if the court determines that the debtor "does not need the provisions of the chapter under which relief has been sought and the granting of relief under such chapter would be a substantial abuse of the provisions of such chapter."

102. A recent and careful study of cases filed under the new Bankruptcy Code, both in states which have "opted out" of the exemption choice given by the Code and in those which have not, concludes that there is no correlation between filings and the generosity of available exemption laws. Woodward & Woodward, *Exemption as An Incentive to Voluntary Bankruptcy: An Empirical Study*, 57 AM. BANKR. L.J. 53 (1983).

103. Statistics supplied by the Administrative Office of the United States Courts.

proposing what it was proposing before the new Bankruptcy Code was adopted: a modest proposal for a return to the indentured servant device of seventeenth-century colonial days—or at least to the post-Civil War peonage practice—along with a severe restriction on the availability of the voluntary petition introduced in this country in 1841 and the free bankruptcy discharge for the protection of future earnings introduced in 1867. It is a proposal for indentured service on a grand scale, for mass peonage, with the federal bankruptcy courts providing free collection services for the consumer credit industry.

True, the proposal's draftsmen have tried to save it from the thirteenth amendment. Any debtor seeking relief under the Bankruptcy Code who fails to pass the "threshold test" on the debtor's ability to pay debts from future earnings is not told that involuntary servitude must be entered into. He is merely told that that is the only form of remedy available to him under the Bankruptcy Code. That artifice should not, in my judgment, save the proposal from thirteenth amendment challenge. Neither, in my judgment, should the proposal escape challenge under the due process clause of the fifth amendment because of its blatant discrimination. The owners of corporations are not required to keep their businesses in operation for an additional five-year period, and to live at the poverty level during that period, in an effort to pay off existing business debts. Only individuals—the owners of sole proprietorships and others directly dependent on their own earnings—are to be subjected to the five-year period of bondage. But, preferable to any attempt to invalidate the industry's proposal under the Constitution would be its defeat in Congress. And it should be defeated in Congress. In a country which has abolished slavery and involuntary servitude, has largely abolished imprisonment for debt, and has long provided a "fresh start" for financially distressed debtors, the industry's proposal is, as was said by a witness opposing the conditional and suspended discharge proposals fifty years ago, "contrary to the genius of our institutions."¹⁰⁴

104. *Joint Hearings, supra* note 70, at 641.

