May 17, 1999

MEMORANDUM FOR HILLARY RODHAM CLINTON

FROM:	NICOLE RABNER
CC:	MELANNE VERVEER
SUBJECT:	BANKRUPTCY REFORM

Tomorrow morning, Melanne and I participating in a meeting with the President's advisors on bankruptcy reform legislative strategy. The President's advisors are in the process of devising a plan for the bill's likely movement to the Senate floor next week. Attached please find a very preliminary draft of a strategy memorandum for the President – its bleak outlook underscores the pessimism of the President's advisors about our leverage at this stage.

If your schedule permits, we recommend that you hold a very brief conference call or meeting with President's advisors on this issue (Gene Sperling, Larry Stein, Maria Escheveste and Sarah Rosen). The purpose of the call would be to brief you on our strategy. We believe it would be helpful for you to ask for a report on our proactive strategy to influence and improve the bill before it reaches the President's desk.

VERY PRELIMINARY DRAFT MEMORANDUM FOR THE PRESIDENT

ACTION FORCING EVENT: On April 6, 1999, we wrote to you recommending a strategy to deal with Bankruptcy legislation moving through both chambers in Congress. The goal was to increase our leverage and reduce the likelihood of a veto override. We have made little progress, however, in the face of an extraordinary campaign by the credit industry. The House recently passed a bill that is still fundamentally flawed. Nonetheless, it passed by a vote of 313 - 108 (with fewer votes in opposition than last year's Conference Report). We anticipate that an only slightly better bill will pass in the Senate by a similar veto-proof margin, making exercise of the veto a futile gesture that will only highlight weakness.

RECOMMENDATION: Given this prognosis, your advisors recommend a new strategy designed to achieve very modest improvements that would allow you to reluctantly sign the bill, while expressing concern about the impact of the legislation. Specifically, we propose to:

(1) develop a tactical amendment to be offered on the Senate floor that would give the court discretion to consider the special circumstances of sympathetic debtors, e.g., those who care for non-dependent elderly or children, who are protecting themselves or their families from domestic violence, or who are trying to move from welfare to work;

(2) work with Democratic supporters of both House and Senate legislation in an effort to win their help in obtaining modest changes;

(3) adjust the tone of Administration statements about the pending Senate bankruptcy bill, showing greater favor for this slightly better bill in hopes of increasing the chances that its more reasonable provisions will prevail in Conference; and

(4) recommend that you sign the bill that comes to your desk, while expressing concern that its provisions will hurt low- and moderate-income families struggling to make a fresh start and making the case for further scrutiny of the bill's impact and reconsideration of its provision if harm is found.

BACKGROUND: In April, we proposed a strategy to:

(1) exploit publicly the vulnerabilities of the legislation (by presenting sympathetic scenarios of debtors denied access to a fresh start under the bill, attacking provisions in the bill that roll back existing protections against abusive and coercive collection practices, highlighting the bill's failure to improve disclosure and stem credit card abuses, and critiquing lingering danger it presents to child support and alimony collection);

(2) work with bill proponents and opponents (including Senators Torricelli and Grassley and Representative Nadler) to advance alternative provisions that would substantively improve the current bills;

(3) work with Representatives Nadler, Conyers, Frank, Gephardt, and Bonior to produce a more palatable House bill, or, if that is not possible, to garner the 20-25 additional House votes necessary to sustain your veto; and

(4) work with Senators Durbin, Kennedy, Leahy and others to develop a Senate floor strategy and identify message amendments which could motivate Republicans to compromise.

Thus far, the effort has been unsuccessful. Representative Nadler began the debate by offering an alternative that was to the left of the Senate bill last year. We convinced him that a different strategy was necessary – that the Democrats should instead offer an amendment that made only a limited list of targeted changes necessary to win the President's support. Minority Leader Gephardt, who last year voted for the Conference Report, agreed to support this strategy. He issued a statement indicating his opposition to the Judiciary Committee print and support for the Democratic alternative. However, it appears that the nature of the alternative was largely irrelevant in the face of an extraordinary lobbying campaign by creditors reminiscent of major tax legislation. The Democratic alternative received votes from __ Democrats, but only ___ were willing to oppose the underlying bill after the alternative failed. [Stats to come.]

The poor showing of the Democratic alternative in the House bodes badly for the Senate debate scheduled for the week of May 17th or May 24th. In extensive discussions with numerous Senate members and their staff, we find little willingness to advance changes to the complex means test and reaffirmation provisions that need revision. They are interested in advancing "message" amendments (e.g., a Schumer amendment to make nondischargeable in bankruptcy judgements for violation of the Freedom of Access to Clinics Act) or limited technical changes sought by narrow constituencies (e.g., credit counselors). In any event, few Democratic amendments are likely to succeed; and the majority of Democrats appear prepared to vote for the bill on final passage provided they have an opportunity to offer their amendments. If the Majority Leader takes procedural steps to limit debate in the face of Minimum Wage or Patients' Bill of Rights amendments, Democrats may oppose cloture as a party rights matter; however, a time agreement for consideration of Democratic amendments is likely to be reached.

The advocates fighting against the current bill – largely consumer groups and women's organizations – continue to press the Administration to hold firm, either to exact significant concessions from the industry or to veto the bill. They argue that the creditor industry fears a veto and the negative publicity that would follow and that the Senate Democrats sponsoring last year's promising Senate bill will be strong on the floor. Finally, the advocates remember the rhetorical strength of you and the First Lady from last year and see Administration pressure as significant. The advocates have a more optimistic view than most of your advisors of our leverage at this stage. Unfortunately, they have been severely outspent and outnumbered by the bill's formidable lobbyists – congressional staff report that they have not even been a presence on the Hill.

In light of our limited leverage, the best possible outcome would be further modest changes to the Senate bill, with key provisions from the Senate version prevailing in conference. To that end, we will find a sponsor for an amendment that will be hard to oppose. This amendment would give the court discretion to consider the special circumstances of those who care for non-dependent elderly or children, who are protecting themselves or their families from domestic violence, or who are trying to move from welfare to work. Our greatest concern with these bills has been that they provide bankruptcy judges inadequate discretion to consider the unique circumstances of individual debtors. As we have been unable to argue compellingly for judicial discretion, we will propose that they provide discretion in specific cases where the strict application of the rigid means test formula would impose clear hardship.

We also will work with Democratic supporters of both House and Senate legislation in an effort to win their help in obtaining modest changes that will allow the Administration to demonstrate that we obtained concessions. We will craft a more balanced Statement of Administration Policy on the Senate bill when it comes to the floor – a statement less critical than others that we have issues thus far. We need to show favor toward the Senate proposal in hopes that its slightly more modest provisions will prevail in conference. Finally, we will begin to lay the groundwork for a signing statement that expresses your concern about the adverse impact of this legislation on some debtors and their families. In signing the legislation, you may wish to direct the Departments of Justice and Treasury to undertake studies of the bill's impact so that, if adverse implications are found, you can advance limited proposals to remedy the harm in the future.

_____ **Agree** _____ **Disagree** _____ **Let's Discuss**

Summary of Hyde Amendments

The amendments that Chairman Hyde offered during the House Judiciary Committee's mark-up of H.R. 833 address in part the Administration's concerns about the lack of balance in H.R. 833. Specifically, the Hyde amendments:

- Substitute standards to be drafted by the Justice Department in place of H.R. 833's use of IRS standards in the bill's means test to determine a debtor's expenses and eligibility for Chapter 7 relief. (Sens. Grassley and Torricelli recently wrote Secretary Rubin asking for Treasury to assist in the modification of IRS standards so they would be suitable; so this provision is within the mainstream.)

- Include a presumption that debtors with income below the median income level are <u>not</u> abusing the bankruptcy system in filing under chapter 7. Debtors below this income level have little repayment capacity and therefore almost no chance of successfully completing a chapter 13 repayment plan. This common-sense provision goes a long way toward addressing the Administration's concerns about reducing the cost of administering the means-test bankruptcy for the courts, the trustees, and the debtors.

- Substitute a straightforward test that debtors with the ability to repay a total of $6,000 over 60 months, or $100/month, would be presumed to be abusing the bankruptcy system by filing under chapter 7. This test would replace the test in H.R. 833 that debtors with $5000 in net income over 5 years, or the ability to pay 25 percent of their general unsecured indebtedness over the same period, would face the presumption. Very preliminary Treasury estimates suggest that this change would noticeably reduce the number of debtors affected by the means test, because those with low dollar repayment capacities (who were caught by the 25% provision) would be dropped. These debtors are disproportionately low- and moderate-income. The Hyde amendments also include estimated administrative expenses of 10 percent and reasonable legal fees in the calculation of the debtor's repayment capacity.

An important clarifying edit that is critical for Administration support of the amendment:

- The Hyde amendment means test provides that a debtor's monthly expenses shall be those "reasonably necessary" for the maintenance or support of the debtor, the spouse of the debtor, and dependents of the debtor, and, if the debtor is engaged in business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business. This is the standard currently applied in Chapter 13. However, debtors who are subjected to motions to convert to Chapter 13 must demonstrate "extraordinary" circumstances that make adjustments to income or expenses "necessary and reasonable." We believe that these terms should be deleted to reduce confusion regarding the appropriate standard; for example, creditor motions that require "extraordinary" circumstances to overcome would have the effect of undoing the appropriate Trustee discretion in deciding not to submit a motion.

Additional changes that the Administration would like to see in the Hyde amendment:

- The amendment should clearly include discretion for courts to dismiss filings in bad faith and based on the totality of circumstances.

- The means test should be further modified to reduce administrative costs without reducing repayment capacity. Specifically, debtors with incomes between 100% and 150% of median should be subjected to a preliminary "screen" based on formulaic expenses only; most of them will fail this test, and so would certainly fail a full (and more costly) means test that included a detailed review of additional expense categories.

- The specific time period and threshold ($6,000 repayment capacity over five years) may not provide the most appropriate standard for Chapter 13 referrals. Previously, the Administration has supported a three-year window for calculating repayment capacity. However, the Hyde Amendment is based on capacity to repay $100/month; changing the standard to $3,600 repayment capacity over three years would probably have little effect on the debtors captured by the test.

Talking Points on HR 833, Bankruptcy Reform Bill

- The Administration has issued a veto threat on this bill. If it passes with a veto-proof margin, we have no leverage to get a better bill in conference. We need you to oppose it.

- The Administration wants bankruptcy reform. As part of reform, debtors who can repay a significant part of their debts should be required to do so. The problem with the current bill is that it lacks balance in addressing debtor and creditor abuses in bankruptcy.

- We want you to join us in supporting the Nadler/Conyers/Meehan "Democratic alternative" amendment. This amendment sticks with the basic framework of the bill, but includes specific changes that give balance and fairness to the bill. In fact, the amendment represents a limited list of narrowly tailored changes to the Judiciary Committee report -- changes that are necessary to win our support.

- The biggest problem in the bill is that it includes an unfair and rigid "means test" for determining access to Chapter 7 and the discharge of debts in bankruptcy.

  - First, the bill uses IRS expense formulas to determine a debtor's repayment ability. These standards were created for tax collection, not bankruptcy, and are not appropriate for bankruptcy purposes.

  - Second, the bill proposes to use the IRS standards rigidly, with exceptions for "extraordinary" cases only. But the IRS only uses the standards as rough guidelines, because many households have unusual circumstances. There is no reason to apply standards for collection of credit card debt more rigidly than standards for collection of tax debt and other priority debt.

- Hyde and Conyers are also offering an amendment that addresses these problems with the bill's means test. They have a "Dear Colleague" letter that makes the same points. We urge you to support this amendment.

- The Democratic alternative amendment addresses the Administration's other major concerns with the bill, which must be addressed for the President to support the bill.

  - The bill places the payment of high-priority debts like child support and alimony at risk after bankruptcy, by reducing the debts that can be discharged in bankruptcy. For example, the bill would make broad new categories of credit card debt nondischargeable.

  - The bill does not address clear evidence of creditor abuses in bankruptcy. For example, there is much evidence of coercive and misleading reaffirmations of unsecured debts and low-value secured debts in bankruptcy.

- The amendment also includes new credit card disclosures, for example of teaser rates and of the implications of making minimum payments, that consumers need to manage their credit card debts effectively.

Amendment to S. 625 to Protect Debtors with Special Expenses

In Section 102(a)—

At the end of proposed subsection 707(b)(2)(A)(ii), insert the following:

"The expenses shall include, if applicable, the debtor's actual expenses incurred—

"(a) to maintain the debtor and his or her family safe from domestic violence as identified under applicable federal laws"

"(b) by a debtor who is receiving or has received payments under the Temporary Assistance for Needy Families, applicable state welfare assistance laws, unemployment insurance, or the Social Security Act as amended, and is attempting to obtain and maintain employment"

"(c) for care and support of a household member or member of the debtor's immediate family (including parents, grandparents, and siblings of the debtor, the dependents of the debtor, and the spouse of the debtor in a joint case) that is not a dependent, not exceeding two times the poverty threshold published by the Census for the current year"

["(d) for care and support of foster children that exceeds reimbursements under applicable state and federal law, or associated with an ongoing adoption."]

MEMORANDUM

TO: Larry Stein

FROM: Joel Wiginton

Date: May 17, 1999

RE: **Where the Key Senators are on the Bankruptcy Issue**

General Background

As you know, there are now two competing bills in the Senate: S. 625, the Grassley-Torricelli bill; and S. 945, the Durbin bill (this is S. 1301, the Grassley-Durbin bill as passed by the Senate last Congress). S. 625 currently has five Democratic cosponsors: Sens. Biden, Johnson, Breaux, Bob Kerrey, and Robb. The Durbin bill has four Democratic cosponsors: Leahy, Sarbanes, Kennedy, and Feingold.

Given this backdrop, here is a brief run down of where the key Senators are on the bankruptcy issue (based on information supplied by their staffs).

The Republicans

Grassley: Sen. Grassley has always been more reasonable than many of his colleagues on this issue. Continuing that stance, his staff has shown some interest in dealing with us on our means-test proposal. Although he may be willing to negotiate on other matters as well, this will probably not occur unless he feels that there will be 34 Democrats voting against his bill.

Hatch: Although Sen. Hatch has generally been very conservative on these issues, his staff has at least been quite up front. Sen. Hatch may be willing to negotiate "to some degree" on our means-test and reaffirmations proposals but will not move on the cram-down and the nondischargeable debt issues. Although Sen. Hatch's rhetoric notes that he is not worried about a veto, his staff strongly implied that they would like to avoid this if at all possible. In doing so, his the staff also implied that we could get some "reasonable" changes but would then have to affirmatively support the bill. This is definitely an avenue we should explore (Treasury sent Hatch's staff proposed language on Friday), but in the end Sen. Hatch is unlikely to move too far.

The Democrats

Durbin: Sen. Durbin is ready for a fight. He is reportedly quite displeased by the efforts of Sen. Torricelli and will try and remedy this on the floor. He is likely to pressure the White House to come out with a strong veto threat.

Torricelli: Although Torricelli sent a letter to Sen. Grassley outlining six major improvements he needed in the bill to support it, there is little evidence that he is ready to vote against the bill if these improvements are not achieved. Indeed, he did not offer any meaningful amendments in Committee and currently only plans on offering an omnibus consumer protection amendment on the floor. He may, however, also offer the "Hyde amendment." In addition, on Friday his staff presented Sen. Grassley with the improvements he needed to see in the Manager's mark. No word on Sen. Grassley's response to those demands.

Leahy: Sen. Leahy will likely be much more involved this year. He will primarily focus on getting consumer protections and financial privacy in the bill. It would be quite helpful to our efforts if he decides to be a real player on this matter. He voted against the Grassley-Torricelli bill in Committee.

Kennedy: Sen. Kennedy - as he was last year - will likely be very far to the left on this issue (i.e., he would probably prefer that there be no bill at all). That being said, he signed on as a cosponsor to the Durbin bill, because he thought it was politically necessary. He has said that he will most likely offer Patients Bill of Rights or Minimum Wage as amendments on the floor. It would also be beneficial if we can get him to do a more technical bankruptcy amendment such as reaffirmations. He voted against the Grassley-Torricelli bill in Committee.

Kohl: Sen. Kohl is fairly centrist on bankruptcy. His staff notes, however, that he is disappointed that the homestead exemption provision (he added this with an amendment in Subcommittee last year) and the consumer credit protections are not in the bill. He will, therefore, offer a homestead exemption amendment on the floor (which will pass). He may also offer an amendment on cram-downs. In the end, however, he will likely vote for the Grassley-Torricelli bill. He voted for the Grassley-Torricelli bill in Committee.

Feingold: Sen. Feingold is just like Kennedy on this issue. He too was originally reluctant to cosponsor the Durbin bill, because he believes it is too centrist. He will offer a number of amendments on the floor dealing primarily with the access to justice restraints in the bill. He voted against the Grassley-Torricelli bill in Committee.

Schumer: Sen. Schumer may carry a great deal of water for us on this issue on the floor. He is currently likely to offer a version of our means-test proposal and is considering offering our reaffirmations proposal. He is also offering an amendment that would make damages awarded under the FACE Act nondischargeable. We sent a letter through the DoJ in support of this amendment last week. He voted against the Grassley-Torricelli bill in Committee.

Sarbanes: Although Sen. Sarbanes has cosponsored the Durbin bill, he has noted that he will not be very involved in the debate beyond those issues that would fall within the jurisdiction of the Banking Committee (i.e., the TILA and financial privacy issues). He will almost certainly, however, offer or cosponsor amendments on these matters on the floor.

Dobb: Sen. Dobb was very involved in this issue last year, because he was quite concerned about the impact of the legislation on women and children. Up to this point, he has been relatively silent but may offer an amendment remedying the remaining women and children problems on the floor. His staff has also shown some interest in our reaffirmations proposal.

Jack Reed: Like Sen. Dobb, Sen. Reed was very active on this issue last Congress but has not engaged as of yet this year. His staff has shown some interest in offering credit card consumer protection amendments on the floor and may also consider offering a means-test discretion amendment.

Column on Bankruptcy Reform
OUTLINE SUGGESTION

I. Lead such as "If you had told me a few months ago that I would write a column agreeing with Chairman of the House Judiciary Committee Henry Hyde, I wouldn't have believed it.

II. Open with bankruptcy reform and how some reform is in order – with the proliferation of bankruptcy filings over the past years.

III. Talk about how this bill has serious flaws that need to be addressed (see SAP). Something like, "I find myself thinking about those who this bill would hurt and those it would let off scot-free."

IV. Who this bill would hurt. Debtors in the following scenarios:

   A. Imagine a couple who takes care of his elderly mother. Although she receives Social Security and is not technically a dependent of her son, she relies heavily on the financial support her son provides, enabling her to stay in her small apartment.
   B. Imagine a woman who has been the victim of domestic violence and who is incurring unplanned expenses for a security system for her home, added transportation costs (had to move out of the house and now commutes further to work), or attorneys fees for a restraining order.
   C. Imagine a laid-off steel worker or an out-of-work farmer who is trying to get a better job and is enrolled in a job-training program to learn a new skill and advance.
   D. Imagine a couple who has been waiting years for an adoption to go through and incurs significant one-time expenses relating to that adoption, such as legal fees or transportation.

V. This bill could hurt these people because the new bankruptcy rules that these bills would create would mean that if any of these people found themselves seeking bankruptcy, the system would not be able to take into account any of their individual compelling circumstances in determining how much the debtor must repay. Background: the Means Test proposed in the pending House and Senate bills are rigid and use an IRS formula of expenses to determine how much a debtor can pay back to his/her creditors. These IRS standards were never meant to be used in this way (they were developed for tax-collecting purposes – rather they were meant to be used with significant discretion on the part of the IRS). Used in bankruptcy, they effectively determine how much a debtor is allowed to live on, while the balance of his/her income going to pay back debts, such as credit card debt. One of the problems with the rigid system is that because they don't take the *specific* circumstances of the debtor in mind and only tabulate certain allowable areas of expenses, they can be used to harm Americans who find themselves in unusual but sympathetic circumstances (see attachments for further discussion).

VI. Who this bill would not hurt.

A. Coercive creditors who scare debtors into reaffirming debt that they could otherwise discharge in bankruptcy (and the bill rolls back the only effective current remedy to these practices – class action suits, which help for instance to stop Sears)
B. Credit card companies who send out billions of credit card solicitation – they would not have to provide meaningful disclosure to consumers to ensure that they know what they are doing when they take on this debt. (i.e. the minimum payment disclosure requirement).
C. The rich -- who have loopholes to hide their wealth and protect it from creditors, by, for instance, buying a lavish home in certain states (see NYT opinion piece)

VII. Plea to fix the bill -- hopes that when this measure is taken up by the Senate that they show leadership and address these important concerns.

ONE MORE THOUGHT – I'M NOT SURE WHERE TO PUT THIS:
I think it's important that somewhere in here she also mention that the problems of child support and alimony collection, while narrowed since last year's bill, have not been entirely fixed.

This is a memo That went to The Pres (This is a draft but the substance didn't change - see The section on 'Exploit vulnerabilities' for Schumer

April 5, 1999

MEMORANDUM TO THE PRESIDENT

FROM: GENE SPERLING
LARRY STEIN
MELANNE VERVEER

RE: BANKRUPTCY REFORM STRATEGY

ACTION FORCING EVENT: Bankruptcy legislation is moving rapidly through the House and the Senate. Both chambers plan to complete committee action after recess and take floor action in May. Last year, we worked closely with Senator Durbin, resulting in a 97-1 Senate vote for a moderate and balanced bill. The moderating provisions were largely abandoned in Conference. Your advisors informed Congress that they would recommend a veto of the Conference Report. If the Senate had voted on the Conference Report, we do not know what the outcome would have been, but Senator Durbin threatened delay and bill lobbyists predicted Republican gains in the 1998 election and decided to wait. The House approved the Conference Report by a veto-proof vote of 300-125. Minority Leader Gephardt was among the 80 or so Democrats supporting the Conference Report.

This year, while Congressman Nadler is leading efforts against the Conference Report and working to enlist greater support for a more moderate approach, we expect the House to approve a bill like the Conference report by a similar margin. In the Senate, there seems to be less support than previously among Democrats for fighting unbalanced legislation. Absent a strong effort to influence the legislation, it is likely that you will be presented legislation that you will not want to sign, yet with sufficient support to override a veto.

RECOMMENDATION: We seek your approval of a strategy designed to increase our leverage and reduce the likelihood of a veto override. Specifically, we seek authority to: (1) exploit publicly the vulnerabilities of the legislation (by presenting sympathetic scenarios of debtors denied access to a fresh start under the bill, attacking provisions in the bill that roll back existing protections against abusive and coercive collection practices, highlighting the bill's failure improve disclosure and stem credit card abuses, and critiquing lingering danger it presents to child support and alimony collection); (2) work with bill proponents and opponents (including Senators Torricelli and Grassley and Representative Nadler) to advance alternative provisions that would substantively improve the current bills; (3) work with Senators Durbin, Kennedy, Leahy and others to develop a Senate floor strategy and identify message amendments which could motivate Republicans to compromise; and (4) work with Representatives Nadler, Conyers, Frank, Gephardt, and Bonior to produce a more palatable House bill, or, if that is not possible, to garner the 20-25 additional House votes necessary to sustain your veto.

THE STATUS OF BANKRUPTCY LEGISLATION IN CONGRESS

In the House, Representative Gekas, introduced H.R. 833, which is virtually identical to last year's Conference Report. It now has 93 cosponsors, including nearly 40 Democrats (*e.g.*, Representatives Boucher, Frost, Kennedy, Holden, Menendez, Roemer, Maloney, and Velazquez). Minority Leader Gephardt supported the conference report last year, and would likely do so again (albeit with a low profile). However, if a strong balanced alternative can be constructed that would give him and other House Democrats a viable pro-reform and pro-consumer bill to support and that has the strong public backing of the White House, Gephardt might be willing to rally his caucus vigorously around such a vehicle.

Representatives Conyers and Nadler recently wrote to you praising you and the First lady for your leadership last year and asking you to reiterate your opposition to last year's Conference Report. On March 23, 1999, Jack Lew sent a reply noting that your senior advisors had recommended a veto of the Conference Report last year and that "our position . . . has not changed." Armed with that letter and an alternative bill being developed by a group of bankruptcy experts at the National Bankruptcy Conference, Representative Nadler is confident (perhaps more than we are) that he can prevent some Democrats, who last year supported the Conference Report, from doing so this year. Doing so is critical to a credible veto threat.

In the Senate, we originally hoped that Senator Torricelli would not co-sponsor Senator Grassley's bill, modeled after the Conference Report, demonstrating to other Democrats that the bill was not ready for the caucus' support. Unfortunately, Senator Torricelli did agree to cosponsor S. 625, although extracted some moderating changes as a precondition of his sponsorship. He also wrote a letter to Senator Grassley outlining six areas where the bill needs to be improved before it leaves the Senate. Although we would like to see some other changes as well, we largely agree with the six areas that Torricelli outlined. (The First Lady urged Senator Torricelli to hold firm on these issues.) We are skeptical, however, that the Republicans will accept many of these amendments either in committee or on the floor. (Even if they did, as last year, we can expect any progress made to be undone in conference with the House.)

Senator Grassley is more reasonable on bankruptcy than many Republicans, but we do not believe that he will be able to hold off his colleagues who believe they can get Democratic support without further compromise. Senator Biden is already a co-sponsor and five or six other Democrats have expressed interest in signing on the bill. Senator Leahy also may support the bill in Committee as a demonstration of support for Senator Torricelli, who replaced Senator Durbin as ranking member on the relevant subcommittee. Many signs suggest that Senator Torricelli will not oppose the bill even if the additional changes he seeks are not made. Senator Daschle, who wants a bankruptcy reform bill, will likely support S. 625 in the end if enough Democrats move in that direction. Well positioned Democratic staff believe there may be enough votes in the Senate to override a Presidential veto.

Finally, last year, Banking Committee Chairman D'Amato raised no objection to provisions inserted on the Senate floor that required credit card companies to provide greater disclosure to consumers. These provisions were important to our support of the Senate bill. However, the new Banking Committee Chairman, Senator Gramm, recently noted his opposition to any bankruptcy bill which contains the credit card protections that we view as important. Senator Gramm has reportedly said that a bill with these consumer protections "will pass over [his] dead body."

At this time, neither the Administration nor effective advocates like Senator Kennedy have mounted any offensive. Thus, our assessment is preliminary and we hope to affect it. Some House and Senate Democrats are looking to the White House for political guidance and leadership on this issue. While they want to support bankruptcy legislation, we should be able to keep them from supporting the bills moving in each chamber if we give them a viable alternative and a strong rationale not to do so.

RECOMMENDED STRATEGY

While we believe that the current bills before Congress are sufficiently flawed as to merit continued opposition, we also believe that bankruptcy reform is not only desirable but necessary. Our goal is to gain sufficient leverage in the debate on Capitol Hill to make modest but important changes to the bills, so that we could recommend that you sign the resultant legislation. We recommend the four-prong strategy described below.

1. Exploit Vulnerabilities

It is difficult to rally Members or the public around complicated technical issues like nondischargeable debt and means test formulas. However, there are messages we can use to address each of our major areas of concern.

A. The Formulaic Means Test Will Block Efforts of Responsible Debtors to Get Back on Their Feet

One of our most significant concerns with the current bill is that the procedures established do not afford debtors a meaningful opportunity to have their specific circumstances evaluated and do not give the court the necessary discretion to take those circumstances into consideration. While it is difficult to defend judicial discretion, we can tell stories about sympathetic debtors who would be caught by the bill's rigid approach.

Under the bill, the bankruptcy trustee would determine whether a debtor can afford to repay some of their debts by looking at the debtors income, less certain standard allowances for food, clothing, transportation, and housing expenses rather than at what they actually spend for those items. There may be cases where the actual expenses are above the allowance amount for good reason, but the court can only provide an exception if the debtor meets the burden of proving that their circumstances " exceptional" and the additional expenses "necessary." So, for example:

* No exception likely would be made for a debtor who helped his non-dependent mother meet her expenses so that she could live on her own and stay out of a nursing home. That debtor could be denied access to Chapter 7's "fresh start" and the funds used to pay for his mother's housing expenses would instead go to pay off his credit cards.

* Similar problems arise especially in ethic and lower-income communities where neighbors, friends, and relatives often bear significant costs to help children, elderly, the disabled, the unemployed, and others who are not legally their dependants.

* No allowance likely would be made if a debtor's transportation expenses to get to work on the other side of the region are above the area allowance. The choice posed could be stark: (1) find a job closer to home (even if less likely to provide career advancement) to lower transportation costs and free up money to repay your creditors; or (2) fail to feed or cloth your children.

* No allowance likely would be made if the debtor's rental costs are higher than the area allowance, even thought her apartment allows her to live near to a relative who can safely watch the children after school. The current test could force that single mother to move her family from her home without an opportunity for individualized assessment of the tradeoffs.

In addition to these scenarios, we can make much of the false representation made by bill proponents that the bill no longer would impact below-median income debtors (who make up 80% of those in bankruptcy). All debtors would be subject to the new mean test; while creditors could only bring "abuse" motions against above-median income debtors, the bankruptcy courts and trustees would be required to apply the means test to all debtors.

B. The Bills Roll Back Existing Protections Against Abusive Collection Practices and Coercion.

In a famous, recent case, Sears was found to have harassed creditors into agreeing to repay debts that they no longer had -- having been discharged in bankruptcy. The court found that Sears had violated the "discharge injunction" and was liable for millions in damages to hundreds of thousands of debtors. Under the House bill, creditors could harass debtors to repay discharged debt with little fear of consequences, as class actions and punitive damages -- the tools that brought the Sears' practices to an end --

would be barred.

Another concern is the bills failure to deal with coerced reaffirmations of debt. Thousands of bankruptcy debtors each year agree to "reaffirm" one or more debts -- agreeing to pay it back even though they have the right to have the debt discharged in bankruptcy. We have no objection to letting debtors make an informed choice about whether to repay debts, but we see widespread evidence that decisions are not informed and creditors coerce debtors into reaffirming debts by threating to challenge the bankruptcy proceedings if they do not reaffirm, promising new credit lines in exchange for reaffirmation, and harassing collection efforts aimed at debtors ignorant of their rights. Provisions of these bills will create new opportunities for creditors to threaten and harass debtors.

In numerous cases, debtors "agree" to reaffirm debts even though they do not have sufficient income to pay their current expenses. While some may be optimistic, many more feel they have no choice when approached by a creditor threatening to challenge their bankruptcy. It would not be unusual to see a reaffirmation agreement, for example, where the debtor agrees to repay $1000 in order to get a $500 line of credit -- an effective interest rate of 200% on the new debt, even though far less expensive credit lines are now available even for those currently in bankruptcy. Even where a debtor makes an informed choice, ***reaffirming the debt may harm ex-spouses and children whose child support and alimony may not get paid because the reaffirmed debt is paid instead***.

The Bankruptcy Review Commission concluded that reaffirmations of unsecured debt should be banned outright. We proposed instead a "coercion" check -- a review by the bankruptcy court of any reaffirmation of unsecured debt to ensure that it was an informed choice in the best interest of the debtor and others. We will press this issue more visibly this year, while developing compromise alternatives that we could offer in final negotiations.

C. Consumer's Right-to-Know and Protection from Credit Card Abuse

Consumers are well aware of intense and misleading credit card marketing efforts. Last year's Senate bill contained a number of important credit card provisions including: (1) a requirement that credit card companies disclose on monthly statements how long it would take (and how much it would cost) if consumers only made the minimum payment; (2) a requirement that consumers be notified when credit card companies or retailers take a security interest in the goods purchased; and (3) a requirement that credit card companies inform debtors that they have not assessed the debtors' capacity to repay additional debt and provide a worksheet so that the debtor can easily make that calculation for themselves. Most of these provisions were stripped in conference, leaving only a requirement for the Federal Reserve to study what further disclosures would be helpful.

Legislation incorporating these provisions has been introduced in the Senate. In addition, Representative LaFalce and Senator Schumer have introduced bills that contain a host of additional credit card protections, many of which the Administration supports. One, for example, would eliminate the misleading advertising of "teaser" rates -- which leave consumers shocked by dramatic interest rate increases when rates expire or they incur a penalty for a minor late payment. You are scheduled to unveil a consumer financial protection package the week that Congress returns, which includes many of these credit card provisions, as well as privacy protections. At that time, you can praise the efforts of Democrats in both chambers to protect consumers against abusive credit card practices. While we will not make passage of any *specific* credit card provisions a precondition for bankruptcy support, some balance in this regard is essential. By raising the profile of credit card issues, you will increase the leverage of Democrats seeking to incorporate some of these provisions in the bankruptcy bill and give Democrats an issue around which they can rally.

D. Child Support and Alimony Collection

The bankruptcy bills create or expand categories of nondischargeable debts -- i.e., debts that can be collected after bankruptcy. Last year we argued that these new nondischargeable debts would impair the collection of child support and alimony. In response, the bills' proponents both narrowed the categories of new nondischargeable debts and added a host of provisions that genuinely make it easier for former spouses and custodial parents to collect child support and alimony from debtors in bankruptcy. As a result, the bills probably improve the collection of family support obligations more than it is harmed. However, two concerns remain; we can continue to argue credibly that child support and alimony collection is harmed *in some cases*.

The bills now provide that, in the supervised context of a bankruptcy plan, child support and alimony payments must be given the highest priority. However, under these bills, some debtors will have obligations to repay reaffirmed or newly nondischargeable debt. After the bankruptcy discharge, there is no court supervision or other mechanism to ensure that child support and alimony are paid first. The custodial parent or former spouse is unlikely to be as effective as the card company in collecting payment. Once these lower-priority payments are made, it is not practical to require the custodial parent or former spouse to go after the creditor to assert a claim on those payments.

The bills also raise another concern for the payment of child support and alimony. Iif debtors are forced into Chapter 13 who do not genuinely have the capacity to repay -- as we fear will occur under the current versions of the means test -- they will eventually return to Chapter 7 with a diminished ability to repay their nondischargeable debts -- in particular their child support and alimony -- because while under the plan, they devoted some of their assets to paying their other creditors.

E. The Bills Leave in Place Huge Loopholes for Wealthy Homeowners While Squeezing Low and Moderate Income Debtors in over Their Heads.

Some of the most famous cases of abusive bankruptcy filings involve celebrities who live in multimillion dollar mansions protected by "homestead exemptions" but walk away from other debts. State exemptions also protect such luxuries as race horses and silver spoons in Virginia. Yet, at the same time we are creating a system that will ask low and moderate income debtors to behave responsibly -- to pay back some of their debts if they can -- these bills leave in place the biggest loopholes used by the wealthy. (The House bill currently has a homestead exemption cap of $250,000 but we expect even that to be removed on the floor.)

2. <u>Try to Improve the Legislation</u>

While the Republicans are not presently receptive to significant changes, we must continue to work in good faith with Senators Torricelli and Grassley (and key House members) to make improvements to the bills where possible. On a few important issues, we may be able to offer compromises that will be more attractive to the credit industry than provisions that were in the Senate bill last year. For example, we think we can propose ways to make the means test more "self-executing," requiring judges to explain when they vary from formulaic standards and lowering the costs to creditors of bringing motions to keep debtors from using Chapter 7 when they could repay under Chapter 13. This proposal should address at least one of the creditors' concerns with the discretion that we insist be granted to the courts. While these proposals may not be embraced by the Republicans initially, we hope they will be considered in the "end game." More importantly, they will allow us to present a new "Administration proposal" around which Democrats can rally.

3. <u>Senate Strategy</u>

Senior staff will consult directly with key Democratic Senators -- especially Senators Durbin, Kennedy, and Leahy -- in developing a Senate floor strategy. If Senator Torricelli is unable to lead the caucus in demanding balance for these bills, Senators Durbin and Kennedy may be willing to do so. With them, we will identify the best amendments (both germane and non-germane) to offer on the floor to provide negotiating leverage.

4. <u>House Strategy</u>

Senior staff will work with Representatives Nadler, Conyers, and possibly Frank to try to develop an alternative for full Committee and floor consideration that will represent a balanced approach to bankruptcy reform. We will also seek to engage Minority Leader Gephardt and other House Democratic leaders who may view this year's debate as an opportunity to promote a strong, pro-consumer perspective. The ultimate goal will be either to greatly improve the House bill or, more likely, produce the necessary votes to sustain a possible veto in the House.

Special Expenses Not Included in House/Senate Bankruptcy Reform Means Test

Many debtors face unusual expenses that are essential for their well-being or for the well-being of those who depend on them. Debtors may incur certain expenses in the course of protecting themselves against domestic violence, or in overcoming barriers to the transition from welfare, disability, or unemployment to work and financial independence (for example, for expenses for job training, relocation, or special equipment). Many debtors provide support for family members to enable them to live in dignity, even when the family member lives apart and does not receive enough income to qualify as a dependent of the debtor. [Possible addition, though critics may argue that those in bankruptcy shouldn't be continuing these responsibilities: Debtors who adopt children incur one-time and ongoing expenses related to the adoption and care of the child.]

At-Risk Debtors

1. Victims of Domestic Violence

Debtors may incur certain expenses in the course of protecting themselves against domestic violence. These can include relocation expenses to move the debtor and his or her household away from the violent spouse, additional transportation expenses for the debtor to get to work from a new location or for the debtor to undertake work in a workplace location removed from the knowledge of or access by the violent spouse, the legal costs associated with getting and enforcing court protective orders, the costs associated with increasing the security of the debtor's own home, and income gaps associated with unavoidable absences from work due to the danger of being threatened or assaulted at the workplace. Federal law under the Temporary Assistance for Needy Families and Title IV of the Social Security Act as amended provide guidance to states for establishing methods of identifying individuals at risk for domestic violence. It is essential to recognize the additional expenses or gaps in income incurred by such debtors to protect themselves and their households.

2. Individuals Trying to Move from Welfare or Unemployment to Work

Debtors who are welfare recipients can incur certain expenses associated with overcoming barriers to obtaining and maintaining employment. These include education and training expenses to prepare themselves for a work situation, care of a dependent child or family member, additional transportation expenses, additional housing expenses in case the work situation demands relocation, and expenses associated with freeing themselves from substance abuse. Assisting debtors who have lost jobs to regain their financial stability and independence is also a vitally important "fresh start," with long-term benefits for creditors, taxpayers, and our economy. Just as in making a transition from welfare to work, such debtors may need to incur certain expenses in making the transition to financial independence and security, and the ability to repay their debts. For example, many debtors who have lost jobs need to retrain for new jobs, or need to develop new skills to improve their job prospects in their profession. In addition, debtors may incur other expenses associated with seeking new economic opportunities, such as additional transportation or housing expenses, or relocation expenses. These expenses must be allowed in order for the debtor to increase future income and ability to repay debts.

3. Caregivers and Providers for Non-Dependent Family Members

Many debtors provide support for elderly or disabled family members to enable them to live and thrive in the community, as there are many situations in which the family member does not receive enough income to do so. Often, if the family member receiving assistance lives independently, the financial assistance may not be large enough to make the family member a dependent of the debtor. Yet the payments may be essential to the family member's well-being, for example to provide home care or household goods that make institutionalization unnecessary.

[4. Foster Parents and Adoptive Parents

Debtors who adopt children incur one-time and ongoing expenses related to the adoption and care of the child. Debtors who care for a foster child in their homes often have expenses above the payments they receive for the support of these children. These are expenses necessary for the support of these children.]

Use of IRS Standards for the Means Test in S. 625

- **The Administration supports the development and use of fair and reasonable expense standards for bankruptcy that reduce the costs and improve the fairness of means testing.**

- **S. 625 currently requires the use of IRS Collection Standards for this purpose, but the standards are not meant to be used alone and without discretion.**
  - The Tax Code permits the IRS to compromise when the taxpayer makes an offer to settle unpaid tax debt for less than the full amount of the balance due.
  - The Internal Revenue Manual (IRM) provides further guidelines for revenue officers to determine whether an offer-in-compromise is adequate.
  - The IRM also explicitly supports discretionary application of the standards: it states that the IRS should avoid rejection of an offer solely based on a narrow evaluation of assets and income, and formulaic expenses.

- **Last year during its consideration of the IRS Restructuring and Reform Act, Pub. L. 105-206, Congress criticized the inflexible application of the IRS Collection Standards, even though the standards were applied with more discretion than in S. 625. Congress directed the IRS to further increase flexibility in applying the standards.**
  - The Reform Act requires that the Collection Standards must be used so that taxpayers entering into an offer-in-compromise have adequate means to provide for basic living expenses.
  - The IRS is explicitly required to consider the facts and circumstances of a particular taxpayer's case in determining whether the Standards are adequate for that taxpayer.
  - If the facts indicate that use of the Standards' expense allowances would be "inadequate under the circumstances," the taxpayer is not limited by the national or local expense formulas.
  - The Reform Act further authorizes the Treasury Secretary to prescribe additional guidelines for whether an offer-in-compromise is adequate and should be accepted, such as whether the taxpayer faces hardship or a substantial reduction in income (*e.g.*, due to job loss).
  - The Reform Act also requires the IRS to allow the taxpayer to appeal any rejection of such offer-in-compromise directly to the IRS Office of Appeals, whose role is to attempt to resolve disputes between the IRS and taxpayers without resort to expensive and time-consuming litigation. There is no parallel body with such discretion in bankruptcy.

- **Without comparable flexibility when applied in bankruptcy, the IRS Collection Standards are not well-suited to bankruptcy.**
  - The Joint Committee on Taxation expressed the sense of Congress that flexible application of the IRS Standards "enhances taxpayer compliance," encourages them "to meet their obligations and remain in the tax system," and thus improves the government's ability to collect tax debts when taxpayers default on payments.
  - The application of the IRS Standards in the means test in S. 625 only allows any flexibility if the debtor can prove "special" circumstances that make adjustment of income or expenses " necessary and reasonable."
  - This is more restrictive than the "inadequate under the circumstances" standard that Congress directed the IRS to use for every case of tax debt. Congress would correctly criticize the IRS

if it imposed inflexible, formulaic standards on taxpayers.

- Inflexible use of the IRS Standards ultimately will result in more unsuccessful Chapter 13 reorganization plans and ultimately greater costs both to the courts and to creditors.

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

May 5, 1999
(House)

STATEMENT OF ADMINISTRATION POLICY

(THIS STATEMENT HAS BEEN COORDINATED BY OMB WITH THE CONCERNED AGENCIES.)

H.R. 833 - Bankruptcy Reform Act of 1999
(Gekas (R) Pennsylvania and 106 cosponsors)

The Administration strongly opposes H.R. 833. If the bill were presented to the President in its current form, his senior advisers would recommend that he veto the bill. However, the Administration strongly supports the Democratic alternative offered by Representatives Nadler, Conyers, and Meehan, which would make a limited number of targeted changes to address the most significant problems with H.R. 833.

The Administration continues to support bankruptcy reform that asks both debtors and creditors to act more responsibly. However, H.R. 833 fails the test of balance between creditors and debtors. As currently drafted, many of the bill's provisions are unfair to middle- and low-income debtors; at the same time, the bill fails to close loopholes in current law that protect the wealthiest debtors. The bill focuses on perceived abuse of the bankruptcy system by debtors without adequately addressing abuses by creditors, and takes an excessively rigid approach to limiting access to discharge of debts under Chapter 7 of the Bankruptcy Code.

H.R. 833 in its current form would limit access to Chapter 7 to debtors who meet an inflexible and arbitrary means test. The Administration agrees that debtors who can repay a portion of their debt should not have access to Chapter 7. The Administration also agrees that some expense standards should be used to guide the determination of ability to repay, analogous to how expense standards are used by the Internal Revenue Service (IRS) to guide the collection of tax debt. However, H.R. 833 simply takes IRS expense standards, which were not developed for bankruptcy purposes, and applies them rigidly to determine ability to repay in bankruptcy. Under H.R. 833, a debtor whose ability to repay according to the IRS formulas was even $1 above the minimum threshold would have to demonstrate "extraordinary circumstances" in order to gain access to Chapter 7.

Representatives Hyde and Conyers will offer an amendment that also includes a means test but which would use expense standards that are tailored for bankruptcy purposes and that would allow bankruptcy judges limited and appropriate discretion in their application. The Administration could support the Hyde-Conyers amendment (provided that one technical and conforming change is made to make the language of the amendment internally consistent).

The Democratic alternative includes a means test very similar to the Hyde-Conyers amendment that would ensure that debtors who genuinely have the ability to repay a portion of their debts would remain responsible for those debts. Moreover, the Democratic alternative would significantly reduce the administrative and legal burden of means testing by limiting paperwork requirements on low-income debtors with little ability to repay.

The Democratic alternative also would address creditor abuses in bankruptcy, especially those abuses that place priority debt such as child support and alimony payments at risk. There is extensive evidence of coerced or abusive reaffirmations of unsecured debt and low-value secured debt. Such reaffirmations frequently are the result of misleading information or threats from creditors. Remarkably, H.R. 833 would ban class actions filed against creditors who violate reaffirmation requirements -- the mechanism that was effectively used to end abusive practices in important consumer protection cases. Rolling back an avenue of consumer redress for such significant creditor abuse is simply unacceptable.

Many bankruptcy experts have advocated either banning or severely curtailing such reaffirmations because they jeopardize both a debtor's "fresh start" and a debtor's ability to pay priority obligations. The Democratic alternative proposes more limited changes to help address this abuse. Reaffirmations of unsecured and low-valued secured debt would be subject to streamlined court review as part of the means-testing process. If the creditor provided certain easily-calculated disclosures about the financial implications of the reaffirmations (such as the effective annual percentage rate and the amount of any fees and penalties that could be applied), and if the means test suggested that the debtor truly could afford to repay all of his priority debts after taking on this additional obligation, then the reaffirmation would be presumed not to create undue hardship and to be fully understood by the debtor. In addition, those persons to whom the debtor owes child support or alimony obligations would have an opportunity to present evidence that the reaffirmation would place payment of their priority debt at risk.

The Administration also remains concerned about provisions in H.R. 833 that put additional credit card and other nonpriority debts in greater competition after bankruptcy with child support, alimony, and other societal priorities like educational loans and taxes. The Democratic alternative is consistent with the view of the Administration that caution should be exercised in the creation of additional types of nondischargeable credit card debt. H.R. 833 also eliminates virtually all "cramdowns" of secured debt to the actual value of the secured item in bankruptcy. While there are good reasons to limit the most dramatic cramdowns that occur for debts incurred close to bankruptcy, barring most cramdowns, as H.R. 833 would do, puts at risk repayment of other secured and priority debts.

The Administration continues to believe that reform must ensure that debtors are treated fairly and responsibly in the bankruptcy process, recognizing creditors' superior information and bargaining power. The Democratic alternative includes provisions adapted from H.R. 900, sponsored by Representative LaFalce, that would provide key information to consumers about credit card debt, including clear notice about the expiration of low "teaser" rates and the length of time to pay off a debt if only the minimum payment is made. Better information will help consumers avoid high debt burdens.

Finally, the Administration supports changes that would close loopholes in current bankruptcy law, such as those enabling unlimited homestead exemptions and exemptions from repayment requirements for individuals who are able to file for bankruptcy under Chapter 11, that protect some of the wealthiest debtors from having to repay a significant portion of their debt. Bankruptcy reform should not place a greater responsibility for debt repayment on moderate- and low-income debtors than it does on high-income debtors.

The Administration remains ready to work with the House to address these concerns, building on the responsible and balanced reform of the Nadler, Conyers, and Meehan Democratic alternative and the bipartisan approach of the Hyde-Conyers amendment.

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The New York Times

THE NEW YORK TIMES **EDITORIALS/LETTERS** SUNDAY, MAY 9, 1999

Editorial Observer/FLOYD NORRIS

Bankruptcy Reform That Spares the Wealthy

Watching a rich man stiff his creditors while walking away with millions can grate on people. Yet a gaping loophole in the bankruptcy laws routinely allows that to happen.

That loophole enabled such people as Martin A. Siegel, the former investment banker who was convicted of insider trading; Bowie Kuhn, the former baseball commissioner, and Burt Reynolds, the actor, to emerge from bankruptcy with ample assets — sometimes valued in the millions — even as their creditors suffered huge losses.

Last week, amid much rhetoric about how outrageous it was that people who could afford to pay some of their bills were able to walk away from all of them, the House of Representatives passed a bankruptcy reform bill. If enacted, the bill will make it much easier for creditors — particularly credit card companies — to collect money from bankrupts.

But while it will become harder to evade a few thousand dollars of credit card debt, it will not be any more difficult for millionaires to shelter their assets while declaring bankruptcy.

> The House helps a few lucky debtors go broke in style.

The wealthy can often stay millionaires because the laws in a handful of states — most notably Florida and Texas — set no limit on the value of a home that a bankrupt person can keep even as his debts are discharged by the court. So some people, as bankruptcy nears, sell their homes in states like New York and buy million-dollar homes, for cash, in Florida.

A fair bill would put a limit on the amount of home equity that could be protected from creditors. The Senate tried to do that last year, with a limit of $100,000, but that bill was killed. The House wants no limits on what state legislatures let the rich keep.

The House bill will make life harder for poor and middle-class people who file for bankruptcy. People whose income has been above the regional median income will be forced into plans requiring some repayment of debts, even if future income is likely to be less because the person has lost his previous job. The calculations regarding how much a person can afford to pay may not take into consideration his actual living costs. It is reasonable to try to force bankrupts to pay what they can afford, but this bill, with its lack of discretion for bankruptcy trustees and judges, is likely to bring unreasonable hardship for some.

This bill was pushed by the credit card companies, who worry that people abuse them by taking on credit card debts and then going broke. The companies already can challenge any bankruptcy on fraud grounds, but doing so costs money and may not seem to be worth it when only a few thousand dollars or less are at stake in any one filing. They hope that strict rules will enable them to force many more people to repay at least some money.

The 1990's have seen booms in bankruptcy filings — and in credit card issuance. Last year, 1.45 million people filed for bankruptcy, up 3 percent from 1997, while credit card companies sent out 3.4 billion card solicitations, a 15 percent increase. It would appear that rising bankruptcies have not yet caused lenders to grow more cautious.

One interesting feature of the House bill is that it requires the Government to pay for random audits of bankruptcy filings to see if people are cheating. Yet Congress will not spend money to let the Internal Revenue Service conduct random audits of tax returns. Protecting Visa's revenues would seem to be a higher priority than protecting those of the Government.

Two centuries ago, it was common for states to allow creditors to throw people into prison if they had not paid their debts. But even then, the creditor had to pay the state the cost of imprisoning the man. Now, if this bill passes, the taxpayers will foot the bill to force people to pay their debts.

Unless, of course, they are once-rich people who can afford to buy expensive houses in Texas or Florida. Those people are to be protected even as the Government cracks down on middle-class people who have fallen on hard times.

HR 833 and the Democratic Alternative: Bankruptcy Reform

The Democratic alternative (offered by Nadler, Conyers, and Meehan) makes ***a limited number of targeted changes*** to the House Judiciary Committee print that are necessary to achieve balance and fairness to low and moderate income debtors. The changes to the bill are:

Means Test: The Democratic alternative makes a few key changes to make the means test fair and less rigid.

- **Expense Standards Designed for Use in Bankruptcy:** H.R. 833 uses IRS expense formulas to determine a debtor's repayment ability. These standards were created for tax collection, not bankruptcy, and are not appropriate for bankruptcy purposes. The Democratic alternative would allow Treasury and the Executive Office of the U.S. Trustee to develop standards specifically for use in the bankruptcy context.
- **Limited Judicial Discretion.** Whatever the guidelines, I.R.S. experience shows that they should not be applied rigidly. H.R. 833 requires a showing of "extraordinary circumstances" and "necessary" expenses. The Democratic alternative would require that the expenses be only "reasonably necessary" allowing the court to determine whether a person truly has the capacity to repay.
- **Reducing Unnecessary Paperwork Burden and Unnecessary.** H.R. 833 requires that a complex means test analysis be performed on debtors even though a quick review could tell that they have no capacity to repay. The Democratic alternative would provide a streamlined process so that the paperwork and analysis is only done for those for whom there is some possibility they can repay under a Chapter 13 plan.

Limiting Coercive Reaffirmations: There is extensive evidence of coerced or abusive reaffirmations of unsecured debt and low-value secured debt. Such reaffirmations frequently are the result of misleading information or threats from creditors. H.R. 833 would ban class actions filed against creditors who violate reaffirmation requirements -- the mechanism that was effectively used to end abusive practices in important consumer protection cases. The Democratic alternative eliminates this rollback of existing consumer protections and would provide a streamlined process for reviewing if the creditor is making an informed choice and has the capacity to repay the reaffirmed debt.

Protecting Child Support and Alimony – Limiting New Nondischargeable Debts: H.R. 833 places the payment of high-priority debts like child support and alimony at risk after bankruptcy, by reducing the debts that can be discharged in bankruptcy. The Democratic alternative does not.

Balance – Responsibility for Creditors: H.R. 833 asks greater responsibility of debtors but not of creditors. The Democratic alternative asks credit card companies to provide information that consumers need to manage their credit card debts effectively, including equally conspicuous display of all terms accompany marketing of teaser rates and disclosure of the implications of making minimum payments.

The New York Times
TUESDAY, MAY 18, 1999

Why Squeeze Every Last Penny From the Bankrupt?

By Henry J. Hyde

WASHINGTON

Early this month, with the support of more than 300 of my colleagues, the House of Representatives approved sweeping changes in our national policy on bankruptcy. Generally, these are much-needed reforms, but one part of the legislation could leave some debtors without enough money for basic needs.

For the last century, Americans filing for bankruptcy generally have been able to receive an immediate financial fresh start. The legislation now making its way through Congress effectively channels many debtors into a form of bankruptcy relief where they will have to repay a portion of what they owe for up to five years, a fair expectation in a society operating on the premise that obligations will be honored. The sticking point is how to determine whether an individual has some meaningful ability to repay.

Even those in debt need to eat.

I'm a conservative, and I'm certainly a market capitalist, but I also believe in capitalism with a human face. Declaring bankruptcy can be a traumatic experience, and as we justifiably bolster creditors' rights, we ought not ignore the need to leave the debtor with a decent standard of living during the repayment period.

A majority of my colleagues believe that we should be guided by the Internal Revenue Service's expense allowance standards in determining the expenses of bankrupt individuals and their families for certain basic needs like food, clothing, rent and utilities. These standards, which are far too restrictive, were developed by the I.R.S. to maximize the collection of taxes from delinquent taxpayers, and I do not think it is a particularly Republican idea to advance them. In our successful effort last year to curb abuses by the I.R.S., Congress required it to apply these standards more flexibly in tax collection cases.

The treatment of food needs is an example of what is wrong here. The I.R.S. allowance applies uniformly in the contiguous 48 states, failing to reflect regional differences in the cost of food. In addition, under the I.R.S. schedule, allowable expenses for food increase dramatically with increases in income, a confirmation that the standards are not designed to reflect actual need. Serious problems are evident when a debtor earning $51,000 a year gets $421 per month for food when living alone and $619 per month — less than 50 percent more — when supporting a household of four. If more than a 5 percent increase beyond these standards in a family's food budget is needed, the bill passed by the House does not allow it unless the debtor can demonstrate extraordinary circumstances.

An amendment that I offered would have replaced the I.R.S. expense allowances in the bankruptcy legislation with a "reasonably necessary" standard that has been used for the past 15 years in voluntary debt repayment plans. Although existing case law already interprets and applies this standard, I proposed that the Department of Justice issue more precise guidelines. If my amendment had been adopted, many Americans still could have been channeled into repayment plans without depriving debtors and their families of the means to pay for their basic needs.

I hope Congress will reconsider this humane approach to living expenses, perhaps in similar legislation to be taken up as early as this week in the Senate or in a House-Senate conference to reconcile different versions of bankruptcy reform legislation. Decency and dignity need not be victims in an otherwise useful reform. □

Henry J. Hyde, a Republican from Illinois, is chairman of the House Judiciary Committee.

Book, Movie, War, Reality

By Larry Beinhart

WOODSTOCK, N.Y.

Taking a detour into the absurd, a Yugoslavia official, Goran Matic, claimed last week that there are no real Kosovar refugees. That the people we see acting like refugees are just that — actors, 3,000 to 4,000 of them, getting paid $5.50 a day by NATO. The way it was in the film "Wag the Dog."

As if to match him, a NATO spokesman would deny the story *only on condition of anonymity.*

But nobody believed Mr. Matic anyway. His problem was that he only saw the movie. He didn't go back to the book it was based on. The book has a different title — "American Hero" — and it's about the creation of an actual war as a theatrical event, while the movie is about the creation of the *illusion* of a war.

The thing is that modern war really is a theatrical event. In the old days, the media cooperated with government — by commandment in totalitarian countries, by mutual agreement (with some few exceptions) in the democracies.

Until Vietnam. In its analysis of that failure, as Colin Powell pointed out in his biography, the American military explicitly understood that it is necessary to plan how the war will play out on television as well as on the ground.

Combat is now a theatrical event. That's good.

That sounds like a bad, cynical thing. But it's not. As we learned in the Persian Gulf, a well-thought-out, thoroughly planned war in which civilian casualties are avoided and our casualties are lower than they are for stunt men working on normal movies, a war that has a definite conclusion and is over quickly, is better than an unfocused, messy, dragged-out war.

Thus the Bush Administration took a look at Yugoslavia years ago and said — I'm paraphrasing here — "That's going to make a lousy picture; let's not do it."

But now the Clinton Administration has put it into production. They too should have gone back to the book first — not necessarily my book, "the book." If somebody had actually worked on the plot, story conferenced it, they might have said: "O.K., let's say we bomb them, and Milosevic doesn't fold, he just steps up his campaign against the Kosovars. What then?" What now?

We know several things about war movies. First of all, it's necessary for the good guys to do bad things. We have to prepare for that; we have to know that the bad things really are necessary. Also, it's better if the good guys seem purposeful and smart, not confused and ineffectual. Finally, we know that we'll need an ending, preferably happy.

So Mr. Matic's remark inadvertently gives us a lesson, unfortunately too late to follow this time: if wars are to be theatrical events, *never start shooting without a script.* Which is the Hollywood version of what Karl von Clausewitz used to say: "No one starts a war — or rather no one in his senses should do so — without being clear in his mind what he intends to achieve by that war and how he intends to achieve it." □

Larry Beinhart, the author of "American Hero," is working on a screenplay titled "Divorce."

Enforce Campaign Laws

To the Editor:

Once again you are advocating more laws regarding campaign financing (editorial, May 12). What is wrong with the laws that exist? Active enforcement of existing laws would provide sufficient control to prevent the abuses we saw during 1996. The Justice Department has fallen asleep in its enforcement responsibilities, the members of the Federal Election Commission act as if they are political appointees (surprise!), and both political parties are taking advantage of the situation by pushing the limits as far as they can.

If the President took the lead by telling Attorney General Janet Reno to take the gloves off on law enforcement, more legislation would become unnecessary. Adding more subheadings to the legal code is counterproductive and will lead to more lobbying and more campaign contributions.

DAVID M. BARRETT JR.
LaGrange, Ga., May 12, 1999

Insuring Our Children

To the Editor:

Re "Kids' Insurance Fund" (letter, May 16):

If states are having trouble finding children without medical insurance, they should print pamphlets about the program that schools could give to parents when they register children for school. No child's registration should be complete without proof that he or she has medical coverage from a private insurer, Medicaid or a state-subsidized program.

ELLEN FREILICH
New York, May 17, 1999

Bottom Line on Kosovo

To the Editor:

Owen Harries (Op-Ed, May 16) is right when he castigates the Clinton Administration for using "parsimonious means" to solve the Kosovo humanitarian crisis. The Administration wants the Yugoslav Government to accept terms that neither it nor any other government would ever accept unless threatened by a more than adequate use of force.

The Administration, however, does not want to send the ground troops to fight a war over what it officially does not wish to dispute — Yugoslavia's sovereignty over Kosovo. This forces the Administration to modify its demands and negotiate with the Yugoslav Government. The Administration will have to do what Mr. Harries suggests: "bear fully in mind the interrelatedness of things." It must be prepared to do something it has so far refused to do: negotiate over Kosovo's future political status and convince the Yugoslavs that the Kosovars will neither now nor in the future have de facto independence.

JOHN P. PAVELEC
Lakewood, N.J., May 16, 1999

Raise Teacher Standards

To the Editor:

In the debate over the Board of Regents' push to raise graduation standards and New York State legislators' rebellion against it (front page, May 12), little attention has been paid to teacher preparation. It is true that employers expect schools to provide better prepared students, but this cannot be done with current staffing, particularly in mathematics. The recent import of Austrian mathematics teachers, which I helped arrange, demonstrated the severe shortage of qualified teachers.

This is a national crisis. Raising standards without addressing teacher shortages and providing appropriate teacher training will result in higher failure rates and punish the very students we are trying to help.

ALFRED S. POSAMENTIER
New York, May 12, 1999

The writer is a professor of mathematics education at City College, CUNY.

The New York Times Company
229 West 43d St., N.Y. 10036-3959

Unethical Referrals

To the Editor:

Re the May 16 and 17 front-pa[ge] "Research for Hire" series: The r[e]lationship of trust between a patie[nt] and a physician is paramount. Whe[n] a physician accepts money for referring patients to clinical trials, that is the ultimate abuse of that trust and an abuse of power.

The American Medical Association's Council on Ethical and Judicial Affairs has had a clear policy on this issue for more than 20 years. Payment by or to a physician solely for the referral of a patient is fee splitting and is unethical. A physician's primary concern must always be with the health of the patient. Receiving payment for referral to a clinical trial violates the requirement to deal honestly with patients.

D. TED LEWERS, M.D.
Vice Chairman, Board of Trustees
American Medical Association
Chicago, May 17, 1999

Saving City Gardens

To the Editor:

The celebration of Bette Midler's philanthropic support for New York City's community gardens (editorial, May 14) obscures the government failure that precipitated the need for this private intervention.

Mayor Rudolph W. Giuliani's extortionate demand that private parties pay the city not to destroy the community gardens located on city-owned property will make it more difficult to save hundreds of other community gardens across the city. Viewed as a potential national model, it establishes a high price for our own government not to destroy the livability of our communities.

Preservation of publicly owned urban green space should be recognized as a legitimate function of government, not left to the serendipitous intervention of one generous movie star.

JOHN D. ECHEVERRIA
Washington, May 17, 1999

The writer is the director of the Environmental Policy Project at Georgetown University Law Center.

America's Love for Guns

To the Editor:

President Clinton blames Hollywood and television for encouraging gun crimes like the massacre in Colorado (news article, May 16), but the same television shows and movies are watched by children and adults in almost every other country of the world without producing the same degree of slaughter. Canada, for example, had fewer than 200 gun deaths in 1997, while the United States had 10,000.

The real issue is the almost nationwide desire to embrace guns as a necessary and normal way of life, which only increases the availability of weapons to Americans of all ages. As long as it is considered reasonable to own a gun, the United States will continue to have the highest death toll by guns in the world. Reversing that mind-set and removing guns from homes is the real challenge to a bold leader. Television and film are useful scapegoats for a cautious one.

DAMON McELHONE
Brooklyn, May 16, 1999

The New York Times
TUESDAY, MAY 18, 1999

Morally Bankrupt Creditors

By David S. Broder

Sunday, May 16, 1999; Page B07

Politics, as everyone knows, makes strange bedfellows. But it still raises eyebrows -- and suspicions -- to discover Hillary Rodham Clinton and Henry Hyde making common cause on the bankruptcy bill that passed the House on May 5 and is scheduled to be up for debate in the Senate this week.

A year ago, when similar legislation was close to final approval on Capitol Hill, the first lady sounded the alarm inside the White House and a veto threat from the president stopped it cold. When it was revived earlier this month in the House, Hyde, the chairman of the Judiciary Committee and leader of the effort to impeach and remove President Clinton, found himself in the odd position of repeating some of her arguments.

Conscious that he was in strange company, the veteran Illinoisan explained, "I am as capitalist as anybody, but it does not seem to me when there is a bill that is truly tilted toward the creditors, that giving a little flexibility for living standards for people who are bankrupt is a violation of one's credentials as a conservative."

Hyde had made the same argument in committee, recounting some of the "75 enhancements here for the creditors" and pleading with his colleagues to "throw a little, small bone to the debtor." But his amendment was defeated by what he called the "awesome creditor lobby" led by the banks that control the credit card market.

The complexities of bankruptcy law are beyond my understanding, but the odd alliance between Hyde and Hillary -- who argued inside the administration that the legislation might give the issuers of plastic as much claim to a bankrupt worker's earnings as his ex-wife or their children -- is not the only signal that this legislation may deserve more scrutiny than the press has given it so far.

There's also the fact that the members of the National Conference of Bankruptcy Judges endorsed Hyde's amendment, as did Brady Williamson, the chairman of the bankruptcy law reform commission, and major consumer groups.

They all admit there is a problem in the explosion of bankruptcy cases in this decade. Last year, more than 1.4 million Americans filed for individual bankruptcy, seeking legal protection against their creditors. That is almost a threefold increase in 12 years.

No one disputes that among these cases, there are a number of people -- the estimates range from 4 percent up to 15 percent -- who could, if pressed, pay off some of their debts. A few of them are the publicized wealthy individuals who run up big bills for luxuries, then put all their assets into lavish homes in states with high homestead exemptions and laugh when their creditors try to collect.

It is only these cases the bankers and retailers say they want to reach, by making it harder for people to file under Chapter 7, which basically lets you wipe out your debts and start clean, and forcing them instead to file under Chapter 13, which requires repayment of at least some debts over a period of up to five years.

But statistics show most of the Chapter 7 filers are people with modest incomes who just get in over their heads. The fastest-rising category of debt is in revolving credit card accounts, and the banks that dominate that business have been the most aggressive lobbyists for tightening the bankruptcy law.

But they have been at least as aggressive in marketing their cards, mailing out an incredible 3.45 billion -- not million but billion -- solicitation letters last year. Beth Climo, a spokeswoman for the American Bankers Association, told me that since the banks underwrite these loans, they are careful about issuing credit.

But Elizabeth Warren, a Harvard Law School professor who has studied this issue, countered that banks make so much money on unpaid credit card balances -- thanks to interest rates much higher than on home mortgages, car loans or other forms of "secured" debt -- that they deliberately lure people into borrowing beyond their means. Now, she said, they are trying to get Congress to rig the rules so their loan losses will be reduced.

Critics of the legislation say it should at least force the credit card bankers to include more specific consumer warnings on the monthly bills, telling customers, for example, how many months (or years) it will take them to pay off the outstanding balance if they make only the minimum required monthly payment. But disclosure provisions in the House bill are modest -- and in the Senate version, almost nonexistent.

After his amendment was defeated, Hyde voted for final passage of the bill, expressing the hope that it will be improved in the Senate. But the Clinton administration -- with Hillary Clinton riding herd -- is demanding big changes and threatening a veto.

This one bears watching.

~~Sa~~

Find myself agreeing w/ Henry Hyde

Bankruptcy bill with serious flaws.

Reform is in order - debtors w/ capac to repay should be required to do so, but this bill does not strike the right balance

Let me describe ~~for you~~ scenarios of those who will be affected - hurt by ~~the~~ bill which does not take into account ~~spec~~ circumstances ~~&~~ people find themselves in

losers of reform

(1) victim of domestic violence
debtor has to in
Imagine who incurs expenses relating to protecting herself from an abusive spouse - security,

(2) Imagine an ~~out of w~~ laid-off steel worker who has enrolled in work training program to get a better job

(3) ~~proba~~ Imagine a couple taking care of an elderly parent to keep them out of a nursing home - only has her SS check - needs add'l support (not tech a dependent),

(4) Imagine a couple who has waited for years to adopt a child - expenses associated w/ it

None of these debtors would have their circum reviewed in deciding how much they need to live on and therefore how much of their income they need to pay back

Praise Hyde - gave judges the discretion to consider the circum. Unfort. the Chairman's amendment was defeated in the face of ~~cc~~ aggressive creditor lobbying.

Now let's talk about those who aren't hurt by this leg:
(1) creditors who coercise debtors to reaffirm debt
(2) credit card co. who mail solic - not screened
(3) The Rich - homestead exemption

Plea - we need to do this right - hopes the Senate shows leadership.

somewhere - child support & alimony payments.

mobilize amend alt
amendment - Ken, Durbin - Leahy Sarbanes def. in bill — Jon / Reed / Schum
targeted amendments — Hyde.

Sub - non dep.
- welfare to wk career adv.
- adopting - fostercare
Hyde - domestic violence
limited disc.
reaff.

5 ex - fall through the cracks.
Henry Hyde.

credit card -
land off sleepwalk cons. solicitation
worker -
hard times - training -
farmers.

praise Hyde

→

→ hope with the Cong.

Imagine a woman who

Imagine -
Steel
8 kids, coal miner
working for peoples.

to
need reform
need balance
who wd not get hurt -
→ credit and targets
reaff. felons - th -
not aff. homestead
Burt Rey
wd be hurt -
dom violence - ers
only
farmworker -

NEWS FROM THE HOUSE DEMOCRATIC LEADER

For Immediate Release:
May 5, 1999

House Democratic Leader Richard A. Gephardt
H-204, U.S. Capitol

Gephardt Statement on H.R. 833, The Bankruptcy Reform Act of 1999

"Today, the House will consider H.R. 833, legislation that will make unprecedented changes to the consumer bankruptcy laws of our country. While I support a balanced approach to bankruptcy reform that places equal responsibility on both debtors and creditors, I must oppose H.R. 833 because it fails to strike such a balance.

"Reps. Nadler, Conyers, Meehan and Berman will offer a substitute to H.R. 833 that moderates the bill in significant ways that achieves this necessary balance. The Nadler/Conyers/Meehan/Berman substitute would moderate the means test in H.R. 833 to hold responsible debtors who have the ability to repay a portion of their debts. But at the same time, the Democratic sponsored substitute would address creditor abuses that would jeopardize the repayment of priority debt such as child support and alimony payment. In addition, the substitute includes a very important bipartisan farm provision that would raise the eligibility threshold for family farmers to seek protection under Chapter 12 which was left out of H.R. 833.

"I also support the Hyde/Conyers amendment to H.R. 833 which would make a modest but important improvement to the bill's needs based formula by striking its reliance on a rigid IRS expense allowances formula and maintain current law under which bankruptcy judges are given limited discretion to tailor expense standards for bankruptcy specific purposes. Proponents of H.R. 833 have unreasonably rejected even this modest change to the bill.

"The reforms that we make to our consumer bankruptcy system could have as significant an impact on the lives of hardworking American families as any legislation that we will consider in the 106th Congress. As such, we must approach this effort with the greatest responsibility on achieving balance in our bankruptcy system. H.R. 833 fails to accomplish this goal; therefore, I must oppose it."

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Contact: Laura Nichols/Sue Harvey (202) 225-0100

HRC TPs for Daschle mtg

Talking Points on Bankruptcy
May 18, 1999

Bankruptcy is coming up for floor action very soon.

As you know, the Administration has serious problems with the bill. We are also realistic about our prospects for making significant improvements.

Still, I believe if we work together we can make a difference. I am asking you to:

(1) Do all you can to get 34 votes against final passage (veto proof margin), enabling us to have leverage in conference to improve the bill.

(2) Mobilize behind the Durbin substitute, co-sponsored by Leahy, Kennedy, Sarbanes and Reed – which passed last year by 97-1.

(3) Support a group of targeted amendments to improve the bill – including the Hyde Amendment (which we hope will be offered by Torricelli or Schumer).

For my part, I will do everything I can to be helpful.

The Honorable Charles Grassley,
Chairman

The Honorable Robert G. Torricelli,
Ranking Member

Subcommittee on Administrative Oversight and the Court
Committee on the Judiciary
United States Senate
Washington, D.C. 20510-6275

Dear Chairman Grassley and Senator Torricelli:

We are responding to your letter of April 21 regarding the bankruptcy reform legislation, S. 625, that you introduced and that is under consideration in the Senate. As you know, the Administration supports bankruptcy reform that is balanced and that asks both debtors and creditors to act more responsibly. We appreciate your bipartisan efforts to produce such legislation, and we look forward to working with you in this important process.

Your letter asks us to consider either modification to the Internal Revenue Service (IRS) National Standards Expense Allowances, or to create an appropriate set of alternatives specifically tailored to bankruptcy, for use in the "means test" of S. 625. These standards would be used to guide judicial decisions about whether individuals who have filed for relief under Chapter 7 of the Bankruptcy Code have the capacity to repay a portion of their debts and must therefore file a Chapter 13 repayment plan rather than seek liquidation under Chapter 7.

As you noted in your letter, some have suggested that the IRS Standards are insufficiently flexible for use in the bankruptcy context. In a March 24 letter to Chairman Gekas of the House Judiciary Subcommittee on Commercial and Administrative Law, the Justice Department agreed, stating that

> . . . the use of Internal Revenue Service (IRS) Standards for allowable expenses is inappropriate because those standards were not intended for these purposes. The IRS standards were meant to provide guidelines for determining appropriate expenses. Last year . . . Congress criticized the inflexible application of those guidelines and directed the IRS to also consider the taxpayer's facts and circumstances.

The Administration supports the development and use of fair and reasonable expense standards for bankruptcy purposes, to limit costs and improve the fairness of the means testing process. To achieve this goal, we believe that the most effective approach is for the Treasury Department and the Justice Department to work together to develop standards tailored to bankruptcy, using IRS expense allowance standards as appropriate.

We also agree with you that the best way to apply such standards is as a "rough guide," with appropriate exceptions for "special circumstances" of debtors. Rigid enforcement of any set of standards is both more administratively burdensome (because standards must be developed and applied in far more detail, to deal with the complexity of individual household, work expense, and business situations) and ultimately more costly (because they inevitably fail to account for the actual circumstances of some debtors, leading to unachievable repayment plans and further litigation and administrative costs).

As you know, Chairman Hyde introduced an amendment to H.R. 833 during the House Judiciary Committee's mark-up with a similar intent. That amendment required, among other things, the Director of the Executive Office for the United States Trustee (EOUST) to develop standards for bankruptcy. It also provided appropriate, limited discretion in the application of these standards, much as you envision. We support the addition of such requirements to S. 625, and also recommend additional language requiring the EOUST Director to consult with the Treasury Department in the development and application of the standards.

We would be happy to continue to work with you and your staff to draft specific language on this topic, and to assist you in enacting bipartisan and balanced bankruptcy reform legislation. Thank you again for your letter on this important topic.

Sincerely,

Robert E. Rubin
Secretary of the Treasury

Janet Reno
Attorney General

cc: The Honorable Orrin Hatch
The Honorable Patrick Leahy
The Honorable Henry Hyde
The Honorable John Conyers
The Honorable George Gekas
The Honorable Jerrold Nadler

AMENDMENTS SUBMITTED TO H.R. 833 – BANKRUPTCY REFORM ACT OF 1999
Monday, March 2, 1999; 7:15 p.m.
(listed in alphabetical order)

Member	Summary
Barrett #10	Caps liability for the unauthorized use of a debit card at $50, the same level as credit cards.
Barrett #11	Provides that if a credit card company rejects an application for credit which is submitted in response to their own "pre-approved" solicitation, they may not report that rejection to credit bureaus or otherwise sell or distribute that information.
Bentsen #15	Strikes all provisions preempting state homestead laws.
Bentsen #16	Changes the effective date of the national homestead exemption so the state legislatures can enact legislation that would opt out of this new national standard.
Bentsen #17	Preserves a state's ability to enact legislation to opt out of the new national homestead standard prior to the effective date of this legislation.
Conyers #19	Grants debtors in possession of consumer goods under a rent-to-own contract, and the lessor or bailor, as having the same rights and obligations with respect to the consumer goods as would have been accorded if the rent-to-own contract had been a purchase contract.
Conyers #23	Waives the provision of chapter 11 relating to small business debtors or to single asset real estate in cases where the application of those provisions could result in the loss of 5 or more jobs.
Conyers #24	Excludes from the bill's definition of current monthly income any benefits received under the Social Security Act, in addition to excluding payment to victims of war crimes and crimes against humanity (as the bill already does).
Delahunt/Kanjorski/Houghton/Rothman/Barrett #27	Strikes paragraph (3) of section 147 of the bill, which permits States to "opt out" of the provision in section 147 that establishes a $250,000 Federal cap on the value of real or personal property that a debtor (other than a family farmer) may exempt in bankruptcy under the "homestead exemption."

Delahunt/LaFalce/Watt/Roybal-Allard #28

Adds a new subsection 154 to the bill disallowing claims in bankruptcy for consumer credit card debts if, at the time of the solicitation to open the account, the debtor was not informed in writing in a clear and conspicuous manner of 9 specific factors.

Doggett/Watt #29 Provides residents of continuing care retirement communities with the status of "priority unsecured creditor" so that they may increase their chances of getting some or all of their initial deposit back from a bankrupt continuing care retirement community.

Dooley #35 **Late**. Requires the Federal Trade Commission to set standards to be used by the United States Trustees in approving credit counseling agencies, programs described in section 109(h) and instructional courses concerning personal financial management.

Gekas #13 Manager's Amendment. The Amendment (1) makes various technical changes; (2) makes a clarifying revision to the type of expenses that a debtor may claim pursuant to the IRS Other Necessary Expenses categories (the revision specifies that the debtor must claim *actual* monthly expenses for the specified categories); (3) revises certain provisions so that they conform with the Bankruptcy Code's other provisions pertaining to an award of attorneys' fees; (4) clarifies that the chapter 7 trustee must file a statement as to whether or not a case should be presumed to be an abuse in every case administered by such trustee; (5) revises chapter 13's requirements for confirmation to require the court to find that the debtor filed the chapter 13 case in good faith; (6) revises the title of section 134 of the bill; (7) deletes Section 215 (claims relating to insurance deposits in cases ancillary to foreign proceedings) as this provision is included in title XI of the bill, as revised by this Amendment; (8) adds a new provision to describe certain procedural matters pertaining to appeals, as amended by the bill; (9) adds provisions with respect to the treatment of certain funds subject to state insurance law or regulation for the benefit of claim holders in the United States; (10) repeals sections of the Bankruptcy Code that are no longer necessary; and (11) amends a statutory cross-reference so that it better comports with the drafters' intent, which is to include in the definition of a "financial participant" certain securities contracts, forward contracts, repurchase agreements and swap agreements in addition to certain commodity contracts.

Graham #14 The bankruptcy code prohibits the discharge of federally made, guaranteed or insured education loans or education loans made by non-profit institutions. This amendment would extend the prohibition from discharge to all qualified education loans. Includes exceptions for undue hardships.

Hyde/Conyers #12 Deletes the reported bill's application of modified IRS expense allowances for determining permissible projected living expenses of debtors and their families during the life of chapter 13 plans. In its place, the amendment adopts a standard that allows only "reasonably necessary" expenses and directs the Executive office of United States Trustees to issue guidelines that will assist in making assessments of whether expenses qualify. The amendment does not affect other provisions of section 102 that are designed to limit the availability of an immediate fresh start in chapter 7, channel significant numbers of chapter 7 debtors into five-year chapter 13 repayment plans, and generate greater recoveries from creditors.

Jackson-Lee #3 Disallows the discharge of debts by corporations under chapter 11 of the Bankruptcy Code, when the debt arises from a tobacco-related action that involves a claim of false pretenses, false representations, or fraud.

Jackson-Lee #4 Changes chapter 11 bankruptcy, disallowing the discharge of debts incurred by health care organizations when they arise from judgments based on false representation, false pretenses, or fraud.

Jackson-Lee #5 Excludes Social Security benefits from the determination of what constitutes an individual's "current monthly income" for the purposes of this bill.

McCollum #31 Amendment in the nature of a substitute. Substitutes H.R. 833 as introduced for H.R. 833 as reported by the Committee on the Judiciary.

Moakley #34 **Late**. Provides bankruptcy protection for funds placed in qualified state tuition programs under the Internal Revenue Code for post-secondary education costs.

Moran/Ackerman/Dooley(need letter) #32 **Late**.

Inserts a disclosure requiring that a debt relief agency providing bankruptcy assistance to an assisted person shall provide a written notice within three business days after the first date on which a debt relief agency first offers to provide any bankruptcy assistance services to an assisted person, advising assisted persons of their rights and responsibilities of disclosure. Requires that an attorney or bankruptcy petition preparer give an assisted person a written contract specifying what the attorney or preparer will do and the cost. Inserts a "debtor's bill of rights." Requires that a debt relief agency disclose in any advertisement of bankruptcy assistance services or of the benefits of bankruptcy that the services or benefits are with respect to proceedings under this title of the Bankruptcy Code.

Moran #33 **Late.** Amend the Truth in lending Act (TILA) to require Credit Card Issuers to make disclosures regarding minimum monthly payments. It would also ensure that consumers have all the information they need in order to avoid the imposition of late fees and requires that Worldwide Web-Based Credit Card Solicitations are subject to the same "Schumer Box" disclosures as all other credit card solicitations.

Nadler #18 Permits debtors to choose between the Federal law or their state law for determining which property would be exempt in bankruptcy.

Nadler #20 Strikes section 130 of the bill which restructures chapter 13 to apply the standards in the means test to the calculation of repayment plans in chapter 13. The deleted section also gives unsecured non-priority creditors improved status vis-a-vis other creditors in chapter 13.

Nadler #21 Excludes from the bill's definition of a debtor's current monthly income, which is used to determine that debtor's ability to repay debts, any payments received in satisfaction of a domestic support obligation. Strikes that provision of the bill that permits lessors of residential real property from evicting debtors-tenants who have not made payments as required by a lease agreement. Requires that domestic support payments to the parent, child, and government due during the plan be made, but that only arrears due to the custodial parent and child, not the government, must be provided for in the plan. Creates exceptions for the automatic stay actions necessary to assist or protect families and children. Makes alimony, maintenance, support or property reasonably traceable to such alimony, maintenance or support, as well as amounts payable as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree – but only to the extent reasonably necessary for the support of the debtor or a dependent of the debtor – exempt from property in bankruptcy. Requires that funds received by a creditor whose debt has been made nondischargeable under the newly added exceptions to discharge in the bill, must hold it in trust for five years, make every effort to pay it to individuals holding debts in the nature of support obligations (but not governments). They must make these payments to any such individual whose identity is reasonably ascertainable.

Nadler #22 Strikes that provision of the bill that prevents debtors who bring lawsuits against creditors for violations of reaffirmation agreements or of discharges of debts from bringing those lawsuits as class actions.

Nadler #25 Makes nondischargeable in bankruptcy any debts that arose out of (1) a violation of Federal, state, or local law that protects access to health care facilities or reproductive health care facilities, (2) harassment or intimidation of any person attempting to enter or use a health care facility or reproductive health care facility, or (3) damage to or destruction of a health care facility or reproductive health care facility, or (4) an actual or attempted violation of a court order or injunction that protects access to a health care facility or reproductive health care facility.

Nadler #26 Would disallow a claim for a debt under 11 USC 502(b) if it is based on the extension of credit to an individual who the lender knew or should have known was already over extended (i.e. the extension of credit would cause the debtor's aggregate unsecured debts to exceed 40% of the debtor's annual gross income) or if the claim was based on a secured debt if the creditor has violated section 129(h) of the Truth in Lending Act.

Nadler/Conyers/Meehan(need letter)

#37 **Late**. Substitute. Provides a realistic means test which takes into account the debtor's actual income and expenses. Does not omit expenses a debtor would have to pay in a chapter 13 plan from the test used to determine whether the debtor must file for chapter 13. Does not rely on IRS guidelines to determine how much a debtor should live on. Allows adequate judicial discretion to determine whether the debtor appropriately belongs in chapter 7. Avoids using a debtor's ability to repay a specified percentage of unsecured non-priority debts which is easy for debtors to manipulate. Holds both debtor and creditor attorneys to strict application of Rule 9011's penalties for misconduct or bringing a frivolous case. Contains a safe harbor for families below the median national income. Provides a balance by requiring credit card lenders to behave responsibly and to provide borrowers with the information they need to avoid bankruptcy. Prevents some of the more highly publicized cases in which creditors illegally enforced debts after bankruptcy through "reaffirmation agreements." Deletes a section which would have denied victims in these cases a legal remedy by prohibiting class action suits. Eliminates new grounds for making credit card debts non-dischargeable, but leaves intact current law which makes prebankruptcy debt run-up and fraudulently incurred debt non-dischargeable. Eliminates a provision which would have allowed landlords to evict debtors without obtaining the permission of the bankruptcy court. Removes a provision which allows secured creditors to treat the unsecured part of some loans as secured debt. Modifies the child support portions of the bill to take away the special new rights over families that state and local governments would have obtained in a bankruptcy case. Places families first.

Scott #2 Exempts Veterans benefits from the calculations of monthly income for the purpose of determining income available to creditors.

Thompson (MS) #30 Protects monetary awards given to individuals in cases where the award is made on a finding of discrimination based on race, religion, gender and national origin.

Watt #6 Replaces the provisions of H.R. 833 which require that all bankruptcy filers file their tax returns with the court and instead require that a debtor file tax returns with the court at the request of any party in interest.

Watt #7 Requires that credit card billing statements contain disclosures which advise consumers of: (1) the number of payments it would take the consumer to pay of the current balance if the consumer only pays the minimum payment each month and (2) the total dollar amount which the consumer would pay if the consumer only pays the minimum payment each month.

Watt #8 Allows a bankruptcy filer to object to a creditor's claim in bankruptcy if the creditor had not made the disclosures to the debtor described in Watt #7.

Watt #9 Clarifies that the burden of proving that a filing is an abuse of the bankruptcy code is on the moving party by a preponderance of the evidence. Deletes the provisions of the bill which allow a debtor to rebut presumed abuse by demonstrating "extraordinary circumstances."

Whitfield #36 **Late.** Establishes a mechanism whereby bankruptcy trustees may receive compensation when they transfer cases from chapter 7 to chapter 13. Under this provision, the level of compensation would be determined by the bankruptcy judge.

Velazquez #1 To allow the expansion of the credit committee membership under chapter 11 bankruptcies to include a small business when it is determined that the small business' claims are disproportionally large to its gross revenues. And to ensure better access to information for those small businesses not included in the committee by allowing the committee to be open for comment and subject to additional reports or disclosures.

* Summaries derived from information submitted by the amendment sponsors.

DRAFT - NOT FOR RELEASE

May 4, 1999
(House)

H.R. 833 - Bankruptcy Reform Act of 1999
(Gekas (R) Pennsylvania and 103 cosponsors)

The Administration strongly opposes H.R. 833. If the bill were presented to the President in its current form, his senior advisers would recommend that he veto the bill.

Many of the bill's provisions are simply unfair to middle- and low-income debtors; at the same time, the bill fails to close loopholes in current law that protect the wealthiest debtors. The Administration continues to support bankruptcy reform that asks both debtors and creditors to act more responsibly. However, H.R. 833 fails the test of balance between creditors and debtors, particularly in its provisions affecting low- and middle-income debtors. The bill focuses disproportionately on perceived abuse of the bankruptcy system by debtors and takes an excessively rigid approach to limiting access to discharge of debts under Chapter 7 of the Bankruptcy Code.

H.R. 833 in its current form would limit access to Chapter 7 to debtors who meet an inflexible and arbitrary means test. Reps. Hyde and Conyers intend to offer an amendment that also includes a means test but which would use expense standards that are appropriate for bankruptcy and would allow limited, appropriate discretion in their application so that debtors denied access to Chapter 7 are those who are likely to be able to repay a portion of their debt under a Chapter 13 repayment plan. Provided one technical change is included, the Administration could support the Hyde-Conyers amendment. ***[Do we know yet if the change has been made?]*** The Democratic amendment to be offered achieves the same goals and also significantly reduces the administrative and legal burden of means testing by screening out low-income debtors with little ability to repay. Under either amendment, debtors who genuinely have the ability to repay a portion of their debts would remain responsible for those debts.

The Administration continues to believe that reform must ensure that debtors are treated fairly and responsibly in the bankruptcy process, recognizing creditors' superior information and bargaining power. In addition to the changes described above, H.R. 833 needs to be revised to so that the bill: (1) appropriately balances greater repayment of dischargeable debts with the need to protect child support, alimony, secured debts, and other societal priorities like educational loans and taxes debts; (2) adds procedural protections and clear guidelines for reaffirmations of unsecured and low-value secured consumer debts to ensure that the financial terms of the reaffirmation are adequately disclosed and to enable judges to use streamlined procedures to identify potentially unwise and possibly coercive reaffirmations; (3) limits the anti-cramdown provision in the bill such that [Treasury please supply]; and (4) includes new disclosure requirements to ensure that credit card companies provide consumers with the information they need to manage their credit card debts, to help consumers avoid the need for bankruptcy. The Democratic amendment addresses all of these concerns.

In addition, the Administration supports changes that would close loopholes in current bankruptcy law, such as those enabling unlimited homestead exemptions and exemptions from repayment requirements for individuals who are able to file for bankruptcy under Chapter 11, that protect some of the wealthiest debtors from having to repay a significant portion of their debt. Bankruptcy reform should not place a greater responsibility for debt repayment on moderate- and low-income debtors than it does on high-income debtors.

The Administration remains ready to work with the House to address these concerns, building on the responsible and balanced reform of the Democratic amendment and the bipartisan approach of the Hyde-Conyers amendment.

* * * * * * *

Message Sent To:____

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FYI

Hyde-Conyers Dear Colleague Letter:

May 3, 1999

Dear Colleague:

During floor consideration of H.R. 833, the "Bankruptcy Reform Act of 1999," we hope to offer a bipartisan amendment relating to permissible living expenses of debtors and their families. If our amendment is adopted, the legislation will remain overwhelmingly pro-creditor but will treat those experiencing financial distress more humanely.

Our amendment makes a significant improvement to H.R. 833's needs-based formula. It replaces the bill's reliance on IRS expense allowances and instead incorporates a test based on the disposable income standard of current law--whether income is "reasonably necessary . . . for . . . maintenance or support." To enhance predictability, the amendment requires the Director of the Executive Office for United States Trustees to issue guidelines that will be considered in the application of the "reasonably necessary" standard. In our view, the limited effort to modify the IRS standards in the Committee on the Judiciary--by including a five percent add-on for food and clothing only and providing for the continuation of certain private school expenses--fails to solve major problems with incorporating IRS schedules into our bankruptcy law.

H.R. 833 contemplates a major overhaul of our consumer bankruptcy system. For the last century-- dating back to the first permanent bankruptcy law of the United States, the "Bankruptcy Act of 1898"--individual debtors generally have been able to receive an immediate financial "fresh start" without having to encumber their future incomes. By greatly enhancing the potential for dismissing Chapter 7 "liquidation" cases--bankruptcies that provide immediate, limited discharges of obligations in return for debtors giving up any nonexempt assets--H.R. 833 channels many debtors into five year Chapter 13 repayment plans. This major shift in bankruptcy policy necessitates focusing on what portion of a debtor's future income will be available for living expenses.

The reported bill says in effect that debtors and their families must adhere to a somewhat modified version of the IRS to facilitate compromises with delinquent taxpayers. The delinquent taxpayer model, however, is inappropriate for imposition in bankruptcy because (1) the successful collection of taxes is a matter of national self-preservation, and (2) the private sector can minimize the risk of losses by adhering to prudent creditor practices. The great irony here is that Congress recently gave expression in the Internal Revenue Service Restructuring Act of 1998 (P.L. 105-206) to the need for flexibility in the application of IRS expense allowances--with the IRS to determine the appropriateness of applying the schedules to individuals. Relief from modified IRS expense allowances in this bankruptcy legislation, however, requires debtors to demonstrate "extraordinary circumstances"--a more rigid and inflexible approach than even the IRS practice.

Professor Jack Williams of Georgia State University School of Law, who chaired the National Bankruptcy Review Commission's Tax Advisory Committee, pointed out in a written submission for our bankruptcy hearings this year: "Tying debtor eligibility to a formula that the IRS deviates from on a regular basis makes no sense." He described the IRS collection standards as "too parsimonious." Professor Williams stated:
"[O]ne must conclude that the standards are unrealistic. The IRS personnel know this fact and often deviate from the collection standards in an effort to permit settlement of tax claims."

A few days ago we heard from the Commercial Law League of America, an organization with over 4,600 individual members that describes itself as having "long been associated with the representation of creditor interests, while at the same time seeking fair, equitable and efficient administration of bankruptcy cases for all parties involved." The League wrote:

"Utilizing the IRS guidelines is problematic because: (i) it converts a guideline utilized in a nonbankruptcy setting, that is subject to discretion, to a rigid standard in the bankruptcy setting, under which the court is expressly prohibited from exercising any discretion (i.e., a guideline is converted to an absolute standard), (ii) it will ultimately reduce distributions to creditors because fewer individuals will seek Chapter 13 relief and those that do will be far less likely to complete the payment plan, and (iii) it takes discretion away from the court to be flexible enough to apply a now well-developed standard to realistically assess the debtor's prospect for reorganization."

Judge Randal Newsome, President of the National Conference of Bankruptcy Judges, also wrote on April 30th after reviewing a similar amendment offered in the Committee on the Judiciary. He stated:

"On behalf of the 319 members of the National Conference of Bankruptcy Judges, I firmly believe that your amendment would lead to a far less complex and far more workable needs-based bankruptcy system than one which attempts to incorporate IRS expense standards. . . . Replacing those standards with your flexible test will lead to far less confusion, and thus far less litigation."

An unfortunate consequence of applying IRS living allowances in bankruptcy cases is to penalize some family members because they live with the debtor and cannot benefit from a support order. The bill includes protections for the beneficiaries of support orders issued by family courts that are not constrained by the living allowances IRS seeks to impose on delinquent taxpayers. Spouses and children in families that stay together effectively may be penalized by being forced to live under very restrictive, modified IRS allowances, whereas a noncustodial parent-with sufficient income--who is subject to a support order may be able to provide for his or her former spouse and children more generously. Parents who remain married to each other and live with their children should be able to provide for "reasonably necessary" living expenses. Regrettably, the bill as reported does not give bankruptcy judges the flexibility to achieve such an outcome.

We urge our colleagues to support our amendment which recognizes that we can dramatically change current law--by requiring large numbers of debtors to make future income available to creditors--without depriving debtors and their families of "reasonably necessary" living expenses.

Sincerely,

Henry J. Hyde

John Conyers, Jr.

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TARGETED MEANS TESTING FOR CHAPTER 7

The principal goal of this proposal is to minimize the total cost of a means test for moving potential Chapter 7 filers who can repay some of their debt into Chapter 13. The benefit of moving filers who can repay is the increased debt repayments that would result. The direct costs of means testing include the costs to the panel trustees, bankruptcy administrators and filers of providing information for testing, the attorney's and administrative costs associated with challenges to trustees' findings, and the additional administrative costs of inappropriate referrals to Chapter 13 that result in failure. Beyond these costs are the burden of personal compliance, and the inherent rights of debtors to a fair hearing on their particular circumstances, if they are to be denied access to Chapter 7. By targeting means testing effectively, the proposal assures that virtually all debtors who can repay are moved fairly and at minimum cost to the system. Much as the IRS uses its repayment capacity standards today, the proposal allows for limited discretion by Trustees and judges to consider special circumstances of debtors, subject to clear presumptions created by the detailed guidelines. Thus, this proposal would reduce the costs of means testing compared to current bills, permitting greater debt repayment.

Summary of Proposal

The resources expended to scrutinize debtors' ability to repay are related to the "payoff" in terms of expected repayment. Evidence on filers' actual ability to repay suggests that the best screen approach has two parts: low-cost screens for debtors who are unlikely to be able to repay, plus a more complete means test targeted to those who have some chance of being able to repay. Figure 1 summarizes the proposal.

(I) *Very Low Potential to Repay:* Debtors who document incomes below 75% of the national median, adjusted for family size, are not subject to further means testing. Unless the totality of circumstances suggests abuse, it is automatically presumed that filing for Chapter 7 by such debtors is not abusive.

(II) *Low Potential to Repay:* Debtors with incomes between 75% and 150% of the national median are initially screened using a simple preliminary test of repayment capacity. This *preliminary* test calculates ability to repay the lesser of 30% of debt, or $15,000, given that they can repay a minimum of $50/month, based only on their income and the subset of allowable expenses included in the *formulaic* portions of the IRS standards, the National and Local Standards, determined only by income, family size, and area of residence. If they cannot repay according to this test, they certainly could not pay if the additional nonformulaic expenses allowed under the IRS' Other Necessary Expenses are included, and they are presumed to be filing appropriately in Chapter 7. Debtors who may be able to repay according to this screen are subject to a complete means test involving a detailed review of income and expenses, and any other special circumstances that substantially influence the likelihood of repayment success.

(III) *Some Potential to Repay:* Debtors with incomes above 150% of the national median are fully examined for the ability to repay according to a complete means test involving a detailed review of the debtor's income, expenses, and any special circumstances.

ANALYSIS

Who can be expected to repay?

Recent national studies of the repayment capacity of Chapter 7 filers show that income is a very strong predictor of repayment capacity and therefore is an appropriate measure for a simple initial screening test.

* According to Ernst & Young, March 1998,[1] and additional data provided to the Treasury, filers with incomes below 75% of the national median adjusted for family size represented 54% of Chapter 7 filers. Their repayment capacity was extremely low. Ernst & Young found that only about 3 out of every 100 filers in this income category had the ability to repay even $3,000 or 20% of their debt. Moreover, the debtors who met this $3,000/20% threshold had the lowest average ability to repay among all income groups.

* Those with incomes between 75% and 150% of the national median constituted 36% of Chapter 7 filers. About one-fourth of these filers --less than 3 out of every 10 -- had some ability to repay even a small portion of their debt. The degree of repayment capacity did not differ substantially at different levels of income within this range.[2]

* Those with incomes above 150% of median comprised only 9.7% of all Chapter 7 filers. But nearly 5 out of every 10 of these filers had some ability to repay.

What is the repayment potential?

Available data preclude a precise estimate of the amount of debt each debtor would actually repay in a Chapter 13 plan. As we note below and as other studies have argued, many factors suggest that actual repayment may be significantly less than *ex ante* repayment capacity would suggest: the administrative and legal costs of executing means testing (which our proposal is intended to minimize), the potential for "gaming" means-test expense formulas and repayment thresholds, the limited actual success of voluntary Chapter 13 plans, the variability in debtor circumstances post-bankruptcy and the real possibility that debtors forced into an

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[1] Ernst & Young,"Chapter 7 Bankruptcy Petitioners' Ability to Repay", March 1998, with additional data provided to Treasury; Culhane & White, "Taking the New Consumer Bankruptcy Model for a Test Drive", December 1998, using the needs-based provisions of HR 3150; and Ernst & Young's March 1999 update based upon HR 833.

[2] Of those debtors with incomes between 75% and 100% of the national median, over 20% had some capacity to repay. Of those debtors with incomes between 100% and 150%, 37% had some capacity to repay.

involuntary Chapter 13 may be even less motivated to adhere to a repayment plan— all imply that actual repayment may be significantly below potential repayment. Thus, formulating a precise estimate of expected repayment is very speculative. Instead, we consider *potential repayment* - that is, the maximum possible repayment assuming that *none* of the factors just mentioned reduce repayment. We assume that debtors who would be moved by the means test have between median and average debt repayment potential for their income range. As we have argued, it is likely that repayment will be less. Moreover, repayment is probably disproportionately lower for the lower-income ranges, since administrative and other costs are more likely to exceed the repayment capacity of debtors in these income ranges.

What are the costs of means testing?

Additional Administrative Costs of Means Testing

The Congressional Budget Office estimated that the additional federal costs of last year's House bill would be $16-24 Million annually. This includes approximately $8 Million per year in costs for the U.S. Trustees due only to oversight of the means testing provisions and maintaining the tax information required by the testing, and $8-$16 million in additional judgeship costs due to the new burden on the court system of means test determinations and associated litigation.[3] We assume that these costs are unaffected by whether or not the means test is targeted effectively; this is likely to be a conservative assumption, because oversight and court costs would probably be reduced proportionally with the burden of the means test itself.

CBO did not estimate the additional costs for the *private* Trustees, who are responsible for the actual management of bankruptcy filings under the current system. Under the House bill, both Chapter 7 and Chapter 13 Trustees would be required to conduct a means test. These expenses will reduce the debt ultimately recovered by creditors. Chapter 13 Trustees' expenses are covered under current compensation rules. We presume the Chapter 7 Trustees' expenses for conducting the tests would be also covered by allowing an additional percentage of any repayment ability discovered, like their current law compensation in Section 326 (a) of Title 11. The current Senate bill gives responsibility for administering the Chapter 7 means test to the U.S. Trustees. In that case, the additional costs to the private Chapter 7 Trustees would be borne instead by the Federal government.

The additional private Trustee costs of means testing can be separated into the costs of determining the debtor's monthly total income, the monthly total allowable expenses under the IRS formulaic standards, the determination of the debtor's secured and priority monthly debt payments, and the assessment of nonformulaic, case-specific factors under the IRS' Other Necessary Expenses allowance.

[3] Cost Estimate, H.R. 3150, CBO, May, 1998

We developed evidence on the likely cost of each component of means testing from a number of sources. The Chapter 13 Trustee from the Northern District of California has estimated the additional costs to the private Trustees of means testing under H.R. 3150.[4] She reports that total out-of-pocket administrative expenses of the district (not including overhead) are likely to increase by about $90-110 per new case due to the full means testing requirement. The income-determination portion of the test accounts for a little more than half of this amount, with the remainder covering the determination of expenses and debt repayment. This is likely a generous assumption. Other experts we questioned (including bankruptcy trustees and IRS administrators) believed that income determination -- which only requires tax records and evidence on pay from current employment -- would be far simpler than assessment of case-specific expenses, and so would comprise a relatively smaller share of the cost of means testing. In contrast, assessment of case-specific expenses, including both nonformulaic expenses and debt payments, would be a far larger share. Based on these expert recommendations, we estimate the administrative costs per case for the income test would be around $20; the cost of the secured and priority debt determination would be around $40; and the calculation of case-specific expenses would be around $30-50 per case.[5] The high-end estimates assume more Trustee time for review of expenses. Presumably the Chapter 7 Trustees' expenses would also rise by comparable but slightly lower amounts, perhaps by about 75-80% of the Chapter 13 expense, as they will be performing much the same examination but do not apply this information in the formulation of a Chapter 13 plan.

Additional Attorney Costs

Debtors' lawyers' fees for a Chapter 7 filing have averaged about $800 per case, and, for Chapter 13 cases, have averaged about $1300 per case. Requiring the Chapter 7 attorney to apply a means test would increase fees, perhaps near to that of the average Chapter 13 fee. An income-only or formula-based screen would increase the Chapter 7 lawyer's costs by perhaps one-quarter of the difference between a Chapter 7 filing and a Chapter 13 filing today due to the additional demands upon the lawyer's time --by about $100-125 per case. (The attorney time could be considerably lower for an income-only screen.) A complete means test would increase debtor attorney costs by perhaps $200 per case.

Costs of Contesting a Finding

Additional administration and litigation expenses are incurred when debtors or creditors

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[4] Devin Derham-Burke, Chapter 13 Standing Trustee, N.D. of California, "Report on Cost to Administer Chapter 13 Cases under H.R. 3150", March, 1998.

[5] The estimates all assume that well-designed, standardized forms for expense reporting are developed, and that debtors must comply in good faith with providing the required expense information prior to Trustee review. Costs to the debtors of providing this information are not included in our calculations.

choose to contest a Trustee's conclusion with regard to ability to repay. Cases involving debtor challenges are assigned to the U.S. Trustee. We assume the debtors most likely to attempt to rebut a Trustee motion for dismissal will primarily consist of those "at the margin" of apparent ability to repay, for whom only a modest increase in expenses or adjustment in income could be the difference between satisfying the ability to repay criterion or not. Debtors who would most obviously fall into this category include those above 100% of median income who are estimated to be able to repay between 25-50% of debt, comprising about 3% of total Chapter 7 filers.[6]

Creditors are also likely to find it cost-effective to challenge filings by debtors who are at the margin of ability to repay and who have substantial outstanding debt, but who did not generate Trustee motions. This group of debtors probably has, on average, somewhat less favorable apparent repayment circumstances than those who do generate motions. Debtors who could most obviously fall into this category include the debtors above 100% of median income who are estimated to be able to repay between 0-25% of debt, comprising about 2% of total Chapter 7 filers. Thus, up to 5% or more of filings could result in further informal action and formal litigation after the means test, by both debtors and creditors.

The number of such cases, and the intensity of litigation, would be significantly smaller if the means test was applied with appropriate judicial discretion comparable to that now applied by the IRS - specifically, a standard of review in which the means test result creates a rebuttable presumption in the case of unusual circumstances. With such a standard, the Trustee would be able to address the case-specific factors that would lead debtors to believe that they would not succeed in Chapter 13 during the means-test review, rather than having to address them in subsequent, more costly litigation. Similarly, the Trustee could account for other factors that would likely affect repayment capacity, so that those who are moved would be significantly more likely to succeed in Chapter 13 – thereby making further litigation less likely to be viewed as worth the cost by either debtors or creditors. Without such discretion, debtors who truly believe that they will not do well in a Chapter 13 plan have little to lose by litigating, because their attorney fees will simply come out of their (already-limited) ability to repay used to determine their Chapter 13 plan. Similarly, a very strict "extraordinary" standard may cause creditors to pursue additional litigation, in the belief that they would have a better opportunity to overturn any judgment by the Trustee. *IRS collection officials indicate that they use considerable discretion in applying the collection financial standards to individual taxpayers, to avoid the additional administrative and legal costs associated with taking enforcement actions based on rigid standards; they have found that applying rigid standards is not cost-effective.*

The estimates of rates of further action following the Trustee's means test determination are consistent with those of the U.S. Trustees, who estimate that additional cases requiring action

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[6]We assume that few filers below 100% of median income would seriously contest a Trustee motion for dismissal, due in part to their limited willingness and ability to incur additional attorney costs.

by the U.S. Trustee due to challenges of motions for dismissal could total between 1-6% of current filings, and that a small share of cases (about 8%-10% of these actions, or 0.1-0.5% of filings) would go through complete formal litigation. The high-end estimates are based on the assumption that a large number of "marginal" Chapter 7 filers challenge. The Trustees estimate the total U.S. Trustee costs of these cases to be $2-11 million per year.[7]

Debtor attorney costs for these further actions would also reduce the debts ultimately recovered. Based on discussions with U.S. Trustees, we estimate debtors' lawyers hourly fees to be about $150-200/hour. Using the estimates of time requirements for additional actions and litigation developed by the U.S. Trustees for their own costs, we estimate the debtors' legal fees for additional administrative actions to be about $750-$1,000, and attorney costs for litigation, about $ 3,000-$5,000.

Notice Costs

The U.S. Trustees have estimated that the costs of providing notice to all creditors of the findings of the Trustee's investigation of the debtor's ability to repay are $5 - $10 million per year, as a result of mailing costs and associated administrative expenses. The Trustees have also noted that preliminary, easily verifiable information - such as information on debtor income - can be provided at the first meeting of creditors. Though we do not consider these savings in the following comparison, more than half of the notice costs (approximately $3-$5 million per year) could be avoided under the Administration proposal.

Cost and Debt Recovery Comparison of Administration and Current Bill Means Tests

Table 1 below summarizes the cost advantages of the "targeted discretion" means test. The principal reason that administrative and legal costs are much lower in the Administration proposal is that full means tests are avoided for the large share of Chapter 7 filers who, through simple screens, can be identified as having virtually no capacity to repay. The screens require only a determination of income and family size (for all debtors), and of debt expenses (for a large group of middle-income debtors). As the Table shows, screening out these individuals has essentially no impact on the debt recovery, because essentially all individuals with some repayment capacity are still subject to a full means test. Second, the Administration proposal also reduces administrative and legal costs by providing limited judicial discretion in reviewing the means test results, subject to clear presumptive guidelines. We have used conservative assumptions regarding the estimated reduction in challenges and further legal action; as noted above, IRS experience and consideration of debtor and creditor incentives to challenge the outcome of a nondiscretionary review in the 5% or more of bankruptcy filings that are close cases suggest that the savings could be significantly larger. The substantially lower cost of the Administration means test would significantly increase the repayment potential of Chapter 13

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[7] Communication from Executive Office of U.S. Trustees.

plans resulting from the means test.

What are the additional costs and benefits of referring debtors to Chapter 13?

In addition to the administrative and legal costs of means testing are the costs of the resulting Chapter 13 plans. These costs must be weighed against the benefits of additional debt repayment by the additional Chapter 13 filers resulting from the means test. It is likely that these costs would be higher and benefits lower compared to the voluntary Chapter 13 filings that occur today. In this section, we compare the consequences for debt repayment and additional administrative and legal expenses of the "targeted discretion" approach to the current House/Senate approach for debt repayment in Chapter 13.

Table 1 reports the repayment potential of debtors under each means test. As the Table notes, the targeted screen does not make mistakes for debtors with incomes above 75% of the median; virtually all debtors who can repay a nontrivial portion of their debt will be identified for potential movement to Chapter 13.[8] Thus, a key question is whether the limited discretion in the targeted test would lead to a significant reduction in debtors actually moved, and whether this reduction in turn would have a significant impact on actual debt repayment net of administrative and legal costs.

What share of debtors might meet a standard of "special circumstances" in determining access to Chapter 7 but not a standard of "exceptional circumstances"? Debtors with substantial ability to repay - that is, far above the repayment thresholds for the means test - are unlikely to be able to meet either standard except in truly unusual cases. The group most affected is likely to be those near the test threshold, that is, those with 25-50% repayment capacity according to the test. To provide an upper bound on the potential loss of repayment capacity, we assume that all debtors in this repayment range are able to convince the Trustee that they have unusual circumstances that make them unable to pay. (This is a truly extreme assumption; more realistically, only a subset of these debtors will be affected by the greater discretion, as well as a small share of debtors with greater apparent repayment capacity.) According to Ernst & Young estimates, less than one-fourth of filers who meet the means test (3.2% of the 14% who meet the test) are in this category. These debtors account for a significantly smaller share of potential repayments than their numbers suggest because they are close to the margin of the means test.

In actuality, the impact of the Administration's proposal for limited discretion on the debtors moved to Chapter 13 is likely to be much smaller than one-fourth of all debtors who meet the means test. About two-thirds of these "marginal" debtors are above 100% of median

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[8]As the Table notes, there is very slight repayment capacity in debtors with incomes less than 75% of median, who would be screened out under the targeted test. No studies have concluded this modest repayment capacity can be recaptured by any of the bankruptcy reform proposals.

income and would be subject to creditor motions, which creditors have appropriate incentives to bring if the debtors truly can repay. Because the share of repayment capacity in this "marginal" group is disproportionately low and because of the threat and use of creditor motions, we estimate that the impact of allowing limited discretion on actual repayment would be well under 10% of potential repayment. This "upper bound" on the reduction in repayment potential would be significantly offset by the reduction in administrative and legal costs from the reduction in the number of Chapter 13 plans that would fail, compared to a rigid means test.

Movement to Chapter 13 does not guarantee debt repayment. Debtors filing Chapter 13 voluntarily have had relatively low success rates. On a nationwide basis approximately one-third of those who file complete plans and receive a discharge, but the rates of plan completion and discharge vary widely by district. Available data on repayment rates is entirely local; most recently the Chapter 13 trustee for the Western District of Missouri reported that about 20% of district debtors completed their plan, and that those completing their plans repaid about 43% of their nonpriority unsecured debt.[9] Of the remainder, approximately 63% ultimately fail in their repayment plan and are either dismissed or converted directly to Chapter 7 (and many of those dismissed refile for Chapter 7, in worse financial circumstances, incurring the costs of means testing once again).

Success rates in Chapter 13 are likely to be particularly low for debtors who have marginal capacity to repay and who are close to the means-test limit. For example, consider a debtor judged by the means test to have 31% capacity to repay. If this debtor has any sort of unusual circumstances - such as the need to provide financial support for a nondependent parent or other relative, slightly higher-than-median work or personal expenses (e.g., because of longer commute distances or having a home in an area that is slightly more expensive than average) - then it is likely that either priority debt repayment will suffer or the Chapter 13 plan will be unsuccessful. The study by the Chapter 13 Trustee of the costs of H.R.3150 report that the administrative costs of failing Chapter 13 cases is significantly greater than for cases that succeed. The IRS has found that a significant number of "borderline" tax debtors have reasonable expenses that are not "median." To avoid the additional administrative expenses associated with failing tax collection cases and the legal expenses associated with the application of rigid standards, the IRS applies its standards with at least as much discretion as a means test that allowed for "special circumstances" would imply.

A means test with limited discretion to account for such unusual circumstances would avoid the additional administrative costs of a significant number of unsuccessful Chapter 13 plans. Thus, targeted means testing with limited discretion would allow the bankruptcy system to direct greater attention to determining the true repayment capacity of the subset of debtors who are likely to be able to repay a significant portion of their debt.

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[9] Hon. Arthur Federman, "What Means Testing Really Means--An Empirical Study," *Consumer Bankruptcy News*, April, 1999.

Table 1. Cost Comparison of Current Bill Means Test vs. Targeted Discretionary Testing

Income	*Share of Ch. 7 filers*	**HR 3150 Means Test**					**Targeted Discretion**				
		Share of Ch. 7 filers subject to full test	*Share of filers with repay-ment potential*	*Potential Repayment*	*Add'l adminis-trative costs*	*Add'l legal costs*	*Share of Ch 7 filers subject to screens*	*Share of filers with repayment potential*	*Potential Repayment*	*Add'l adminis-trative costs*	*Add'l legal costs*
<75%	54%	all	1.7%	<.09B*	$38-51 M	$86M	income screen:all full test: 0%	0	0	$8-9M	$43M
75-150 %	36%	all	9.3%	$.7B	$34-41 M	$142-146M	income/formulaic expense screen:all full test: 11.3%	9.3%	$.7B	$16-19M	$105-110 M
>150%	10%	all	4.7%	$1.9B	$9-12M	$137-141M	full test: all	4.7%	$1.9B	$8-11M	$113-117 M
Total	**100%**	**100%**	**16%**	**$2.6B**	**$81-104 M**	**$356-364M**	**21.3%**	**14%**	**$2.6B**	**$32-39M**	**$257-266 M**

*The total repayment capacity for this category of debtors is around $85 million. However, as Ernst & Young note, because of the absence of creditor motions and marginal capacity to repay of the few debtors in this category with any capacity to repay, it is very unlikely that any of this debt could be recaptured through means testing.

Conclusion

(I) A cost-effective screen should not examine low income debtors. It should expend resources examining debtors with some capacity to repay.

> The costs simply do not justify examining debtors with incomes below 75% of the national median to find those with any capacity to repay. A Chapter 7 filing by a debtor with income less than 75% of the national median should automatically be presumed not be abusive with regard to the means test.

(II) The optimal screen should minimally examine the disposable incomes of moderate income debtors, eliminating those who do not have the ability to repay, and giving a full Trustees' examination only to those remaining.

> Since one must examine on average 10 such debtors to identify 3 who can repay, it is not cost-effective to examine all of them fully. A minimal screen would calculate the debtor's ability to repay, basing the allowable expenses on only those portions of the means-test-allowed expenses that are set in formula. We do not make a mistake using this screen: debtors without the ability to repay formulaic amounts will clearly not be able to repay if consideration is given to all their expenses.

(III) Debtors with incomes greater than 150% of the national median should be fully examined, applying a means test.

Reaffirmations

Administration Proposal

The Administration supports the following reforms in bankruptcy law governing the approval of reaffirmations:

- Court review of reaffirmations that are least likely to be in the debtors best interest: court review is required for reaffirmation of unsecured debt and of secured personalty debt with original purchase price under $500, to determine that these reaffirmations are fully informed, voluntary, in the debtor's best interest, and do not pose undue hardship. In addition, costs and attorneys' fees cannot be added to these reaffirmations. This proposal is similar to the ABI proposal, which requires review for unsecured debt and secured debt of less than $3000.

- Guidance to determinations of whether the debtor is fully informed and whether the reaffirmation creates an undue hardship: An affidavit filed with the reaffirmation would create these presumptions.

  - A presumption that the debtor is not fully informed would be created if the affidavit did not include the model form on disclosure of financial terms developed by the Judiciary Committee.

  - A presumption that the reaffirmation presents undue hardship would be created if, when the cost of the reaffirmation is added to the debt expenses calculated in the means test, the debtor's income is insufficient to repay all nondischargeable debts.

  This guidance applies both for court review (where it is required) and for reaffirmations subject to review by the debtor's attorney.

- Notice and standing for domestic support creditors, allowing them to object to a proposed reaffirmation that is likely to jeopardize payment of their priority debt.

- No coercion: the Court must find that the agreement was not part of a threat, as in the current bills.

Current House and Senate Bill

The current House and Senate bills require that creditors who seek reaffirmation of wholly unsecured debts provide a disclosure that the debtor is entitled to a court hearing, and that the debtors can waive their rights to hearings if represented by counsel. Thus the court must hold a hearing to determine whether the agreement should be approved if: (1) the debtor was not represented by counsel (as in current law), or (2) has unsecured consumer debt and was represented by counsel but did not waive the right (which rarely occurs). The bills also require that the court must find that the agreement was not the result of a threat.

Background on Administration Position

The Administration agrees with the Bankruptcy Commission that debtors need to receive full and complete disclosure of the facts of reaffirmation agreements, that many reaffirmations involve terms that are far worse than those available elsewhere, that the existing attorney affidavit procedure provides inadequate protection from unfavorable reaffirmations. Thus, the Administration has sought additional protection against unwise reaffirmations. Along with the American Bankruptcy Institute, the Administration has endorsed court review of reaffirmations that are least likely to be in the best interest of debtors and priority creditors like divorced spouses. Such reaffirmations include unsecured debt and debt secured by small personalty items of little value, which are often the basis of reaffirmations that are very unfavorable and/or are the result of misleading or coercive offers by creditors. Finally, believing that debtors with adequate information and protection against coercion were capable of making wise decisions even in the case of unsecured credit, the Administration does not support a ban on reaffirmations of unsecured credit.

Accordingly, the Administration supported the reaffirmation reform proposed in last year's Senate bill, S. 1301. The Senate bill required that the reaffirmation agreement contain a clear disclosure of the components of the reaffirmed debt--principal, interest, late fees, creditor's attorneys fees and other costs of collection. In addition, in cases where the debt was unsecured or was for purchase of a personalty item of original value less than $250, the bill required the court to make a number of findings for approval, including finding that the agreement was in the debtor's best interest, did not impose undue hardship, was not the result of coercion, and was not excessive relative to collateral value. The Administration also sought further protections, by requiring that the court find clear and convincing evidence that the agreement was in the debtor's best interest and would not cause a hardship, and by applying the bill's provisions to debts for purchases of somewhat higher original value than $250. One criticism of the Senate proposal was that the bill language did not provide clear guidance for courts to use in deciding whether reaffirmations met the conditions for approval, so that reaffirmations would be costly to review and the diverse standards currently used by courts might continue to be applied.

This enhanced Administration proposal addresses the concerns about feasibility and clear guidance. It also builds on the new information on repayment capacity to be collected as part of the bankruptcy reform process – indeed, it applies the same results and standards to reaffirmations as the reform bills apply in the means test for determining ability to repay – thereby limiting costs of reaffirmation review and assuring that priority debts will be paid. Thus, the enhancements to the reaffirmation proposal make it largely self-executing.

Detailed Description of Administration Proposal

The proposal for "no coercion" is the same as the finding required in the current House and Senate bills. We describe below the specific guidance for whether "full disclosure" has occurred, and for whether the reaffirmation constitutes an undue hardship for the debtor.

Presumptions for affidavits/court approvals:

By providing clear guidance for courts, attorneys, and parties at interest in developing reaffirmations that are in the best interest of the debtor, *yet do not harm* priority creditors, the proposal would improve the quality of all reaffirmations without imposing significant new administrative burdens on the bankruptcy system.

(1) *fully informed*: Debtor is *presumed not to be fully informed* unless the creditor who is party to the agreement discloses credit terms according to forms provided by the Judicial Conference, and provides the disclosures to the court as part of filing. This form is provided at Attachment A. The disclosures included on the form are standard information that the debtor, the attorney, and the court need in order to assess whether the reaffirmation is in the debtor's best interest:

* the amount of the prepetition claim
* total amount of the reaffirmed debt, and component amounts attributable interest accrued, attorney fees, late fees, other costs relating to collection
* the monthly payment of the reaffirmed amount or, if the reaffirmation agreement extends new or additional credit, the minimum monthly payment on that amount
* annual percentage rate of interest (APR) and other types of finance charges and their manner of calculation, including but not limited to late fees, service fees, etc, assuming that Regulation Z applies to the transaction and treats it as a refinancing; separately, the same information for any new or additional credit extended[1]
* date payments start
* total number of payments made to satisfy the reaffirmed indebtedness, if paid on schedule
* if secured: date any lien is released, if payments are made on schedule
* if secured: description of collateral, value, and basis for valuation

Disclosures that meet these requirements create a presumption of full information.

(2) *undue hardship*: A proposed agreement is presumed to be undue hardship if, when all monthly payments in the proposed reaffirmation are added to the debtor's monthly expenses as calculated in the Section 707(b) means test, the total expense exceeds the debtor's monthly income. This test simply adds one line (the expense of the reaffirmation) to the ability to repay calculations that will be performed for all Chapter 7 debtors.
For debtors who undergo the full 707(b) means test, this calculation is straightforward - documentation on income, expenses, and nondischargeable debt payments not counted in expenses is filed as part of the case. The only additional information required of the debtor is the

[1] There is debate over the exemption granted to credit agreements that are the result of " court proceedings" in Regulation Z. This proposal does not suggest changing the exemption.

total monthly payment for the proposed reaffirmation; if the total expenses counting the reaffirmed debt are greater than the debtor's monthly income, the reaffirmation is presumed not to be in the debtor's best interest. For reaffirmations that do not involve a regular monthly schedule of payments, the debtor's total expenses over the period of the reaffirmation (including the total payments for the reaffirmed debt) are compared to the debtor's total income over the same period.

For debtors who are "screened out" of the means test under the Administration proposal, the debtor's monthly expenses are estimated to be 1.4 times the applicable monthly expenses under the IRS National and Local Standards for food, clothing and other items[2]; housing and utilities; and transportation. The "undue hardship" presumption is then whether the debtor's monthly income is greater than the sum of these monthly expenses, plus monthly payments on existing nondischargeable debts, plus monthly payments on the proposed reaffirmations.

The debtor may rebut a presumption of undue hardship by demonstrating circumstances that, despite the presumption, justify the proposed agreement. For debtors who were not subject to the full Chapter 7 means test or who did not have adequate ability to repay according to the means test, this would require documenting expenses and required debt payments to provide evidence that the reaffirmation does not jeopardize payment of nondischargeable debts. Any such evidence can also be used by the court as a factor in determining whether the Chapter 7 filing is presumed abusive, and/or in setting the terms of a Chapter 13 repayment plan.

Notice and standing for domestic support creditors

(1) *Notification*: The debtor must notify creditors owed child support and alimony payments of any proposed reaffirmation agreement with sufficient time to allow such creditors to object to the court's approving an agreement.

(2) *Standing for parties at interest*: A creditor with a domestic support claim may object to the approval of an agreement because of substantive or procedural defects on the grounds that the debtor's future income and/or expenses are not described adequately in the information provided by the debtor on capacity to repay and that the true capacity to repay is insufficient to protect his or her own claim adequately. If an objection is made, the court must hold a hearing.

(3) *Fee shifting*: The court may award the creditor all reasonable costs in bringing an objection, if the court grants the objection and finds that the position of the debtor who proposed the agreement was not substantially justified (as guided by the presumptions). The court may award the debtor all reasonable costs in contesting an objection brought by a party in interest if the

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[2] According to the data in the BLS's Consumer Expenditure Survey, average total consumer expenditures are about 40% larger than annual expenditures for the items covered in the National and Local Standards.

court does not grant the objection and the court finds that the position of the party in interest was not substantially justified, or that the party brought the objection solely for the purpose of coercing a debtor into waiving the right to reaffirm.

NY Times 5-9-99

How Much Protection For Bank Customers?

By DAVID CAY JOHNSTON

YOUR bank can collect details about your spending habits, like how much you charged last year at lingerie, liquor and lawn-and-garden stores, and then sell that information to companies that market bras, booze and bug killers.

And your bank is not required to tell you if it does. Nor can you do anything about it, except maybe pay for everything with cash (in which case your bank can collect and sell data on your A.T.M. use patterns).

Last week, President Clinton pressed for tougher laws to curb or at least improve disclosure of what he called banking-industry abuses like these. Consumer advocates say, however, that with the Government unlikely to afford adequate protections, bank customers must be wary.

The President wants to have banks improve disclosure of fees, charges and interest rates. Consumer groups say that bank customers shouldn't have to be corporate lawyers or accountants to comprehend what their banks are offering.

"Many people in this country are essentially math-illiterate, and they need information disclosed in terms that they can understand but that Congress is not requiring," said Gary Klein of the Consumer Law Center in Boston.

Mr. Clinton wants credit card issuers who lure customers with low teaser rates to state prominently how much they charge after the introductory periods — in some cases, more than 2 percent a month. For now, customers should concentrate not on the initial rates, often promoted even on the envelopes containing these offers, but on the regular rates, sometimes disclosed in small print and sometimes not at all.

Automated teller machines present special challenges. People who use A.T.M.'s operated by banks where they do not have accounts often have to go through several steps to learn whether and what they will be charged. Last week, the Senate approved a requirement that banks post charges on the machines.

Several of the President's proposals are meant to protect customers' privacy. Mary Griffin, a lawyer for Consumers Union, the nonprofit publisher of Consumer Reports magazine, wants Congress, at a minimum, to require full disclosure in plain English when banks sell information about their customers and their spending habits. Better yet, she said, customers should be able to block the sharing or sale of this information, as President Clinton has proposed.

But in the Senate, which last week passed a bill to repeal the core laws that have governed the banking industry since the Depression, the focus was much less on protecting consumers than on letting banks, insurers and securities firms enter one another's businesses.

The President says that as banks expand their domains, there is greater need for new restrictions and privacy protections. When one company can own a bank, an insurance company and a brokerage firm, he said last week, "you should not have to worry that the results of your latest physical will be used to deny your application for a mortgage or a credit card."

Consumer advocates also want Congress to prohibit banks from pitching insurance and investment products to people with pending loan applications, a practice they regard as coercive. Banks aren't allowed to turn down loan applicants for refusing to buy other products, but those seeking loans often have the opposite impression. Consumer advocates advise applicants to get their loans first, then choose insurance and investments separately and free from untoward pressure.

THE consumer groups say the President should have tried to give customers who buy securities from banks at least as many rights as those who buy from brokers. Most important, they say, are protections against being steered into unsuitable investments, like an especially volatile mutual fund or Internet stocks for an elderly widower with only modest savings.

Also missing from the President's proposals are limits on the rates banks can charge on loans or credit cards, consumer groups say. States used to set limits, but Congress, with the backing of the Supreme Court, has asserted its dominance.

Banks say the loosening of restrictions benefits many customers, because interest rates can be set according to each borrower's credit risk. While some people pay higher rates because of poor credit histories, the banks say, others now borrow at lower rates.

But with credit card lenders having to write off only 1 percent of the money owed them, Mr. Klein said, punitive rates are not justified.

While the President is threatening to veto the Senate bill for weakening regulations aimed at making sure banks lend in the inner cities, he has not listed the other consumer issues as veto bait.

Banking trade groups say that issues as complex as privacy and disclosure should be dealt with separately, rather than having them jeopardize legislation needed now. "These consumer protection issues," said Ed Yingling, chief lobbyist for the American Bankers Association, "are not germane to the bill."

But Stephen Brobeck, executive director of the Consumer Federation of America, said that the longer the delays, the greater the need to police bank practices. "Banks are pushing the envelope in every direction, testing consumers and regulators," he said. "And why? Because their consumer business is far and away their most profitable business."

Limited Improvements in the Means Test

All of these proposals improve the performance of the means test in identifying debtors who truly can repay a significant enough portion of their debt to make a Chapter 13 plan worthwhile, and/or lower the administrative costs of the means test. All can be implemented as specific, incremental changes in the current Senate bill. These proposals are all in addition to our proposal for appropriate, limited judicial discretion. *Status of proposals in italics.*

Development of Expense Standards Appropriate for Bankruptcy

Direct Dept of Justice (EOUST) in coordination with Treasury Dept. to develop expense standards appropriate for bankruptcy.

Hyde Amendment/ Nadler Amendment.

$100/Month Threshold for Means Test

Change the threshold from the percentage amount to a flat $100/month or $6,000 over 5 years, as it is now in HR 833.

Already in House bill (Hyde, Graham).

Means Test "Screens" to Reduce Administrative Burden

Safe harbor creating a presumption of nonabuse based only on income for those below median income.

Similar to provision in House bill (however, though no motions are allowed, bill still appears to require detailed means test and Trustee report on all filers).

Presumption of nonabuse for middle income debtors (100-150% median income) if they cannot pass the threshold based only on income, priority/nondischargeable debt payments, and formulaic expenses. These changes would reduce burden of means testing by over 80% - over $100 million/year in administrative and attorneys' costs - without missing any debtors who can pay.

Similar provision in Nadler; Administration proposal.

Additional Allowed Categories of "Other Necessary Expenses"

Administrative expenses and reasonable attorneys' fees (up to 10% of Chapter 13 expected payments).

In House bill.

Continuation of educational expenses of dependent child under 18, up to $10,000.

In House bill.

Continuation of charitable contributions.

In House bill.

Expenses for care of nondependent member of debtor's immediate family (child, parent, grandparent, or sibling of debtor, and of debtor's spouse in joint cases).

Expenses to maintain debtor and family safe from domestic violence.

Expenses for education, supplies, and other services that help debtor move from welfare to work.

Expenses associated with foster care or adoption.

New Administration proposals.

Limited Flexibility for Formulaic Standards for Categorical Expenses

Up to 10% adjustment to debtor's formulaic monthly expenses as specified by National and Local Standards, if debtor demonstrates such adjustments are "reasonably necessary" or " reasonable and necessary."

House bill includes 5% adjustment to food and clothing allowance if debtor demonstrates " reasonable and necessary." IRS reports larger problems for appropriately addressing variations in housing costs than for food and clothing.

Allowance for Current Income that Is Not Expected to Recur

Debtor required to provide documentation on income from past 6 months that is not representative of future income because of unusual circumstances, for example because of job loss or taking a new job. Trustee can consider this information in determining whether to file motion, and court in acting on it.

Nadler Amendment; possible Schumer Amendment.

Appropriate Adjustment of Median-Income Safe Harbors for Debtors in Large Families and with Support Obligations

If debtor is making child support or alimony payments to nonresident children or former spouse, relevant median income for determining debtor's safe harbor is increased by the amount of the payments.

Not yet proposed; discussed as Administration fallback.

Debtors with family size larger than four receive an additional increase in relevant median income for each additional family member ($592 per month per family member).

Similar provision in House bill; Nadler Amendment; Schumer Amendment; Administration proposal.

<u>Consideration of Additional Required Payments in Chapter 13 Not Included in Means Test</u>

In decision to bring motion of abuse and in evaluation of motion, Trustee shall consider additional expenses that are likely to be required in Chapter 13 plan but were not included in means test determination, e.g., required payments on arrearages, etc. Otherwise have debtors that meet means test but cannot work out repayment plan.

Nadler Amendment; likely Schumer Amendment; Administration proposal.

<u>Reasonable Flexibility in Implementing Chapter 13 Plans</u>

IRS "3 Year Rule": Debtor who can pay 100% of debt payments over 3 years is required to do so in 3 years, rather than taking all disposable income (per means test) to repay in less time.

IRS "1 Year Rule": Debtor with expenses higher than allowed expenses, but which are not reasonably necessary, is allowed one year to adjust allowed expenses; repayment for the first year is according to actual disposable income for the first year, not disposable income per means test.

IRS generally applies both rules in developing repayment plans under its guidelines.

Other Issues

Limited Improvements in Reaffirmations

Current Administration proposal: court review required for all reaffirmations of unsecured debt and low-valued (<$500) secured debt, guided by presumptions for undue hardship and full disclosure. A more modest proposal would require court review only in cases where clear "undue hardship" and "full disclosure" tests indicate a problem (review still required if debtor not represented by counsel or does not waive right to hearing, as in current Senate bill).

"Undue Hardship" Test

Determine whether means test shows positive ability to repay after adding reaffirmation payments. If not, presumed undue hardship and court review required.

"Full Information" Test

If full disclosure per terms developed by Judicial Conference (already in use in some districts), then debtor presumed fully informed. If not, court review required.

Protection of Child Support and Alimony Payments

Creditors owed child support and alimony given notice and standing to challenge proposed reaffirmation, on grounds that it jeopardizes debtor's ability to repay.

Moderation on Anti-Cramdown Provisions

Balance between rights of secured and unsecured (but often priority) debtors. For example, prohibition of lien stripping for autos purchased within 2 years of filing and all other goods within 6 months of filing.

Credit Card Disclosure Provisions

Items from recent Administration proposal.

Nondischargeability

Most important is probably increasing "safe harbor" for cash advances in 90 days before bankruptcy from $250 to something more reasonable, e.g., $1,000.

Dear Senator Schumer,

The Administration is deeply concerned by the [ ] incidents of violence, vandalism, and harassment perpetuated [*word choice???*] against family planning clinics. Some of these acts have resulted in the deaths and maiming of innocent people. The Administration believes [ ] that these unlawful activities must not be tolerated, and that when they are committed, those found **liable** should be held accountable under the law.

The Administration has a strong record of supporting efforts to end clinic violence. In addition to supporting the Freedom of Access to Clinic Entrances Act (the "FACE Act"), the Administration has made a modest request [*is there a reason why you use the modifier "modest?" -- are you not trying to draw attention to this? – if so perhaps we should leave it out completely*???] in **its** FY 2000 budget to provide security enhancements to clinics.

The FACE Act, **of which you were the principal House sponsor, and which** the President signed into law, provides federal protection against unlawful and violent actions while it protects the right to engage in peaceful picketing **and** protest unaccompanied by force or physical obstruction. Violators of FACE are subject to criminal penalties of imprisonment, a fine or both. In addition, the court may also assess civil [ ]penalties **for** a particularly egregious offense or against a repeat offender. State **clinic access laws and state and federal anti-racketeering laws** are additional tools used to prosecute clinic violence.

Unfortunately, **some defendants found liable for clinic violence are abusing the bankruptcy system in an effort to shield themselves** from civil monetary penalties assessed under these **laws. More specifically, these defendants are filing for Chapter 7 to discharge their obligations to the victims of their clinic violence and to escape responsibility for their actions.** In order to [ ] stem the tide of clinic-related **violence by ensuring that penalties for these acts are strictly enforced**, we support your amendment that would make court-ordered fines and debts resulting from clinic violence nondischargeable.

Although the Administration's **general** position has been **to oppose the expansion of nondischargeable debt**, we view your amendment as an important tool in our current efforts to end this type of violence. [ ]

Certainly, one could argue that damages awarded for all intentional torts should be nondischargeable. Indeed, this is largely the case under the "willful and malicious injury" exception contained in Section 536(a)(6) of the Bankruptcy Code. Some damages resulting from clinic-related violence, however, are not protected under this exception. This is made clear by the Supreme Court's recent decision in <u>Geiger v. Kawaauhau</u>, 523 U.S. 57 (1998), in which the Court held that the word "willful" "modifies the word 'injury' indicating that nondischargeability takes a deliberate or intentional injury, not merely a deliberate or intentional act that leads to injury . . ." Although some clinic-related violence is committed with the direct intention to inflict injury, some such violence indirectly results in injury. Take for example a family planning clinic which is bombed at night. The perpetrator may not know that some of the clinic's employees are working late and still in the building. The

bomb, nonetheless, still injures these employees. Should damages awarded to victims such as these be any less protected simply because the bomber did not *intentionally* intend to injure them with his or her bomb?

In addition, there is another compelling reason to create a specific nondischargeability carve-out for clinic-related violence damages. There are numerous reports of those who have been found liable for such acts blatantly – even enthusiastically – announcing how they are going to escape responsibility for their actions by filing for Chapter 7. Indeed, such abuse of the bankruptcy system appears to be part of a concerted plan on the part of these perpetrators to perpetuate their acts of violence and intimidation.

This issue and your amendment are not about [ ]abortion. Reasonable parties on both sides of this **matter** agree that violence against clinics should not be tolerated. This is why we have laws in place designed to deter such activity. We must not permit those who have **committed odious acts of violence to escape responsibility for their actions. Your amendment goes a long way toward achieving this goal.**

Reaffs
credit card
Homestead
Means Test

The Senate Bankruptcy Amendments as of May 12

General Disclosure/Creditor Responsibility Amendments: not enough right

(1) The Moran Disclosure Amendment from the House debate;
(2) Hatch reportedly okay with: (a) Feinstein back-end credit extention amendment; and (b) the Fed study from last year. (figure out

Durbin:

(1) S. 1301 as a substitute;
(2) Consumer credit disclosure provisions form S. 1301 (as a whole or in pieces);
(3) The Durbin "means-test" or "needs based bankruptcy."

Kennedy:

(1) *Maybe* reaffs; yes
(2) Non-germane amendment (patients or minimum wage).

Sarbanes:

(1) Consumer credit disclosure provisions (perhaps with or in addition to Durbin). his bill sup.

Leahy:

(1) Consumer credit privacy provisions of S. 187; right dir
(2) IRS records privacy.

Biden:

(1) Median income safe harbor.

Kohl:

(1) Homestead;
(2) Cram downs. 2 or 3 yrs – autos

Feinstein:

(1) Back-end credit extension amendment.

Torricelli:

(1) *Maybe* Hyde.

Schumer: → Leahy

(1) Small business exemption to replace provision which would exclude creditors attempting to collect a debt of less than $1,000 from the creditor abuse protection sections;
(2) FACE amendment;
(3) Means-test replacement;
(4) Smaller means-test fixes (e.g., 5 to 3 years, consideration of administrative costs, etc);
(5) TILA provisions from the Schumer bill.

Feingold:

(1) Attorney fees shifting;
(2) In forma pauperis;
(3) Credit counseling exigent circumstances expansion;
(4) Apartment automatic stay amendment;
(5) A carve-out making FEC damages nondischargeable.

Treas 5/12

Protection of retirement savings

Section 203 of HR 833 and 224 of S. 625 exempt from the bankruptcy estate a qualified retirement fund, pursuant to certain standards. The effect of the amendments would be to enhance debtors' ability to prevent their interests in tax-benefited retirement accounts and funds, including Individual Retirement Accounts, from being used to satisfy their debts. The Administration has made encouraging adequate retirement savings a singular priority. We recognize that a fresh start is not meaningful if it requires the debtor to accept an impoverished retirement. However, a debtor should not be able to shield abundant resources from creditors, including federal, state and local governments, in the form of retirement savings. In addition, the amendments lack any safeguard against contributions made from proceeds of a fraud. Finally, and of lesser importance, the jurisprudence on the treatment of true spendthrift trusts and tax favored savings plans is confused; and clarification would be useful. We could propose the following:

(1) *fraud*: amounts in trusts or tax-favored plans cited in the two bills that arise from fraud and to which an order of restitution would apply under applicable nonbankruptcy law are not excluded from the estate

(2) *amounts held in plans*:

(A) *cap*. amounts retained in such plans, contracts, funds, or trusts in excess of $250,000 [higher] shall not be excluded from the estate

(B) *lookback*. if the debtor converts property that is nonexempt to amounts in such plans, contracts, funds, or trusts, in the 2-year period ending on the date of filing of the petition, such property shall not be exempt under this section to the extent that the value of the converted property exceeds $100,000.

(3) *contributions:*

(A) *current bill*: proposals that repayments of a loan, if applicable, are not subject to the automatic stay

(B) *explicit necessary expense:* continuation of most recent [3 year average] amounts from wages and collection of amounts withheld into tax favored savings plans established under Internal Revenue Code up to average over past three years of such amounts