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WAGE EARNER PLANS UNDER THE BANKRUPTCY ACT

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HEARINGS

BEFORE

SUBCOMMITTEE NO. 4

OF THE

COMMITTEE ON THE JUDICIARY

HOUSE OF REPRESENTATIVES

NINETIETH CONGRESS

FIRST SESSION

ON

H.R. 1057 and H.R. 5771

BILLS TO AMEND THE BANKRUPTCY ACT WITH RESPECT TO THE
USE OF CHAPTER XIII

MAY 24 AND 25, 1967

Serial No. 10



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WAGE EARNER PLANS UNDER THE
BANKRUPTCY ACT
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WAGE EARNER PLANS UNDER THE BANKRUPTCY ACT

WEDNESDAY, MAY 24, 1967

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE No. 4
OF THE COMMITTEE ON THE JUDICIARY,
Washington, D.C.

The subcommittee met, pursuant to call, at 10 a.m., in room 2141, Rayburn House Office Building, Hon. Byron G. Rogers (chairman of the subcommittee) presiding.

Committee members present: Representatives Rogers, Whitener, Conyers, Jacobs, McClory, Wiggins, and Poff.

Staff members present: Benjamin L. Zelenko, counsel, and Donald E. Santarelli, associate counsel.

Mr. ROGERS. The committee will now come to order. Today the Subcommittee on Bankruptcy and Reorganization begins hearings on H.R. 1057 and H.R. 5771, bills that have been introduced by our subcommittee colleague from Virginia, the Honorable Richard H. Poff, and by another subcommittee colleague, the Honorable Robert McClory, of Illinois. These are identical bills which would amend the Bankruptcy Act relative to the use of chapter XIII.

Chapter XIII was enacted into law by Congress as part of the Chandler Act of 1938. Under chapter XIII an insolvent debtor may choose to pay out of his future earnings his obligations pursuant to an extension or composition. Under section 606 of the Act a wage earner is today defined as "an individual whose principal income is derived from wages, salary, or commissions."

The chapter XIII procedure permits the debtor to discharge his debts under judicial supervision without greatly risking the loss of employment or possessions. The fundamental feature of the operation of the wage earner plan is that its use is at the option of the debtor. It is a voluntary alternative to bankruptcy.

The bills before the subcommittee would authorize the bankruptcy referee to deny bankruptcy relief upon a determination that the petitioning debtor has failed to establish that he cannot obtain "adequate relief" under chapter XIII. In such circumstances, the bills require the referee to vacate the order of adjudication and dismiss the proceedings unless the debtor amends his petition to one for a wage earner plan under chapter XIII.

The proposed legislation has generated much discussion and conflicting opinion. The subcommittee has invited representatives of various groups and organizations which have indicated an interest to appear and testify.

At this point, the bills, H.R. 1057 and H.R. 5771, the subject of the hearings, will be placed in the record.

(The documents referred to follow:)

[H.R. 1057, 90th Cong., first sess.]

A BILL To amend the Bankruptcy Act with respect to the use of chapter XIII

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 55(b) of the Bankruptcy Act (11 U.S.C. 91(b)) is amended to read as follows:

"b. At the first meeting of creditors, the judge or referee shall preside and, before proceeding with other business, shall, if the bankrupt is a wage earner within the meaning of subsection (8) of section 607 of this Act, determine whether the bankrupt has shown that adequate relief cannot be obtained under chapter XIII of this Act. In the event that the judge or referee shall determine that the bankrupt has failed to make such a showing, he shall enter an order vacating the order of adjudication and dismissing the bankruptcy proceedings with notice to all of the bankrupt's creditors, unless, within such time as the judge or referee shall fix, the petition be amended to comply with the requirements of chapter XIII for the filing of a debtor's petition. In the event that the bankrupt is not a wage earner or shall make such a showing as aforesaid, the judge or referee may then allow or disallow the claim of creditors there presented, and shall publicly examine the bankrupt or cause him to be examined, and may permit creditors to examine him."

[H.R. 5771, 90th Cong., first sess.]

A BILL To amend the Bankruptcy Act with respect to the use of chapter XIII

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 55(b) of the Bankruptcy Act (11 U.S.C. 91(b)) is amended to read as follows:

"b. At the first meeting of creditors, the judge or referee shall preside and, before proceeding with other business, shall, if the bankrupt is a wage earner within the meaning of subsection (8) of section 607 of this Act, determine whether the bankrupt has shown that adequate relief cannot be obtained under chapter XIII of this Act. In the event that the judge or referee shall determine that the bankrupt has failed to make such a showing, he shall enter an order vacating the order of adjudication and dismissing the bankruptcy proceedings with notice to all of the bankrupt's creditors, unless, within such time as the judge or referee shall fix, the petition be amended to comply with the requirements of chapter XIII for the filing of a debtor's petition. In the event that the bankrupt is not a wage earner or shall make such a showing as aforesaid, the judge or referee may then allow or disallow the claim of creditors there presented, and shall publicly examine the bankrupt or cause him to be examined, and may permit creditors to examine him."

We shall first hear from our colleague, the Honorable Richard H. Poff, sponsor of H.R. 1057.

Mr. Poff has been a Member of Congress for many years, and served with considerable distinction from the great State of Virginia, and is an honored member of this subcommittee. We would be pleased and most happy to hear from you at this time, Mr. Poff.

STATEMENT OF HON. RICHARD H. POFF, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF VIRGINIA

Mr. POFF. Mr. Chairman and my colleagues on the subcommittee, first, may I express my sincere appreciation for the kind comments you have seen fit to make, and to reciprocate them in fullest measure.

Indeed, it has been a number of years, to be precise, now, nearly 15, and I have so much enjoyed the good fellowship of my colleagues, and have learned a great deal at their hands, I count myself most fortunate indeed.

The chairman has been gracious in acceding to my request for hearings on this legislation. As he has indicated, it is indeed controversial.

That fact does not intimidate me. We in Congress are accustomed to controversy, and here in this anvil of democracy, we will attempt to hammer out the conflicting views, and see if we can arrive at a conclusion which represents the composite judgment of this body, and of the other body, and if we are successful, hopefully the President will sign the measure into law.

In the interest of time, Mr. Chairman, I shall not address myself in full detail to the subject orally. Since we have a number of other witnesses scheduled today, all of whom are learned in the field, and who will be able to bring more expertise to bear upon this subject than I, I will make a brief oral summary of the bill, and ask your permission, sir, to insert at this point in the record a statement which I have prepared in explanation of the bill.

Mr. ROGERS. We will be most happy to receive that statement, and we will insert it in the record at this point.

(The document referred to follows:)

STATEMENT OF HON. RICHARD H. POFF, A REPRESENTATIVE IN CONGRESS FROM
THE STATE OF VIRGINIA

Consumer bankruptcy in the United States is beginning to assume alarming proportions. We are witnessing a "Personal Bankruptcy Explosion." Between 1940 and 1966, nonbusiness bankruptcies increased from 40,000 to 176,000, a jump of more than 420%. As a percentage of total bankruptcies, the figures are even more dramatic. In 1940, the figure was 25%, in 1966, it was 91%. Dollarwise, the loss, once counted in thousands, now runs into hundreds of millions.

Unquestionably, these statistics have a nexus with the growth of installment sales. In 1940, consumer credit outstanding was \$9.2 billion; today, it is about \$93 billion. That there is a nexus, however, is no indictment of installment sales. On the contrary. Deferred payments for present enjoyment of goods and services is, as an institution, a wholesome and healthy product of the American free enterprise system. Making it possible for people to use things they otherwise would have to forego, this institution has facilitated purchases, stimulated production, inspired the inventive genius, promoted industrial growth, created new jobs and in general elevated the American standard of living to a plateau mankind has never known before.

No, it is not the growth of installment sales which deserves the indictment. The blame for the personal bankruptcy explosion belongs elsewhere. It belongs not with the institution but with the methodology of the institution. The misuse and abuse of the system. It belongs, too, with changes that have taken place in society's attitudes about principles, values and priorities. With these changes, every echelon of society, material and spiritual, must be concerned.

It is impossible with any degree of precision or finality to inventory and define all the root causes of the tragedy of consumer bankruptcy. This is because the consumer is a human being, and human beings are all different. They are motivated differently. They are oriented differently. They are gifted differently. They are handicapped differently. They live in different environments. They are beneficiaries or victims of different fates. So, in large part, we must be content to deal with surface rather than root causes of this human tragedy.

Even in this limited area, we are likely to fall into the vice of oversimplification. Assuming that hazard, I will undertake to outline the dreadful process which ends in personal bankruptcy. The tragedy is in three acts. The first act might be entitled "The Consumer Becomes Overextended," the second, "The Camel's Back Is Broken," and the third, "The Hateful, Fateful Decision is Made."

In the first act, our hero appears. He is not the villain. If he were, the plot would be uncomplicated. A villain would be dishonest, unprincipled, ruthless and unrepentant. He would deceive his friends, incur debts, quit his job, live high, de-

fault his obligations. Take bankruptcy and, with a disdainful twist of his mustache, slink away and begin to play his role again on another stage.

No, the central player in our little skit is a hero, and for that reason, the plot is more complicated. Our hero is innocent, honest, proud and well intentioned. He loves his God, his country and his family, works hard and earnestly tries to pay his debts. True, he may sometimes be unwise and imprudent. But he means well.

Then things begin to happen. His son wrecks the car. His wife becomes bed-fast. A new labor-saving machine takes his time-and-a-half pay. Earnings drop, bills pile up.

These bills were extraordinary and unexpected. In the meantime, he has been imprudent. In the full blush of health and wanting the best for his family, he has paid cash for the necessities and signed notes for the niceties. Even some of the necessities were acquired under his new credit card. What has happened has been largely his fault, but not altogether. He and his family have been reading the newspaper ads and listening to the TV commercials. "A dollar down and a dollar a week" has a tremendous appeal, particularly for those who otherwise must deny themselves things others buy for cash. And it sounds so easy and so safe!

And often it is easy—easy to make the purchase. The merchant, depending upon large volume turnover, doesn't want to frighten the customer across the street to his competitor. Time is money and often he can't afford the time it takes to analyze the customer's family budget or to obtain a reliable credit investigation. Then, too, the merchant knows that no matter how hard he tries he cannot always get accurate information about the customer's other debts and contract commitments. So, he makes the sale and hopes for the best.

And suddenly and surprisingly, our hero finds himself overloaded with "easy payments." Then, all the merchants, the cautious merchants who investigated and the careless merchants who were too busy or too indifferent to investigate, wake up one morning all in the same sorry bed.

All of which brings us to the second act and "The Camel's Back Is Broken."

Already the beast is carrying a bale of straw, and there are many straws scattered on the ground. Here again we must remember that the principal player in this drama is not the villain. If he were a villain, he would need no new straw to break the camel's back. He would simply hide his physical assets, jump in his new gold Cadillac beside his chauffeur, ride down to the referee's office and file his bankruptcy petition.

No, our hero is still holding on. If he happens to live in a State which has realistic debt collection laws, he may yet save the camel's back. However, these laws in many States are unrealistic and unwise, from the standpoint of the creditor as well as the debtor. In some States, the garnishment laws tie up the debtor's salary or wages for unreasonable periods before he is able to establish the exemptions to which he is entitled under the law. The delay is sometimes protracted, especially when the laws require the debtor's employer to file monthly affidavits in response to garnishment process.

Such laws, theoretically designed to protect creditors' rights, often prejudice them by tilting the delicate balance between solvency and insolvency. Sometimes, they are the last straw. If the debtor loves his family (and our hero does) and if he is frustrated in establishing the exemptions necessary to feed, clothe and shelter his family, his anxiety takes him to his lawyer's office. And if more than one creditor descends upon him, his anxiety becomes desperation and his next stop may be the referee's office.

This brings us to the third and final act. "The Hateful, Fateful Decision Is Made." Bankruptcy, or something else? Here, we reach the heart and moral of our three act play. If our hero had played the part of the villain throughout, the decision would have already been made. If the villain is able to conceal his misdeeds and if his creditors are unable to prove fraud, his discharge is granted and the scenario is over. But our hero must decide. Bankruptcy, or something else?

The difficulty is that too few know that a choice is available. They don't know there is "something else." Our hero doesn't know anything about the bankruptcy law. His own lawyer may know something but not everything about the bankruptcy law. Even if he does know about chapter XIII, he may not have had any previous practice under the chapter, and it's always easier and faster to follow familiar procedures, particularly if he is unskilled in the intricacies and complexities of family finance. Then, too, some of his creditors who do know something about chapter XIII don't like what they know.

Unhappily, a few creditors actually prefer that the debtor take straight bankruptcy. Knowing that the debtor with a discharge in his pocket is ineligible for straight bankruptcy again for another 6 years, they actively seek him out and urge new credit upon him. But happily, such creditors are a miniscule minority. The overwhelming majority of creditors, like most debtors, are honest and humane.

Altogether too many events and circumstances conspire to discourage recourse to chapter XIII. This is a great pity. A pity for the creditors and a pity for the debtor. Added to the bankruptcy statute in 1938, the chapter permits the debtor to avoid the stigmatic consequences of bankruptcy by paying his debts out of future earnings. With the consent of a majority of his creditors in number and amount, he can make regular deposits with the trustee who applies the money to payments of all debts over a three year period.

A chapter XIII proceeding offers the debtor a host of benefits, the nature and extent of which are known to few lawyers and practically none of their clients. Let me list some of them.

(1) The so-called "wage-earner's plan" suffers from a misnomer. Its benefits are available to the salaried employee as well as the wage earner.

(2) Every exemption available to the debtor in straight bankruptcy is available to him under chapter XIII proceedings.

(3) Any contract into which the debtor has been enticed by fraud or misrepresentation to enter can be either reformed or annulled.

(4) In proper cases, interest and finance charges or unsecured creditors' claims can be reduced or eliminated.

(5) Certain types executory contracts may be revised or rejected.

(6) During the dependency of the proceedings, collection suits, garnishment process and involuntary bankruptcy petitions can be suspended.

(7) Even after the plan has been approved and put into operation, deposits required of the debtor under the plan can be reduced in amount or time can be extended if the debtor later experiences unforeseen hardships.

(8) At any time during the proceeding, if it becomes apparent that the debtor cannot in fact meet the requirements imposed upon him under the plan, the referee can restore the debtor's right to pursue straight bankruptcy.

(9) Finally, at the end of the three year period, if the referee is convinced that the debtor made a good faith effort to abide by the plan, he can grant him a discharge even though the debtor may not have completed all of the payments.

In summary, it is fair to say that the debtor loses none of his rights and gains many benefits by pursuing the procedures of chapter XIII.

The advantages to creditors are equally attractive. True, some creditors, especially those who are unfamiliar with chapter XIII, are reluctant to consent to a plan which suspends their collection rights and defers the maturity of their claims for a three year period. They fail to take into account the single alternative, and that alternative is straight bankruptcy and discharge of part or all of their claims. Most consumer bankruptcies are no-asset cases.

Those who authored chapter XIII back in 1938 had great hopes for it. Their hopes were not in vain. Today, in some judicial districts, the large majority of all consumer petitions are chapter XIII filings. In 1964, for example, 88.4% of all employee cases in the Southern District of Alabama were in that category. In the Eastern District of Arkansas, the figure was 71.5%, and in the Southern District of Georgia, 73.5%. Indeed, in 9 judicial districts, the figure was more than 50%.

However, the authors' hopes have not all materialized. Far from it. In only 29 judicial districts did chapter XIII petitions represent more than 15% of total employee filings, and in 10 districts, the figure was less than 1%. The national average in 1964 was only 19%.

Notwithstanding these rather bleak statistics, the basic merit of the wage-earner plan is reflected in the fact that this program that year kept thousands of honest debtors out of the roll call of bankrupts and returned some \$8 million to patient, sympathetic creditors.

It is, I repeat, a great pity that chapter XIII is so little used. In recent years, four great universities have conducted exhaustive research in this field. Their conclusions, while not statistically unanimous, are remarkably identical. They agree that from 25 to 50 percent of salaried or wage employees who petition bankruptcy courts for a straight discharge could, under proper chapter XIII plans, pay their debts out of future earnings without undue family hardship.

One example illustrates the point. In Michigan, a single man with no dependents earning \$5,500 a year filed a petition in bankruptcy. He had one secured creditor with a claim of \$320 and several unsecured creditors whose claims totaled \$556.63. After claiming all available exemptions, he could have paid all of his debts over a three year period by depositing with a trustee \$3.60 per week.

For the sake of the creditor, for the sake of the debtor and for the sake of the Nation's economy, something should be done to stimulate greater utilization of chapter XIII. This I have tried to do. As a member of the Bankruptcy Subcommittee of the Committee on the Judiciary, I have introduced a bill numbered H.R. 1057. I hasten to add that I have no patent on the bill. It has been introduced in identical or similar form in earlier Congresses. However, I love my adopted child as much as the natural parent.

This legislation is addressed to section 55(b) of the Bankruptcy Act. At the first meeting of creditors after the order of adjudication has been entered. The judge or referee is required to determine whether the bankrupt has shown that adequate relief cannot be obtained under chapter XIII. If not, he will enter an order vacating the order of adjudication unless the bankrupt files a chapter XIII petition.

It will be seen that this amendment does not impair the debtor's right to file a bankruptcy petition. Neither does it affect his right to a discharge. Necessarily, the burden of proof is upon the debtor; only he has access to the evidence bearing upon his ability to pay his debts out of future earnings. As to whether the burden of proof has been borne the decision rests, not with the creditors, but with the court. And the court's discretion would not be absolute. The Judicial Conference, which has already written certain guidelines for the administration of chapter XIII proceedings, would be expected to lay down rules and formulae to guide the court and protect the prostrate debtor. Only when the court finds that the debtor's prospective income is sufficient to meet future family needs and amortize his debts over the three year period would his right to proceed in straight bankruptcy be suspended.

This seems eminently sound and reasonable to me. Its very flexibility is its chief virtue. The simplicity of its mechanics helps to educate consumers, creditors and lawyers to the availability of a workable alternative to bankruptcy. One would think that this bill would sell itself. But not so. Some oppose it.

Some of the criticisms are a little difficult to understand. It has been said that this bill would create new and insurmountable administrative burdens which the referees in bankruptcy could not carry. If this criticism had substance, then referees could be expected to oppose it. My judgment is that most referees are dedicated public servants who will welcome this proposal, and whatever additional burdens might be involved they will be glad to carry. Certainly, no one has proved otherwise.

Another criticism aimed at this legislation is that it would undermine the original social purpose and violate the spirit of the bankruptcy laws by converting a voluntary procedure into an involuntary procedure. Some have even hinted that it is unconstitutional. Let us examine this criticism in its several parts.

Article 1, section 8, clause 4 of the Constitution reads in pertinent part: "The Congress shall have power . . . to establish . . . uniform laws on the subject of bankruptcy throughout the United States."

Under this language, Congress clearly has the power to impose such terms. Limitations and conditions on the right to pursue bankruptcy as it may consider fair to all.

What the purpose and spirit of the bankruptcy laws were intended to be might vary from author to author. In 1898 when our basic Bankruptcy Act was enacted, our American system of consumer credit had not yet been born. However, one of the principal authors of the Chandler amendments, Professor James McLachlan, Hastings College of Law, has written a compelling defense of the principle of legislation similar to H.R. 1057.

It is a trifle misleading to say that this bill would make involuntary what is now voluntary. It is more precise to say that the petitioner's right to proceed in straight bankruptcy would be postponed pending inquiry into his present and prospective financial situation. If the debtor shows that his debts are too great and his income is too small to meet deposit requirements without undue family hardship, then his choice to pursue straight bankruptcy is immediately restored. Even after the plan has been put into effect, that same choice remains available to him.

There may be other criticisms. There always are whenever change is ventured. But the change I propose here is neither revolutionary nor radical and the

criticism should not be reactionary. What I propose is in the enlightened best interests of all. True, in our little three-act drama of consumer bankruptcy, H.R. 1057 will frustrate the villain; but, equally important, it will illuminate the existence of chapter XIII and point our honest hero and his attorney down the avenue of hope, rehabilitation and self-respect.

Mr. ROGERS. Proceed in your own manner.

Mr. POFF. I thank the chairman. As the chairman has already carefully explained, chapter XIII was added to the bankruptcy law in 1938 as a part of the Chandler amendment. It was designed, as he has said, to afford the hard-pressed debtor the opportunity to pay his accumulated debts over a 3-year period, out of the future earnings.

At the time chapter XIII was enacted, it was felt it would be one of the more humane alternatives available to the debtor and would serve a useful function in rehabilitating the bankrupt, and restoring him to a useful posture in the Nation's economy, making it possible for him to become once again a taxpaying citizen.

The prospects were not entirely realized in practice. Strangely, some districts used chapter XIII proceedings more than others. Just in order to dramatize what I mean, Mr. Chairman, I understand that in 1964, some 88.4 percent of all employee cases filed in the southern district of Alabama were in the chapter XIII category.

In the eastern district of Arkansas, the figure was 71½ percent, and in the southern district of Georgia, 73½ percent. In the Nation at large, for nine judicial districts, the figure was in excess of 50 percent.

On the other hand, in some 29 judicial districts, chapter XIII petitions represented no more than 15 percent.

The national average that year, 1964, was only 19 percent. It is impossible, of course, to rationalize fully the divergence of statistics. Why chapter XIII would be used so much in one district and so little in another is something not clearly understood by the profession, or by the Congress.

However, one explanation is that the procedures of chapter XIII are so little known, certainly to debtors, and unfortunately, to much of the bar at large. Then, too, the procedures of chapter XIII sometimes involve somewhat more complexity in practice than a straight bankruptcy proceeding.

In any event, there is a large disparity in the statistics, and possibly this is attributable, at least in part, to the fact that chapter XIII is so little known.

Now to speak to the bill itself, the legislation is addressed to section 55(b) of the Bankruptcy Act. At the first meeting of the creditors after the order of adjudication has been entered, the judge or referee is required to determine whether the bankrupt has shown that adequate relief cannot be obtained under chapter XIII.

If not, he will enter an order vacating the order of adjudication unless the bankrupt files a chapter XIII petition.

Now it will be seen, Mr. Chairman, that this amendment does not impair the debtor's right to file a bankruptcy petition, initially, nor does it deny his right to a discharge, ultimately. Necessarily, the burden of proof rests upon the debtor, because only he has access to the evidence bearing upon his ability to pay his debts out of future earnings.

Now as to whether that burden of proof has been borne, the decision rests, and I think it is important to emphasize, the decision rests not

with the creditors; it rests, rather, with the court, and the court's discretion itself will not be absolute.

The judicial conference, which has already written certain guidelines for the administration of chapter XIII proceedings, would be expected to lay down rules and formulas to guide the courts and protect the prostrate debtor, and only when the court finds that the debtor's prospective income is sufficient to meet future family needs and amortize his debts over the 3-year period would his right to proceed in straight bankruptcy be suspended.

Mr. Chairman, I think it is fair to say that procedures under chapter XIII afford the debtor all those rights, exemptions and safeguards he would otherwise enjoy under the Bankruptcy Act, and in addition thereto, vest in him opportunities which other parts of the Bankruptcy Act would not give him.

What is available to him is the opportunity to come to know that there is such a thing as chapter XIII. That opportunity exists today only if the attorney he chooses is knowledgeable in the field of chapter XIII proceedings, and when the referee encourages the use of those proceedings.

Mr. Chairman, the bill I have introduced this year, 1057, is identical to bills which have been introduced in the past. One of these was H.R. 297, introduced in the 89th Congress, by request, I understand, by our distinguished chairman of the full committee, the Honorable Emanuel Celler, of New York.

I do not choose, Mr. Chairman, unless you care to interrogate me, to go further into the details of the legislation at this point, in order that hopefully, we may conclude evidence today.

Mr. McCLORY. Will the gentleman yield?

Mr. POFF. I will be glad to yield to my colleague.

Mr. McCLORY. I thank the gentleman for yielding, and I just want to add this comment. I am proud to support this legislation, and to recognize the leadership of the gentleman from Virginia in sponsoring this measure. I think that it should contribute a great deal toward recognizing in this Nation individual responsibility, and recognizing that the bankruptcy laws are there for the purpose of providing a solution to those who are without the means to defray their obligations, but at the same time, they are not there for the purpose of lowering any individual responsibility for any overt desire to disregard their lawful obligations that they have the capacity to meet, and I am proud to associate myself in support of this legislation with the gentleman from Virginia, and compliment him on taking a leading role in presenting this measure to the committee.

Mr. POFF. I thank my distinguished colleague, and in conclusion, Mr. Chairman, in order that we may proceed, may I say that the language of the bill as it now appears confines itself to the wage earner, salary earner type petitioner.

I am prepared, if the subcommittee feels it wise to do so, to offer an amendment to the bill addressed to chapter XIII itself, which would alter the definition of the words to make the reach of this legislation cover all natural persons who file petitions.

Mr. ROGERS. Thank you, Mr. Poff. As you point out, we are trying to hear many important witnesses this morning, and the only thing that I may suggest is that we would like in the future to adequately

discuss part of your bill, particularly lines 8 and 9, where it says, "determine whether the bankrupt has shown that adequate relief cannot be obtained under chapter XIII of this Act."

That is, we will want to discuss what that means as to adequate relief in the future. However, we shall now proceed with the witnesses before us. As we all know, the Administrative Office of the U.S. Courts has a Bankruptcy Division, and we have invited Mr. Royal E. Jackson, Chief of that Bankruptcy Division, to be present, but unfortunately he cannot be present, and has submitted a statement, which I will place in the record at this point.

(The document referred to follows:)

STATEMENT OF ROYAL E. JACKSON, CHIEF OF THE BANKRUPTCY DIVISION,
ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS

Mr. Chairman, I am Royal E. Jackson, Chief of the Bankruptcy Division of the Administrative Office of the United States Courts. I have been a member of the staff of the Administrative Office of the United States Courts since February 1940 and have served in the Bankruptcy Division since the fall of 1946. I was appointed Chief of the Division in July 1964.

I speak in opposition to H.R. 1057 which would require the so-called consumer bankrupt, a person whose principal income is derived from wages, salary or commissions, to make an affirmative showing that adequate relief cannot be obtained under Chapter XIII before he can avail himself of the relief provided in an ordinary bankruptcy proceeding which is available to all other persons. The bill would impose upon the bankruptcy court the duty of determining at the first meeting of creditors whether the bankrupt has made a showing that adequate relief cannot be obtained under a Wage Earner's Plan. If the court determines that the bankrupt has failed to make such a showing the court must dismiss the case with notice to the creditors, thus denying the relief sought, unless within the time fixed by the court the bankrupt amends his petition to comply with the requirements for filing a debtor's petition under Chapter XIII.

H.R. 1057 is identical to H.R. 292, 89th Congress. H.R. 292 was considered at considerable length by the Bankruptcy Committee of the Judicial Conference of the United States at its meeting on February 15, 1965. The Bankruptcy Committee of the Judicial Conference is composed of the following judges:

Honorable Oliver D. Hamlin, Jr., Senior Circuit Judge, Ninth Circuit, San Francisco, California, Chairman

Honorable Bailey Aldrich, Chief Judge, First Circuit, Boston Massachusetts

Honorable Phillip Forman Senior Circuit Judge Third Circuit Trenton New Jersey

Honorable Seybourne H. Lynne, Chief Judge, Northern District of Alabama, Birmingham

Honorable Edward Weinfeld, U.S. District Judge, Southern District of New York, New York City

Honorable Wesley E. Brown, U.S. District Judge, District of Kansas, Wichita

Honorable Hubert L. Will, U.S. District Judge, Northern District of Illinois, Chicago

The Committee had the benefit of the views of District Judges Lynne and Brown, both of whom have thousands of wage earner proceedings in their courts. Both judges made a special study of the proposals contained in the bill. In this connection, it should be noted that District Judge Brown, who has been invited to testify at this hearing, served as a referee in bankruptcy in his district for a period of four years prior to his appointment as a district judge in April of 1962.

The Bankruptcy Committee concluded that, while a great many bankruptcy cases can and should be administered as wage earner proceedings, the proposals in the bill were discriminatory in that they single out a low income group who would be compelled to pay debts in full, while other petitioners, not wage earners, would still be privileged to obtain the relief the Congress intended to give insolvent debtors under the Bankruptcy Act, and have all the benefits of discharge of debts. The Committee feels that in this respect H. R. 292 and the successor bill, H. R. 1057, now under consideration, would be "class legislation."

The Committee also believed that it would be manifestly unfair to compel the debtor to accept a plan under Chapter XIII without equal compulsion upon the secured creditors to accept the same plan.

Referees who have extensive experience with the Wage Earner Plan are aware of the great difficulty encountered with debtors who have an earnest desire to pay all their debts in full and voluntarily file Wage Earners' Plans. Many of them fall by the wayside and for one reason or another fail or are unable to live up to the conditions of the plan for a period of three years or so. Ordinarily the courts do not consider a Wage Earners' Plan feasible unless the debtor can pay all creditors within a period of about three years. With this in mind the Committee foresaw great difficulty in forcing a debtor to propose a feasible plan and equally as much difficulty in coercing its execution. Experience shows that in voluntary Chapter XIII cases many debtors change employment, move out of the court's jurisdiction, default in payments under the plan, or incur additional debts despite the court's admonition to the contrary. These problems would likely be multiplied manifold in dealing with a recalcitrant debtor.

In view of these important considerations the Committee recommended that the Judicial Conference disapprove H. R. 292 and this action applies as well to the identical bill, H. R. 1057 now under consideration.

The Judicial Conference approved the Committee's recommendation at its March 1965 session and in its report stated:

S. 613 and H.R. 292, 89th Congress, entirely different bills, contain provisions which would change the wage earner proceeding under Chapter XIII from an entirely voluntary proceeding to a compulsory proceeding under certain circumstances. While it is recognized that many straight bankruptcy cases can and should be administered as wage earner proceedings, it was the view of the Committee that the proposals contained in these bills are discriminatory in singling out a low-income group that would be compelled under Chapter XIII to pay their debts in full. Other petitioners, not wage earners, could still avail themselves of straight bankruptcy proceedings and the benefits arising out of a discharge of debts. Moreover, it seemed unfair to the Committee to compel a debtor to accept a plan under Chapter XIII without equal compulsion upon secured creditors to accept the same plan. Upon recommendation of the Committee, the Conference voted to disapprove S. 613 and H.R. 292.

There are a number of practical aspects to the proposals in H. R. 1057 that should be considered in connection with the day to day administration of wage earner proceedings in the courts. The proposals would have the effect of denying some debtors entirely the relief that is provided in the Act for other debtors who are not wage earners. The proposals, if enacted, will not likely produce many more successful Chapter XIII cases. Nothing in the bill would make Chapter XIII more attractive. Moreover, human nature being what it is, people resent being coerced into anything. A personal preference cannot be legislated.

The proposed legislation provides no objective standard by which a referee in bankruptcy can determine what is "adequate relief." Some referees may have high standards as to "adequate relief" and require few cases to proceed as Chapter XIII cases. Other referees may take a more liberal view. A petitioner's chance of remaining in straight bankruptcy may depend on the forum selected. It would be necessary, of course, for the court to consider the relationship between the debtor's earning capacity, his family support obligations and the total of debts owed. If the debtor is determined to have the benefits of straight bankruptcy as other debtors who are not wage earners do, he can easily arrange to do one of two things: (1) incur more debts, not a difficult matter today; or (2) reduce his earning capacity by quitting his extra job if he is "moonlighting", or quit working altogether until his case is concluded.

These are practical everyday considerations and its seems conceivable that H.R. 1057, if enacted, could in the long run increase creditors' losses rather than decrease them. Assuming that a debtor can be coerced by the court into filing an "adequate plan" the trustee would be unable to force its execution. The trustee who is to collect debtors' payments and make periodic payments to creditors, even with the court's backing, could not enforce compliance with a Wage Earner's Plan against a determined non-compliant debtor. In voluntary Chapter

XIII cases the courts are not always successful in preventing the debtor from incurring additional debts during the pendency of the case. The courts would doubtless be even less successful in dealing with the recalcitrant debtor who really could not be prevented from going on a "credit binge" to frustrate the trustee and the court. There are many ways available to debtors and to lawyers who counsel them to sidestep coercion. I say this because it is the considered judgment of many of our referees who have had extensive experience with the administration of wage earner cases.

I do not mean to imply that the voluntary wage earner proceeding is not a good relief provision of the Act. The Judicial Conference of the United States has on several occasions urged the greater use of Chapter XIII in appropriate cases. In reporting to the Judicial Conference at the March 1958 session, the Bankruptcy Committee of the Conference stated "The Committee believes that a procedure by which a debtor, financially involved and unable to meet his debts as they mature, works out his involvement and pays his debts in full over a period of time, is good for his creditors and good for him." The Committee, however, had in mind a voluntary proceeding in which the debtor had an earnest desire to pay his debts and was not so hopelessly insolvent that a plan of arrangement could not be judicially determined as feasible.

Reports to the Administrative Office from referees in bankruptcy indicate that approximately one-third of the Wage Earner Plans now being filed fail of successful completion. In the fiscal year 1966, 28,261 wage earners' cases were filed. In that year 10,529 cases were successfully completed with total payments to creditors of \$18,826,318. In 1966 fiscal year, 132,038 petitions were filed by employees who sought straight bankruptcy relief. Referees advise us that about one-third of these cases involved persons whose earnings might have enabled them to propose feasible plans of arrangement under Chapter XIII. If this one-third of the employee-petitioners, or approximately 44,000, had elected to use Chapter XIII voluntarily and two-thirds of that number had reached successful completion, according to present experience there would have been an additional 28,000 or 29,000 Chapter XIII cases filed with perhaps double the payments to creditors, or about 36 to 40 million dollars instead of 18 million dollars. I must emphasize, however, that these projections are based on the premise that the debtors be voluntary. I am sure that no such performance can be expected of involuntary debtors.

The Wage Earner's Plan as presently on the statute books depends on voluntary compliance by the debtor for its effectiveness. The debtor must file the petition, draft and submit the plan and make the payments called for under the plan. Chapter XIII was designed to be a voluntary proceeding and many of its provisions require the cooperation of the debtor. Many of its provisions are flexible and are designed to give the debtor an incentive to prepare for future budgeting so that he can be in some measure rehabilitated financially. An involuntary Chapter XIII proceeding would very likely be looked upon by the debtor as a punishment and all incentive to reform his spending habits would be destroyed.

We feel that H.R. 1057 will not improve judicial administration and will not improve the lot of the wage earner. Moreover, if enacted it seems likely that it may increase creditor losses rather than decrease them.

Mr. POFF. Mr. Chairman, may I inquire if a copy of that statement is available?

Mr. ROGERS. Yes; every member has one, and if not, we will make it available. Now the first two witnesses, as I understand, would like to appear and testify together, and they represent the American Bankers Association. Mr. John L. Gibson, chairman, installment credit committee and vice president of the Republic National Bank of Dallas, Texas, and Mr. Curtis Kendall, vice president of the Birmingham Trust National Bank, Birmingham, Alabama.

Are both witnesses present? Would you come forward, please?

STATEMENT OF JOHN L. GIBSON, VICE PRESIDENT, REPUBLIC NATIONAL BANK OF DALLAS, TEX., AND CURTIS KENDALL, VICE PRESIDENT, BIRMINGHAM TRUST NATIONAL BANK, BIRMINGHAM, ALA., ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION

Mr. GIBSON. Mr. Chairman and gentlemen, my name is John L. Gibson, and I am senior vice president of the Republic National Bank of Dallas, Tex.

It is my responsibility to supervise the installment credit department of that bank and I have been engaged in banking or finance business since 1927.

Prior to my association with this bank, I was in the consumer finance business with GMAC and Universal Credit Co., which is now Universal CIT.

I appear before you today in a dual role, as an operator of an installment loan department of substantial size and as chairman of the installment credit committee of the American Bankers Association.

The American Bankers Association represents some 14,000 banks throughout the country who are active in providing credit facilities and services at a reasonable cost to the average man in the street. These banks hold between 30 and 35 million active installment loan accounts, with a total dollar investment of some \$32 billion. This dollar investment is approximately double that of the nearest competitive group.

Installment bankers have been acutely aware of the increasing problem represented by personal or wage earner bankruptcies. We consider it most unfortunate that the provisions of chapter XIII of the Bankruptcy Act are not utilized to a far greater degree nationally than is presently the case.

Years of experience have convinced us the vast majority of people want to honor their obligations. They should be encouraged to accept responsibility, develop pride of accomplishment, and regain their self-esteem.

The greater use of chapter XIII facilities provides a self-respecting means of accomplishing the financial rehabilitation of a very large percentage of the wage earner bankrupts.

The authority that is proposed to be granted to the referee in bankruptcy by H.R. 1057 will be of considerable help in enabling the referee to identify those bankrupts and indeed could clear up their financial obligations if granted the privilege of some additional time to repay.

For these reasons the American Bankers Association through its installment credit committee heartily endorses H.R. 1057 and strongly recommends its passage.

As mentioned earlier, my bank is in Texas and we happen to be one of the States that is relatively untroubled by this problem of wage earner bankruptcies. However, I have with me a long-time friend and close associate who is an experienced installment credit man.

His particular value as a witness for the American Bankers Association rests not only in his personal capabilities and long experience in the field, but also in the fact that he has worked for many years in banks in Mobile and Birmingham, Ala.

As you know, Alabama is a State which has had an abundance of opportunity to work on chapter XIII in bankruptcies. Birmingham

is the city that has become the showcase for experience in the practical application of chapter XIII activities in personal bankruptcies.

His name is Curtis Kendall, senior vice president of the Birmingham Trust National Bank of Birmingham, Ala. He is extremely well qualified to discuss our endorsement of House bill 1057 from a very practical viewpoint. He has had considerable experience in the subject area and is far better qualified to discuss our endorsement of H.R. 1057 from a practical viewpoint.

Mr. Kendall.

Mr. ROGERS. Proceed, Mr. Kendall, in your own manner, and when you have finished, we will ask questions of both Mr. Gibson and yourself.

Proceed, Mr. Kendall.

Mr. KENDALL. Mr. Chairman, gentlemen, my name is Curtis Kendall. I am senior vice president of the Birmingham Trust National Bank of Birmingham, Ala., and I am testifying on behalf of the American Bankers Association.

Banks, of course, are deeply involved in the health of consumer credit as the holders of some 43 percent of the estimated \$73 billion now outstanding. Banks extend consumer credit principally through two channels—the direct installment loan to the individual and the purchase of the installment sales contract from the dealer in goods and services.

Of course, the direct installment loans are made both on a secured and unsecured basis.

In most cases, the extension of consumer installment credit creates the financial vehicle by which goods and services flow to the consumer, enabling him to maintain his standard of living, and enabling business and industry to prosper. Any erosion of the individual's willingness and ability to pay his obligation is of concern to both bankers and the business communities they serve.

The high rate of personal bankruptcies, prevalent in my State over a period of years, particularly in the great steel centers, led to the early use of the debtor's court and wage earner plans under chapter XIII.

Thus long ago, necessity forced the cooperation of industry, labor, civic leaders, banks, the bar and the Federal judiciary in our area to seek an alternate course to straight personal bankruptcy where available.

Chapter XIII, implemented by the machinery of the debtor's court, has proven effective for many years in dealing with those cases that come before it. The debtor's court has become a respected institution. Cases of both financial and personal rehabilitation are legion.

It furnishes those who have both the ability and willingness to pay their debts out of future earnings an opportunity to do so under conditions conducive to preservation of self-respect and without the stigma attached to straight bankruptcy.

Some appraisal of the effectiveness of the debtor's court and chapter XIII machinery can be gained from the fact that in Jefferson County alone, comprising a metropolitan area of approximately 700,000 people, more than \$4 million is being paid to creditors annually, very little of which would be realized under straight bankruptcy.

It might be said that any other area plagued by personal bankruptcies has the same opportunity to make chapter XIII the effective instrument that it is in Alabama.

The facts are that of the total personal bankruptcies filed in my State for the fiscal year ending June 30, 1966, 79 percent were chapter XIII petitions; while for the entire 50 States only 16 percent of personal petitions were filed under chapter XIII.

It might also be noted that Alabama, particularly in the Birmingham area, has been working at this problem since 1933. And more particularly, since 1938, with the passage of the Chandler Act.

But nationwide, the percentage of chapter XIII petitions to total personal bankruptcy petitions has been dropping steadily for the past 10 years, with the exception of 1965, when there was a slight increase.

In the meantime, total personal bankruptcies continue to rise. Also we are witnessing a rapidly increasing number of people who are entering straight bankruptcy with comparatively small debts and a good job—displaying every evidence of ability to pay all their debts out of future earnings if provided a realistic plan and legal protection while doing so.

It is believed that one key to the situation is to encourage widespread use of chapter XIII and the debtor's court procedure where applicable. This appears to be the principal objective of H.R. 1057.

Under the present Bankruptcy Act, the referee has no authority to deny the petition of a debtor who files in straight bankruptcy, even though it appears that the debtor could pay his debts out of the future earnings over a period of time without undue burden.

Under the amendment proposed by H.R. 1057, the court would be given the discretionary authority to deny the voluntary straight bankruptcy petition of a wage earner who fails to show that adequate relief cannot be obtained in a chapter XIII wage earner plan.

Thus, under H.R. 1057, the debtor who files a straight bankruptcy petition must be able to prove then to the satisfaction of the referee that he cannot obtain relief under chapter XIII wage earner plan. For example, his debt may be so heavy that it would be impossible to liquidate it within the allotted time limit.

If for this or any other reason the debtor, in the opinion of the referee, could not qualify for the wage earner plan, then his right to obtain relief under straight bankruptcy would still remain available to him.

In essence, H.R. 1057 would provide that before the debtor could take the "last resort" step into straight bankruptcy, he would be required to explore the possibilities and benefits of the wage earner plan, this exploration to take place under an impartial and professionally qualified referee.

The thinking behind this proposed bill appears to be of a twofold nature:

First: That those who are really able to pay their debts out of future earnings within a reasonable time and without undue hardship should be encouraged to do so.

Second: That those who sincerely desire to pay their debts are entitled to a legally sanctioned and workable plan, impartial advice and financial guidance, as opposed to tossing in the sponge of a personal financial failure and receiving the inevitable black eye under straight bankruptcy.

Chapter XIII, with its wage earner plan and debtor's court, was designed to provide for such situations. However, in spite of the outstanding success of the plan in a few such areas and as my own, its use throughout the country has not been as widespread as was anticipated nor has the availability of the wage earner plan prevented the rapid increase in straight personal bankruptcy on a national scale.

All this indicates that we must continue to probe for further solutions to this problem.

The reasons for the choice of straight bankruptcy over debtor's plans are no doubt varied and quite complex. However, one reason appears rather obvious. Under our present system we have made it both easier and cheaper for the individual to take straight bankruptcy.

The processing of a straight bankruptcy petition requires less legal work and infinitely less clerical work on the part of the attorney's office and that of the court.

During the period a chapter XIII wage earner plan is in effect, the bankruptcy court will assist the debtor in carrying out a plan for the application of future earnings to pay his debts in an orderly fashion, while at the same time protecting a debtor from garnishment of wages, repossession, and certain other judicial actions.

Wage earner plans under chapter XIII are also sufficiently flexible to allow the bankruptcy court to suspend or reduce payments by the debtor in case of an emergency or other unforeseen occurrences that affect the debtor's ability to make his required payments.

Also during the time chapter XIII is in effect, a debtor's purchases of necessity would be supervised so as to avoid any future accumulation of debt.

H.R. 1057 would in no way alter chapter XIII as presently drawn but would encourage its use where it appears to the referee that a wage earner debtor could pay his obligations out of future earnings without incurring any undue hardships.

A few typical examples taken from the active files of the debtor's court of our district will serve to illustrate its effectiveness in dealing with specific cases:

CASE NUMBER 1

Occupation : Railroad Switchman.
Salary : \$520 a month.
Date of Petition : August 1964.
Total Debt : \$3,927.
Court Ordered Payment of : \$130 a month.
Paid out in 31 months. No balance now.

CASE NUMBER 2

Occupation : Semi-skilled labor-steel mill.
Salary : \$508 a month.
Date of Petition : October 1965.
Total Debt : \$4,104.
Court Ordered Payment of : \$160 a month.
Present Balance of Debt : \$138 as of 5/67.

CASE NUMBER 3

Occupation : Bus Driver—Transit System.
Salary : \$360 a month.
Date of Petition : September 1963.
Total Debt : \$3,024.
Court Ordered Payment of : \$84 a month.
Paid out in 36 months.

To summarize, it is believed that a far more widespread use for chapter 13 implemented by wage earner plans, and supervised by the court, will be beneficial to the debtor, the creditors, and to society; and that the most effective way to achieve this is to give the court the discretionary authority provided in H.R. 1057.

The American Banker's Association strongly endorses the principles set forth in H.R. 1057.

Thank you.

Mr. ROGERS. Thank you, Mr. Kendall. We appreciate your statement and that of your colleague, Mr. Gibson. There are a few questions I am sure that the members of the committee would like to ask you, to clarify your thinking in regard to this proposal.

As you know, and as outlined in your statement, H.R. 1057 applies only to wage earners, as defined in the Bankruptcy Act.

Do you think that his bill should be extended to other people like lawyers, doctors, and other professionals? Why do you think that it should be confined only to wage earners?

Mr. KENDALL. Without having seen Congressman Poff's proposed amendment, as I understand it, he would be agreeable to an amendment that would widen this to include all personal bankruptcies. I would certainly be in favor of that.

Mr. ROGERS. This is, to all personal bankruptcies. Instead of only to wage earners. But what about corporate debtors?

Mr. KENDALL. Corporate debtors—

Mr. ROGERS. Yes, they are dealt with under other chapters of the Act.

Mr. KENDALL. Corporate credit is extended on an entirely different basis from consumer credit.

Mr. ROGERS. Yes.

Mr. KENDALL. Consumer credit is extended primarily not on a man's net worth, but on his ability to pay out of earnings, present and future, mostly future. Therefore, sir, the solution to the consumer's problem would seem to lie in the field of helping him get back into adjustment, in the ratio of his earnings to his commitments, whereas we extend credit to businesses primarily on the balance sheet concept. If a business does not have a substantial net worth, it will not get certain types of credit, and we anticipate that our loan to business may well have to be paid, in many instances, out of the sales of assets.

In the consumer field that is a secondary consideration. We are primarily concerned with his income producing ability in the future. Therefore, I think you have a totally different set of circumstances in the two cases.

Mr. ROGERS. Do you have an opinion to offer on that, Mr. Gibson?

Mr. GIBSON. I was of the opinion, Mr. Chairman, that the chapter XI covered the corporate end of this, and therefore, this was going to be confined primarily to the wage earner, the salaried people.

Mr. ROGERS. But you would have no objection to extending it to everyone except corporate debtors? That is, professionals and self-employed persons; not just confining it to wage earners alone?

Mr. GIBSON. I would be agreeable.

Mr. ROGERS. Yes. Well, now, Mr. Kendall, as you know, H.R. 1057 says, quoting from line 9 or 10, on page 1:

In the event that the judge or referee shall determine that the bankrupt has failed to make such a showing, he shall enter an order vacating the order of adjudication, and dismissing the bankrupt proceedings with notice to all credi-

tors, unless within such time as the judge or referee shall fix, the petition be amended to comply with Chapter XIII of the filing of the debtor's petition.

My question is, what proof will the debtor or the bankrupt have to present in order to establish his inability to get adequate relief under chapter XIII?

Mr. KENDALL. Well, one instance comes to mind. If his debts have gotten so greatly out of line that his income, or that portion of his income which could be allotted to debt payment would take him a great number of years, then he could not get relief under chapter XIII, as it is now organized.

But if he can get relief under—within a reasonable time, I believe it is 36 months in most instances that they use now, relate his income, and that portion of his income that is available for debt reduction, you would relate that to the time limit set by the court, I would think.

Mr. ROGERS. Well now, wouldn't that place in the judge or the referee too great discretion in the matter? His thinking of what a man's ability may be to repay would be substituted for that of the individual?

Isn't that what that does?

Mr. KENDALL. Well, some of the elements in that decision are very fixed. We know his income.

Mr. ROGERS. Yes.

Mr. KENDALL. And we know the trade he is in, we know what his future income is apt to be.

We know—we would have another element, such as size of family, and living standard and so on, to take into consideration, but most of our elements, I would think, would be fairly easy to ascertain.

Mr. ROGERS. I assume that a chapter XIII proceeding stops garnishment, and repossession. In other words, if a man has a mortgage, on an automobile, his creditor has got to come in under chapter XIII and be guided by the action taken by the referee.

Now you point out that there have been a number of successful chapter XIII's in your part of the country.

May I inquire if you have ever had any complaint that the chapter XIII proceeding made it possible for the debtor to retain possession say, of an automobile, and run it to death, and wear it out, and deprive the creditor of his security?

Mr. KENDALL. Oh, yes, that is one of the problems that we have to face now.

Mr. ROGERS. Well, suppose an individual who belongs to your profession says, "Well now, if these people are going into chapter XIII, and I am engaged in automobile financing, I may be in a pretty difficult situation, because I can't take possession, and a man will be out there wearing it out and tearing it up, and before we can repossess it, my security is gone."

Mr. KENDALL. That problem exists.

Mr. ROGERS. In addition to that, would this bill prohibit an individual from later taking advantage of straight bankruptcy? In other words, suppose he files his petition, and the referee says, "We think you can work this out under chapter XIII."

Well, now suppose he goes on the plan for a couple of months, and then he says, "Well, I am not interested any further. I don't want to work under this plan, and I want straight bankruptcy relief. I don't want to mess around with chapter XIII."

Do you think he should have a right to do that?

Mr. KENDALL. Let me answer the first part of the question first.

Mr. ROGERS. Yes.

Mr. KENDALL. As I understand the bill, if he tried to do that, and then get back out of Chapter XIII, the referee would have something to say about it, under this new bill, and he might not be able to do it.

Mr. ROGERS. Well, suppose that he said, "Well, if I have got to do this, I am going to quit my job. I don't want to pay this, because I can't, and you have me strapped down," and he does quit his job. Should that be grounds for prohibiting him from getting a discharge in bankruptcy?

Mr. KENDALL. Well, I should think that is a decision that this referee will have to make, and we want to give him discretionary authority to make.

Mr. ROGERS. Yes, in other words, you would still leave it within the discretion of the referee?

Mr. KENDALL. Of the referee, yes, sir.

Mr. ROGERS. Well, now that is an exception to review by the usual procedures. And under this procedure would the referee then be in a position to deny the debtor a discharge under straight bankruptcy?

In other words, under the present statute if I go in and show that I am bankrupt, I can be relieved by filing a petition, being honest about everything, and can be granted a discharge.

But if I go in under this bill, and a referee determines that I can with due diligence pay back in 36 months, and I start on it, and I give up before the 36 months is up, then do you think that the fact that I gave up and said, "No, I don't want to comply with this anymore," that that should be grounds for denying me a discharge in bankruptcy?

Mr. KENDALL. I would be inclined to think that it would be the duty of the referee to see that he did not weary in well doing.

Mr. ROGERS. He did not what?

Mr. KENDALL. Did not weary in well doing. He starts on the right road and then he gets weak.

Mr. ROGERS. Well that is what I want to know. He was weak probably in the first instance, or he would not have been there.

Mr. KENDALL. That is right.

Mr. ROGERS. Now the mere fact that we throw him into a chapter XIII does not make him strong or viable either.

Mr. KENDALL. Well it provides him with a plan whereby he can get stronger, if he wants to.

Mr. ROGERS. In your statement you also say that, and this is on page 4, the bottom line, during the time that chapter XIII is in effect a debtor's purchase of necessities would be supervised so as to avoid any future accumulation of debts.

Now what kind of a supervision would be given by the referee, or what has been the experience?

Mr. KENDALL. That word "necessities" is probably ill advised. It is more or less the luxuries or what one fellow would think is a luxury and another one would not that are supervised. I know of no case where necessities have been supervised to the extent of depriving a man of his normal way of living at all.

It is to prevent his overbuying. So many of these people have absolutely no concept of a family budget whatsoever, until they get in

debtor's court, and therefore for the first time, they learn what a family budget is.

It has been very effective down our way in teaching them something.

Mr. ROGERS. Of course as you and I know, many people are at least a one-automobile family, in some cases two or three cars are owned. And it is a necessity, for people to get to and from work. Well, now if a debtor has an automobile with a big mortgage on it, and the engine goes bad, it is about a \$300 repair bill, would he be in a position to go in and get that work done, without approval of the referee?

Mr. KENDALL. I would think so.

Mr. ROGERS. And would he then be able to take that \$300 and put it under this chapter XIII composition and pay out in that manner?

Mr. KENDALL. I don't know the details of that, except that I know of no instances where a debtor who was trying has had to sufficiently alter his way of life or deprive his family of necessities under this plan.

A rule of reason, I think, down our way, has been what the referees have been governed by.

Mr. ROGERS. Well the rule of reason is the referee's determination of it.

Mr. KENDALL. Yes.

Mr. ROGERS. Rather than a banker's. He is away from the bankers and in the hands of the referee. If he should make application, could the referee say no, you should not have been driving that car so hard, or you would not have had this accident. Would the referee have discretion in matters of that kind?

Mr. KENDALL. Mr. Chairman, I can't anticipate all those things that will come up, except to say this: That as we now set up, I am sure, without knowing the rules of the debtor's court, that our judges are forced to make some homemade law based on their best judgment, and what this bill would do would be to clarify their authority as to what they could and could not do, so I think it would clarify an unclear situation that undoubtedly must exist.

None of the judges have told me this, but I think they must be forced to make decisions now that are at least unclear within the law.

Mr. ROGERS. Well, don't you anticipate that if we adopt this piece of legislation, that we are going to have to hire a few more, appoint a few more, referees and Federal judges to administer this?

Mr. KENDALL. You will certainly have to have some more referees, and you will have to have, what is just as important, you will have to have clerical machinery.

This disbursing of money is big business when you run a debtor's court, and you must have a disbursing machinery along with it that works into it smoothly, and that has been one of the drawbacks to the situation that we are in throughout the country now.

It is so simple to file a straight bankruptcy court, where the attorney, no matter how ethical, could collect his fee, and the thing is all over, and the debtor goes home, whereas, when you go through debtor's court, you have got a lot of clerical work, you have got a lot of supervision, for a long time, and of course, that runs your cost up.

Mr. ROGERS. Thank you, Mr. Kendall.

Questions?

Mr. WHITENER. Well, Mr. Kendall, reading your statement, it appears that the Birmingham area has done a splendid job with the utilization of the Wage Earner's Act, in which I have been quite interested through the years: the only thing that I am wondering is why this is so peculiar to your community, and not to any other area of the country?

Mr. KENDALL. Well, I don't think it is entirely peculiar. I notice that there are five or six other States here that are making wide use of the debtor's court. I think part of it stems from the fact that we had a more acute situation.

When the depression hit, Birmingham was a steel town only, and the economy was in a state of collapse. And it was absolutely imperative that the whole community gang together and do something, and so that started some movements, even prior to the Chandler Act, to do something about it as a community action, and then when the Chandler Act came along, and chapter XIII, it appeared to furnish the vehicle that the citizens were looking for, and it was all the citizens, bankers, laborers, everybody else, so that, I think, was the beginning of it.

Now why so many people still continue to take bankruptcy in our area, I cannot answer. I wish I could.

Mr. WHITENER. Well, I have been very much interested in this particular legislation and I have discussed it with Mr. Poff on numerous occasions, but I must admit that from my discussion, I had not realized that this created a situation where one class of debtor would be forced to go through a procedure that no other class would be required to take. Thus, as you mention, under a chapter XI proceeding, there is no way a referee can make a corporation go through an arrangement, is there?

Another thing about this proposal is that a debtor who falls within the definition of wage earner under chapter XIII can never get a complete discharge for anything less than complete payment of all of his obligations, whereas a corporation can do that without regard to the wishes of the referee.

Mr. KENDALL. Well, first of all, under our debtor's court procedure, we do have composition of the debts. Not all do pay all their debts. There sometimes are original compositions of debts made, a fellow says "I want to go on in bankruptcy, I can't pay this \$5,000."

"Well, can you pay \$3,500?" That is done—now as to class legislation—

Mr. WHITENER. The referee would not have any authority to enter a discharge of debt?

Mr. KENDALL. I would have to leave that to all the learned attorneys that are going to draw the amendments to this bill. I would think that would be taken care of.

Mr. WHITENER. I am not talking about amendments to the bill now. I am talking about the bill that you have. This is what we are dealing with now. Not something we write later.

Mr. KENDALL. Well, the element of class legislation has been injected, and is the element of an amendment, and it is very difficult for me to see where any charge of class legislation could be substantiated, if it is amended to include all individual bankruptcies.

That is about as broad as you can get it, when you have got another set of laws to take care of business now. Maybe we need to amend the bankruptcy law protecting business.

I have no brief for that.

Mr. WHITENER. Well, Mr. Poff and I have been very energetic in this bankruptcy field. The thrust of our activity before was to prevent, in certain instances, the individual debtor from being imposed upon in a way that is not true of a corporation. We fought very vigorously, and I believe had to overcome a veto on the question of dischargeability of an individual debtor, rehabilitation of the debtor financially. While I am in sympathy with the concept that you have here of encouraging the use of chapter XIII, I do have some doubt about the wisdom of a compulsory chapter XIII proceeding, if the debtor and his attorneys are of the opinion that he cannot reasonably go through a wage earner proceeding.

This debtor may have two children in college, and some referee might arbitrarily say, "Well, you don't have to send them to this college. He can go to another one down here for \$300 a year less," and there won't be a thing that the debtor could say about it.

Mr. POFF. Mr. Chairman, would the distinguished gentleman yield to me?

Mr. WHITENER. I would be happy to.

Mr. POFF. I express appreciation now for the work that he has done in the field of bankruptcy. He and I have indeed cooperated often, and I hope we will be able to cooperate on this legislation.

May I ask the gentleman if he does not agree that the argument about class legislation, if it has any validity at all, goes to the very existence of chapter XIII itself, inasmuch as chapter XIII itself is specifically defined for wage earners, including those who earn wages and those who earn salaries?

Mr. WHITENER. You are asking me a question. I don't think that this is under our consideration. In chapter XI, you have a voluntary proceeding which is not mandatory upon the corporate debtor.

Under the present chapter XIII, you have a voluntary procedure for the individual, who classifies as a wage earner. It is not a mandatory composition. So I think that it is apparent that when you apply this to one type of debtor, where the referee can sit up and say, "Now we are not going to let you have bankruptcy until we have made a test," then you do have a discrimination. I want to say this to you, Mr. Kendall and Mr. Gibson, I have been so concerned about the lack of use of chapter XIII that I personally at my own expense have sent out information on it to every lawyer in my congressional district in the past, encouraging them to use it. But I don't find that they have paid much attention to me.

And that is why I was interested in the success you folks have had.

Mr. KENDALL. Well, I think we must preserve, right on through all our thinking, the fundamental difference in consumer credit from commercial credit, because consumer credit as we said is given, extended, after you find a man—you are satisfied of his integrity, and his ability to pay.

Mr. WHITENER. You mean the banks do that?

Mr. KENDALL. It is extended entirely, almost, on his future income.

Mr. WHITENER. By the banks?

Mr. KENDALL. That is right.

Mr. WHITENER. But a man can pay \$400 and get an air travel card, on some airlines, pay nothing, and travel around the world, six times, as long as he has the card.

Mr. KENDALL. That is right.

Mr. WHITENER. And may not be able to travel from here to Birmingham financially, but anyway, he winds up in debt?

Mr. KENDALL. I think at present a great deal of our straight bankruptcy petitions stem from the fact that it is so easy and that it is actually cheaper, and a great many of our bankruptcies get their advice over the backyard fence.

"You got in trouble, Joe. How did you get out?" "Well, I went down to attorney so-and-so and filed bankruptcy."

Whereas he does not have the knowledge nor the inclination to explain to him the more elaborate machinery under chapter XIII. I think that is one reason we have the continued choice on the part of the debtor of straight bankruptcy over chapter XIII. It is more difficult to explain.

Mr. WHITENER. Well, I have had some correspondence at least from one prominent banker in my area, who expresses a concern similar to the one Mr. Rogers cited in one of his remarks. He says that one of his friends had suggested that where there is some credit extended on a chattel mortgage on specific personal property, which deteriorates rather rapidly, that the bank would be really hurt by this type of legislation. So I suppose that the bank financing would be dependent somewhat upon the volume of automobile financing that he is doing, rather than—

Mr. KENDALL. Well, the secured creditor, of course, can be placed at a disadvantage, but we think the overall benefits outweigh that.

Mr. WHITENER. Thank you.

Mr. ROGERS. Mr. Jacobs.

Mr. JACOBS. Mr. Chairman, Mr. Kendall, first of all, let me say that I believe that I am in sympathy with the philosophy and overall objective of this legislation. I have some reservations about details of it as it now stands. I believe that it might be fair to say that those in this Nation who seek bankruptcy generally fall into two categories.

Those who find that they have to, and those who simply find that they have a chance to. An example of those who have to would be the case up in the northern part of my own State of Indiana a couple of years ago, where some very unreasonable measures were taken against a wage earner who according to the note he left committed suicide because of that situation.

On the other hand as a young lawyer, just out of law school, I can recall clients coming to my office and wanting to take bankruptcy who were in substantially better shape than I was at the time.

So I do believe that we all know what we are aiming at, and what we would like to accomplish, but we want to make sure, if we can, not to slip over into one category or the other unfairly.

And, therefore, I am interested in your analysis of the corporation situation. They say death is a great equalizer, and perhaps voluntary bankruptcy sometimes tends to be a great equalizer. It has been my experience in the practice of law that when a corporation is prepared to take voluntary bankruptcy, those assets and that net worth upon which the loan originally was made have vanished, and they, therefore, assume substantially the same unfortunate and un-, as distinguished from irresponsible position of the individual who is taking bankruptcy.

I just wonder if I might have your comment on that situation between the corporation voluntary bankruptcy and the individual.

Mr. KENDALL. Well, I am sure time does not permit, nor am I an authority on it, but my own personal feeling is that the bankruptcy laws badly need amending as to businesses, and that it is too easy to go in bankruptcy, and too easy on the part of us credit grantors to forgive bankruptcy to a business.

Mr. JACOBS. It just strikes me that while we are on the subject, maybe all that should be done at the same time—chapter XI as well as chapter XIII. One other thing that is not possibly the most pleasant subject for me or for the witnesses representing the loan industry, are certain examples around the country of advertising techniques used by various loan institutions. For example, in my hometown, the bank that I do business with and have a very high regard for, occasionally gets on the radio and advertises, "You don't just have to borrow money when you are in trouble. We have happy money," I believe is what they say.

And then somebody pointed out the other day that a fellow borrowed some "happy money" and went to Hawaii on vacation, and wrote back to my good friend, the president of the bank there, and said, "Having a wonderful time. Don't know how I can ever repay you."

[Laughter].

It strikes me that perhaps that problem might be considered; really, the question of unfortunate advertising methods.

It might even be considered in connection with the treatment of bankrupts, and the treatment of creditors who file their claims in bankruptcy. What do you think about it? Is that a just criticism?

Mr. KENDALL. Congressman, I would have to agree with your basic thinking, there. My only comment would be that if we wait on cleaning up a problem we know exists in the personal field, until we clean up business bankruptcy, and then we wait on that until we clean up advertising, we will probably never clean up any of it.

It seems to me that we have got to break them down and solve them one at a time, if we are going to do it. Now I think we are all guilty—bankers, merchants, and everybody else—under the highly competitive conditions under which we operate. I think practically all of us are guilty of appearing at times that it is too easy to get money to buy merchandise, and so on, and I think the consumer, by and large, you know, he has only had this nice tool one generation. I sold real estate when there was no installment mortgage; we did not solicit anybody who was not 50 years old, and had half down, so when you figure that this generation of consumers has only had this marvelous tool you might say a full generation, I think he has proven unusual wisdom and has had a small excess, compared with what he might have done.

I have a great deal of confidence in the wisdom of the mass of consumers to regulate themselves, once the facts are given them, and they make up their collective mind, they have decided not to buy automobiles and appliances, this last year, like they did in 1965.

They were smarter than the businessman who makes automobiles and appliances.

So we have a very complicated situation, in which we will always have something to correct. My only contribution here would be that if

we have a problem that we can correct now, break it off from some of these other complicated problems, take action and go on to those problems later.

Mr. JACOBS. I would only suggest to my fellow committee members that that word is "if," and it seems to me that if we should determine that some of these other problems might be efficiently and expeditiously and fairly looked into along with this legislation, I would be very happy to see that done. I want to add, Mr. Kendall, that you are obviously a very knowledgeable man, and you have made an excellent witness thus far.

I now commend you to the gentleman to the right.

Mr. ROGERS. May I ask one question, before going to Mr. Poff?

The question was propounded by the gentleman from Indiana about the effect of the inducement and the come-on, in obtaining consumer credit. If it is shown that a great amount of the indebtedness accumulated by an individual has resulted from inducements in these ads, should that be reason to deny him bankruptcy relief?

Should that be considered? In other words, could that be considered by the referee in determining whether or not a debtor comes under chapter XIII or whether he is entitled to straight bankruptcy relief?

Mr. KENDALL. I can't answer that categorically. I would say this: That ideologically, I am opposed to concentration of power, in whatever form, and of course, if referees were corrupted, you would have a bad situation.

Likewise today, if referees were corrupted, you would have a bad situation, but your referees get their job from a mighty good source, and the Federal judges, and I can't imagine a better source and more insurance that we will have high-class people as referees than the way they are appointed, so I feel comfortable—there will be abuses, no doubt—but I feel basically comfortable that the referees that would be appointed will be highly honorable men, and will by and large discharge their obligations with fairness to all.

Mr. ROGERS. Mr. Poff.

Mr. POFF. Mr. Chairman, thank you, and the witness can be assured that I will treat him tenderly. I have no other purpose.

Might I add to what you have just said; namely, that while all of us favor a government of laws rather than a government of men, there comes a time when we must repose our confidence in some man, somewhere.

Mr. KENDALL. That is right.

Mr. POFF. And I have confidence that the people selected for this high trust will discharge the duties of their office as those duties are defined in the laws which the legislative branch of the Government writes.

If we cannot have such a confidence, then we cannot have any confidence in government anywhere. I was interested in the line of questioning opened up by our able chairman. His questions illustrate the fact that many creditors then do object to the use of chapter XIII.

It is true today. It would be true if this legislation becomes the law.

It is true partly because creditors are unadvised as to the alternative, and it is true because creditors sometimes are not familiar with

the procedures of chapter XIII, and it is true in the case of certain secured creditors, as the chairman and witnesses indicate.

Yet I think it must be said, then, at this point in the record, that chapter XIII will not permit any arrangement to be put into effect except with the consent of a majority of the creditors in number and in amount. Thus, insofar as the interest of creditors is concerned, I suggest that chapter XIII itself contains adequate safeguards.

I was also interested in the concern that was expressed about placing too much discretion in the hands of the court, or the referee. I would like to repeat what I said in my prefatory remarks; namely, that the discretion, while placed in the court, is not unbounded.

On the contrary, intention underlying this bill is that the judicial conference, which already has written the rules and regulations concerning the operations of chapter XIII, would write additional rules and regulations, concerning the operation of this statute if it becomes law.

Then, too, litigants always have their proper judicial recourses, in the event of abuse, and that, I hope, will always obtain in our form of government.

I have a number of other questions I would like to ask, but in the interest of time, and hopefully, so we can conclude as much of the evidence as possible this morning, I will yield, with my appreciation to both witnesses for their most helpful testimony.

Mr. ROGERS. Mr. McClory.

Mr. McCLORY. Thank you, Mr. Chairman.

I am interested in this legislation, not only in behalf of creditors, but also in regard to debtors, and I would think that there would be definite advantages to the debtor in connection with this legislation.

I am thinking about the future extension of credit to the debtor, who would take advantage of this arrangement under chapter XIII, in lieu of the debtor who goes into straight bankruptcy. Would there not be a better credit rating in that case, Mr. Kendall?

Mr. KENDALL. Yes, I would think so. The debtor's court, in our areas, does not carry with it the stigma of bankruptcy, at all. I mean, as you know from these figures, we have quite a percentage of our population in this that have been through debtor's court, and it has not, the stigma attached to straight bankruptcy has not followed the debtor's court, but I think, of course, a good deal of that is in the high degree of equitable administration of it in our area.

It has been kept on a high plane.

Mr. McCLORY. I am thinking, too, of the protections which are afforded by the Bankruptcy Act, the opportunity to employ straight bankruptcy, whether it is necessary to do so, and if that, if the debtor does resort to straight bankruptcy, then he is barred for a period of 6 years from ever employing that same means again, so that he again is jeopardized when he resorts to straight bankruptcy in lieu of resorting to a chapter XIII, if he has that choice.

Mr. KENDALL. It is a very drastic thing, the effect on his credit.

Mr. McCLORY. You have numerous references to debtor's court. Is that a State court proceeding in which you worked out these—

Mr. KENDALL. It is the machinery under which chapter XIII is operated in our area. They call it debtor's court.

Mr. McCLORY. So I see, that is the Federal court proceeding.

Mr. KENDALL. Yes.

Mr. McCLODY. Do you find nationwide some relief through State legislation, where the State laws authorize voluntary arrangements and budget control of debtor's problems?

Mr. KENDALL. I am not advised on that. I don't feel that I am capable of commenting on that. I have heard of some, yes.

Mr. McCLODY. There are some voluntary programs that I suppose are operated without any legal authority, and really without any legal jurisdiction, are there not?

Mr. KENDALL. Well, many years ago, before this was ever, even before the depression, certain attorneys in every town became known as proration attorneys, where if you were in trouble financially, you could go and that attorney would take the time to do very much what the debtor's court is doing now.

Mr. McCLODY. From your standpoint, it is preferable to have a lawfully authorized arrangement?

Mr. KENDALL. Oh, yes.

Mr. McCLODY. Thank you.

Mr. ROGERS. Mr. Wiggins?

Mr. WIGGINS. One question, Mr. Chairman.

This question was asked, and I don't believe you have answered it directly. If a wage earner has a plan imposed upon him under the procedures envisioned in this bill, and he thereafter fails or refuses to follow the program outlined for him, should his failure or refusal to do so be a basis for denying an absolute discharge?

Mr. KENDALL. I would say there are too many imponderables and too much law in that for me to be competent to answer. I don't know.

Mr. WIGGINS. That is the only question I have. Thank you, sir.

Mr. ROGERS. Our counsel would like to ask a couple of questions.

Mr. ZELENKO. Mr. Kendall, the following has been contended by the National Bankruptcy Conference, and I would like to quote:

If the justification for Chapter XIII is its moral or ethical value, it is submitted that payment of debts under compulsion contributes nothing to a debtor's morale. On the contrary, compelling a debtor to submit to deductions from his income over a long period of time for the payment of past obligations is calculated to destroy his morale and cause his family unnecessary hardship.

Would you care to comment?

Mr. KENDALL. Well that gets into the field of morality, sociology, and what not. I am primarily concerned with the field of banking and I think that anything that makes the debtor, gives him a plan, and gives him a strong incentive to pay his debts is beneficial.

What it will do to its morality, I don't know.

Mr. ZELENKO. Do you mean beneficial to the debtor, Mr. Kendall?

Mr. KENDALL. Well, an honorable man wants to pay his debts to start with, but if he is convinced that there is no alternative, he says, "I will go bankrupt. That is easy. My neighbor did it."

But if he knows that there is a way he can avoid bankruptcy, and still pay his debts, then I think he would want to take them.

Mr. ZELENKO. Someone suggested, in questions to you earlier an approach consisting of a mandatory requirement that a debtor, when applying for straight bankruptcy, submit an affidavit, for example, to the court that he has considered the chapter XIII alternative with his attorney, and has found it unworkable or has found it an unworkable alternative, would that be sufficient?

Mr. KENDALL. It would kill your bill. They would all consider chapter XIII.

Mr. ZELENKO. So it is not just the fact that he has not considered chapter XIII. It is a question of—

Mr. KENDALL. It will kill your bill.

Mr. ZELENKO. One last question, Mr. Kendall. Is it possible that some referees will always find the wage earner plan adequate, while others will never find the chapter XIII alternative adequate, and still others may alternate in their views as to adequacy or inadequacy?

If that is so will the result be a greater disparity than exists at present in the administration of chapter XIII?

Mr. KENDALL. You compliment me with that question. My feeling about the overall picture is there—if you inject this if you want to call it element of compulsion, if you inject it into it, you will have to set up machinery, you will have to set up an administrative machinery that does not exist now in most areas of the country. The courts will have to hire more people, there will have to be more clerical work.

Certain attorneys that go in for it will hire more people. Once that machinery is set up, I think then the bulk of these questions that are being asked today will be ironed out, as it were, in the wash, but until that day, I can't answer these hypothetical moral questions. I am not competent.

Mr. ROGERS. Thank you, Mr. Kendall, and we appreciate you and Mr. Gibson coming and testifying before the committee, and Mr. Gibson, have you anything further to add?

Mr. GIBSON. I think he has covered quite adequately. Thank you.

Mr. ROGERS. Thank you, sir.

Our next witness is accompanied by an honorable Member of the Congress, Mr. Robert Denney. Will you come forward, Mr. Denney?

Your brother, Mr. Max Denney, who is the executive vice president of the American Industrial Bankers Association.

The Honorable Robert Denney of the State of Nebraska.

STATEMENT OF HON. ROBERT DENNEY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEBRASKA

Mr. ROBERT DENNEY. Thank you very much, members of the Subcommittee No. 4 of the House Judiciary Committee. I am not here to testify. I am here to introduce to this committee my brother.

He and I practiced law for many years in a small town together out in Nebraska. Where he is well versed in some of the bankruptcy problems we had. I think he has a good statement to give to your committee. I appreciate the opportunity to introduce him to the committee at this time.

Thank you so much.

Mr. ROGERS. Thank you, Mr. Denney.

Now, Mr. Max Denney, will you proceed in your own manner?

STATEMENT OF MAX A. DENNEY, EXECUTIVE VICE PRESIDENT, AMERICAN INDUSTRIAL BANKERS ASSOCIATION

Mr. DENNEY. Thank you, Mr. Chairman.

I am here this morning representing the American Industrial Bankers Association as their executive vice president.

I also am a member of the consumer bankruptcy committee of the American Bar Association although I am not representing them here today in any capacity.

The American Industrial Bankers Association is a national trade organization of sale financial companies, industrial loan companies, Morris Plan companies and other types of consumer finance companies.

We have approximately 425 member companies with some 6,000 offices. Some of our members have only one office, some have several hundred.

The sales finance companies primarily buy documents involving credit transactions sometimes called paper from dealers. The industrial loan and Morris Plan companies make direct loans in larger amounts to consumers; they also were permitted by State law to issue certificates of investment or indebtedness to those wishing to invest in their operations. Many of our companies also make what is called small loans directly to the consumer.

The total dollar outstandings of the companies and individuals who are members of the AIBA currently average about \$10 billion a year. In other words, the members of this association are engaged in the consumer credit business throughout the United States.

Because of the tremendous increase in the number of individual or personal bankruptcies that have taken place in the past few years, we are naturally very much interested in any legislation that may have a tendency to slow the pace of this increase.

In the past 10 years the total of bankruptcy filings has more than tripled and of this total, nonbusiness or personal filings have risen from 80 to over 90 percent.

There are those who point out that there appears to be a correlation between this growth of personal bankruptcies and the increase in consumer credit outstandings.

While there may be some tie-in between these two figures, the charge that much of the blame for the bankruptcy increase should be placed on the finance industry is not true, as is shown in recent studies on this subject.

In a monograph prepared by George Allen Brunner entitled "Personal Bankruptcies Trends and Characteristics" which was written under the auspices of the Ohio State University Bureau of Business Research. Dr. Brunner points out that contrary to what many have felt, his studies show that the majority of the creditors of personal bankrupts is not the consumer finance industry. Primarily it is those pertaining to what are called open accounts, doctors and dentists, open charge accounts, rents, utilities, and the like.

The consumer finance industry and the related banking industry who make their loans normally on some form of secured basis, accounted for only 7 percent of the debt discharged in bankruptcy, according to George Brunner's studies.

While this figure is not near as large as many have thought, any discharge in bankruptcy of an account involving our industry is a loss we naturally don't like.

Those who have made extensive studies of the bankruptcy problem (and there have been several in the past 4 or 5 years) cite many reasons for, or causes of, this tremendous increase in personal bank-

ruptcies. They range from a lowering of moral standards among those looking for an easy way out of a difficult situation, to economic illiteracy, to insufficient credit checking.

One writer on this subject even suggests we have a credit drunk problem on our hands similar to that connected with those who are unable to control their desire for alcoholic beverages.

Since those who have made detailed studies on this subject of personal bankruptcies cannot agree on any one cause for this strange phenomenon in our present-day affluent society, we of the finance industry are not naive enough to suggest that the mere passage of, or amendment to, a Federal statute is going to solve all the problems. In fact, we feel that the attack on this problem must be three pronged and we are attempting to do something about it.

One prong is education in the high schools and colleges along the lines of using one's credit wisely. Our industry has available to the education field manuals, brochures, filmstrips, and booklets pointing out how credit should be used—the do's and don'ts of installment buying, suggestions on how to prepare and live within a budget, and so forth.

We also hold meetings, institutes, and seminars with the education profession and the clergy on how to teach this subject in the schools and how to counsel with those in need of help.

The second prong we are working on is in the field of adult education. We have joined with the National Foundation for Consumer Credit in helping establish free debt or credit counseling services throughout the United States. At the present time some 64 cities in the United States have services of this kind.

The third prong that we feel would be a tremendous help in solving this personal bankruptcy problem is the amending of chapter XIII of the Bankruptcy Act as called for by H.R. 1057 and/or H.R. 5771.

When chapter XIII was made a part of the Federal Bankruptcy Act back in 1938 it was stated and I quote from the record:

The average wage earner like every other type of debtor desires to pay his debts and avoid the stigma of bankruptcy. If afforded a reasonable opportunity, he would preferably arrange to do so.

The facts since 1938 indicate that such a statement was rather optimistic; however, there is no question but that where chapter XIII is used, it works. The trouble is that it is not being used uniformly throughout the United States.

I am sure figures on this subject have been or will be cited to this subcommittee before these hearings are completed, so I will not take your time by repeating them.

Those who have had experience in bankruptcy know that filing straight petitions is a lot easier than a chapter XIII. You fill out a form, you file it, hold a first meeting, and that is about it.

A chapter XIII requires a plan, requires solicitation of the creditors, some negotiation, and then after the plan is confirmed, it requires work on the part of the trustee to see that the man complies with the plan.

Often times it also involves negotiations with the man's employer. While all this takes much more time and effort, we believe it is well worth it for all concerned.

Inasmuch as the referee under the present law has no authority or discretion to change a straight bankruptcy to a chapter XIII, certainly the blame for its lack of uniform use throughout the country cannot be placed on him. We feel the real blame lies with the legal profession itself. Instead of counseling with the debtor as they should, many are inclined to take the easy way out and just recommend (and in some areas it appears they even encourage) straight bankruptcy.

Several of the studies I have referred to above indicate that from 25 to 50 percent of the debtors filing personal bankruptcy petitions could have paid their debts out of future earnings over a period of 3 years or less without undue hardships, if they had been encouraged to do so.

The American Industrial Bankers Association has endorsed and now advocates the passage of H.R. 1057 or H.R. 5771 because we believe such legislation if passed and properly administered, will help reduce the number of unnecessary or avoidable personal bankruptcy proceedings.

As we understand this legislation, it will accomplish this goal by vesting in a judicial officer of the U.S. courts the authority or discretion to remove from straight bankruptcy those debtors who are obviously able to pay their creditors.

While there is no question but that the Bankruptcy Act serves a worthwhile purpose for those who feel they need a shield to help avert a personal financial crisis, the act ought also to provide that those who have freely entered into a just agreement should be denied its use as a weapon to avoid meeting their obligations and when it can be clearly shown they are capable of doing so.

We believe this legislation will serve the purpose; therefore the American Industrial Bankers Association urges this committee to vote favorably on either H.R. 1057 or 5771.

Mr. ROGERS. Thank you, Mr. Denney. I have a few questions. The first one is, would you have any objection to amending this bill to cover all debtors who may file petitions in bankruptcy, except corporate debtors?

Mr. DENNEY. No, sir.

Mr. ROGERS. What has been the experience among the industrial bankers with those who may have discussed the matter of chapter XIII, wherein you have security, that is, a chattel mortgage, on an automobile, radio, television, or even home furniture?

Has there been any experience of wearing out of that automobile or other security?

Mr. DENNEY. You mean with reference to chapter XIII alone?

Mr. ROGERS. Yes.

Mr. DENNEY. Well, we have had this experience in many instances, and whether it was under chapter XIII, or whether they were just attempting to pay out their regular contract, where because of the hard use of the security, it did wear out before the contract was completed.

As to exact figures or percentages, I do not have it.

Mr. ROGERS. Has your association considered the possible unfairness to bankers financing automobiles which may result from holding their security in abeyance and possible depreciation during chapter XIII proceedings, when in fact the debtor may ultimately choose bankruptcy?

Mr. DENNEY. Well, this whole discussion, or this whole problem of the security wearing out has been discussed; yes, sir, many times, both insofar as this particular chapter XIII question is concerned, and in other instances, and of course, the conclusion that they have generally come to, when they have discussed this matter in panels or just among themselves is that they should try their best to not extend the length of time of the security beyond what the life of the security will be.

I mean, the time of the indebtedness beyond the life of the security. But this can't always be done. As we know, because it depends on the use it gets.

Mr. ROGERS. As Mr. Kendall testified here, no doubt, if everybody is compelled to take chapter XIII first, that it would result in additional expense, additional referees.

Do you concur with that statement?

Mr. DENNEY. Yes, I think it will, but I say compel that. I don't understand that by the act they will be compelled to take chapter XIII.

Mr. ROGERS. Well, now, of course, this leads into the next question I intended to ask you. You again talk to us about lawyers here on page 4. You blame the lawyers for not advising the client that he could file under chapter XIII.

Now, certainly, this bill, as written, and as I quoted before, beginning on page 1, line 10, says that in the event that a judge or referee shall determine the bankrupt has failed to make such a showing, he shall enter an order vacating the order of adjudication and dismissing the bankruptcy.

Now, my question to you is, do you feel that if we pass this legislation that the lawyers would become better educated? Would they then advise their clients: "Look, before you can file this petition, we have got to try to work something out, and make a showing that adequate relief cannot be obtained under the wage earner plan," with a result that the lawyer may be charging and properly would be entitled to a higher fee than just filing a petition in bankruptcy?

Mr. DENNEY. Well, I don't think passing the law is going to educate a lawyer. If that is part of your question. [Laughter.]

And I say this as a lawyer. I have been a lawyer since 1936, but I get the point. No, I don't think in and of itself that the passage of this act alone is going to cause the lawyers to suddenly jump up and encourage clients to take chapter XIII. The passage of a law alone is not ever going to do this, but the Consumer Bankruptcy Committee of the American Bar Association, of which I am a member, is continually trying to get across to the legal profession the wisdom of encouraging people to solve their problems under chapter XIII, and we feel that they will be more inclined to do so when they know there is a question of them having to show that it is possible for their client to come under this act.

Mr. ROGERS. Well, it at least would place an obligation upon the attorney, to my way of thinking, if a debtor came in and said, "I want to get bankruptcy relief." The first thing the attorney should explain, if we enact this bill, is what one has to do before he can obtain bankruptcy relief.

Mr. DENNEY. I would agree with that; yes, sir.

Mr. ROGERS. And certainly it is going to be educating to that extent.

Mr. DENNEY. Well, to that extent; yes, sir.

Mr. ROGERS. And since some of these high-priced lawyers, or even the low-priced ones, work on so much per hour—some of them quote \$50 an hour, and will be willing to settle for \$25—but even at that, if he charges on that basis, and takes a long time to explain this, wouldn't that tend to increase the amount that the lawyers get at the expense of the creditors?

Mr. DENNEY. Yes, I think it would. There is no question this might tend to induce them to talk along this line, if they thought they were going to get a little more.

Mr. ROGERS. Now, there has been representation made to me that in a certain section of the country, there was a man who advertises—or at least has a reputation, I will not accuse him of advertising—that he knows how to handle bankruptcy. What he does, he has the man come in, they file a petition, and then they go in and say, "Yes, we want to take chapter XIII."

Well, all the creditors think, "fine," and the attorney collects a good fee for filing the petition, and then after it is in operation about 60 days, he calls his client in, and says, "Well, now look, this is going to take too long, you just might as well take straight bankruptcy and you pay me another hundred dollars, and I will go down and ask for additional relief."

Have you run into any practice of that kind?

Mr. DENNEY. Do you mean have I personally run into any?

Mr. ROGERS. Yes.

Mr. DENNEY. No, sir; I have not.

Mr. ROGERS. Mr. Whitener?

Mr. WHITENER. Mr. Denney, I want to thank you and your distinguished brother for being with us.

One question that arises in my mind, under the normal chapter XIII proceeding, one of the first steps is to get the acceptance of the wage earner's plan by the creditors.

Now, if we should enact H.R. 1057, what would happen to the provision requiring some agreement among the creditors?

Mr. DENNEY. Well, I don't think that procedure necessarily needs to be changed. As I read the act, it is discretionary with the court, and if the judicial, if the Federal judges would lay down certain guidelines that they would have to get this, have this agreement ahead of time, as part of the basis upon which the referee would render his decision, why, I can't see that it would make any difference.

Mr. WHITENER. Well, my question, I suppose, stated more directly, would be this: under H.R. 1057, the referee would compel the wage earner debtor to proceed under chapter XIII rather than general bankruptcy.

Could, under this bill, the referee with equal authority require the creditors to go along with the chapter XIII proceeding?

Mr. DENNEY. Well, I would think he could.

Mr. WHITENER. Well, I don't mean to sound like a devil's advocate, but why do you make this statement? What do you base it on?

Mr. DENNEY. Well, again it is a question of discretion and if before he makes his decision as to whether they are going to permit the straight bankruptcy to be dismissed, and some under chapter XIII, he is going to examine the whole picture, and unless it can be seen that everybody is agreeable to this, I think it would be within his discretion to turn it down.

Mr. WHITENER. Well, as I understand the chapter XIII procedural steps, among those steps is a requirement that either prior to or subsequent to filing the petition in behalf of the wage earning debtor, there must be notice and meeting of the secured and unsecured creditors.

Mr. DENNEY. Right.

Mr. WHITENER. Now, under the present law, as I understand it, the results of this meeting—the concurrence or nonconcurrence of the creditors is brought to the attention of the referee.

Mr. DENNEY. Yes.

Mr. WHITENER. And if there is not adequate compliance or agreement on the part of the creditors with this plan, then the referee can't allow the wage earner debtor to proceed under the chapter XIII.

Mr. DENNEY. Well, I can't see anything that would prevent him from still denying it, if they couldn't have the agreement that would be within the discretion.

Mr. WHITENER. Now, suppose that the referee orders, as this bill provides, that the wage earner debtor go through the chapter XIII procedure, and all of the creditors or a sufficient number of them agreed with him. Then the wage earner wouldn't have any choice about it, would he?

Mr. DENNEY. He can appeal, as I understand this. He doesn't have to. He can still appeal. And doesn't he have the—

Mr. WHITENER. Yes, but this is my point. That the creditors do not have to appeal, do they?

Mr. DENNEY. They don't have to. They can just say, "We don't want to go."

Mr. WHITENER. That is it.

Mr. DENNEY. I think, as I understand it, he can just stop the whole thing by saying, "I don't want to go under chapter XIII."

Mr. WHITENER. The creditors can stop it in its tracks, but the debtor can't, unless he goes to a higher court. Is that right? Or to the judge?

Mr. DENNEY. I guess I can't answer your question. I am sorry.

Mr. WHITENER. Now another thing: Your tax people, they don't have to agree to anything, do they? They can insist on their pound of flesh before the secured or the unsecured creditors come in, if they have a prior tax claim.

Mr. DENNEY. Of course, they have a preferred claim, as I understand it, and that doesn't change with this act one way or the other, no.

Mr. WHITENER. No. My point is that everybody has a choice except the wage earner if you make this compulsory. Isn't that correct?

Mr. DENNEY. I still don't see it as compulsory, when he has the right to say that he doesn't want to. And then his bankruptcy is dismissed, that's true, his straight petition is dismissed, but he does not have to take chapter XIII.

Mr. WHITENER. That is right, but if he doesn't take one route or the other, he gets no discharge of any liability.

Mr. DENNEY. That is right. And, of course, again as was pointed out by the other two gentlemen, you are going on the basis that this man as a referee has got a sense of judgment based on his experience as a referee, and he is going to look into this thing, and if he thinks that the

plan can't be worked out for one reason or another, he can then say, "All right, we will go ahead through straight bankruptcy."

Mr. WHITENER. Well, now, have you had any intimation as to how the landlords or lessors might feel about this compulsory or——

Mr. DENNEY. No, I have not. My people aren't in that type of business.

Mr. WHITENER. You know, they can take a pretty bad licking, particularly under chapter XIII, if they are limited in the amount of their recovery.

Mr. DENNEY. Yes.

Mr. WHITENER. And I just wondered if in your work you had had any occasion to get their views?

Mr. DENNEY. No, I have not.

Mr. WHITENER. Thank you.

Mr. ROGERS. Mr. Poff?

Mr. POFF. Thank you, Mr. Chairman.

As I understand your response to the questions of the gentleman from North Carolina, it is true that the creditors could frustrate the use of chapter XIII if less than a majority of them were willing to approve the arrangement?

Mr. DENNEY. That is right.

Mr. POFF. Yet I think it must be borne in mind that the consequences of their action is a discharge of bankruptcy.

Mr. DENNEY. Right.

Mr. POFF. And I suggest that the creditors, then, have some incentive to agree to the plan.

Mr. DENNEY. That's right.

Mr. POFF. I will not ask other questions. I thank you gentlemen for your interesting testimony.

Mr. ROGERS. Mr. McClory?

Mr. MCCLORY. No, I have no questions, Mr. Chairman.

I am delighted to have the witness appear this morning with his very important testimony, and also to recognize the very fine sponsorship he has in the person of the Member from the First District of Nebraska, whom we are happy to have in the U.S. House of Representatives.

Mr. ROGERS. Mr. Wiggins?

Mr. WIGGINS. Just very briefly, Mr. Chairman, I particularly want to compliment the three-pronged program that has been instituted by the finance industry, and would suggest at least one more.

In my personal experience, one of the principal causes of these so-called unnecessary bankruptcies is the overzealous collection attempts by your own industry, and particularly your assignees. I would hope that your education program would extend to that part of the problem as well.

Mr. DENNEY. Yes, it does.

The organization that I represent has a school that we call National Installment Banking School, NIBS, at Boulder, Colorado, which is a school for our managers and supervisors, and so forth, and one of the courses that we teach there is this business of not being overzealous in these collections.

We realize that this has created a bad public image, and we are trying to overcome it.

Mr. WIGGINS. More than that, it created the very problem that brings us here this morning.

Mr. DENNEY. Right.

Mr. WIGGINS. And I wish you well in that effort, because if you do solve it, I think it will go a long way to solving the overall problems that we are all seeking solutions for.

Now, the suggestion has been made that whatever the laudatory purposes of this bill, that mechanically, it isn't going to work, that an individual debtor is just not going to pay. What do you say the consequences of that failure should be?

Mr. DENNEY. Well, our experience in this business for some 50 years indicates that there are some people that never will pay, and there isn't any law or anything else that is going to make them pay, but we think that this procedure and this amendment will encourage them, and as Mr. Kendall pointed out, it gives them a plan, and many of them need encouragement, and when this can be pointed out to them, I think it will help.

No, it isn't going to solve all the problems, by any means.

Mr. WIGGINS. What do you feel the consequences of the failure to live up to the plan should be?

Mr. DENNEY. Well, of course, I think that the consequences of the failure to live up their indebtedness of any kind should be the refusal to extend them credit in the future.

Mr. WIGGINS. Well, should it have any impact upon their right to a discharge, in your opinion?

Mr. DENNEY. Well, if they willfully refuse to, then I don't think they should be given a discharge in bankruptcy.

Mr. WIGGINS. All right. Thank you very much.

Mr. DENNEY. Now, I should add to that if they show some good reason, or an emergency that was not contemplated when the plan was originally set up, that makes it an entirely different story. And is again within the discretion, then, of the court.

Mr. WIGGINS. Thank you for your answer, Mr. Denney.

Mr. ROGERS. Counsel has some questions.

Mr. ZELENKO. Just one question, Mr. Chairman.

The Judicial Conference during the last Congress disapproved legislation identical to that which the committee is considering today. I would like to quote one pertinent part of its report:

Other petitioners not wage-earners could still avail themselves of straight bankruptcy procedures and the benefits arising out of discharge of debts. Moreover, it seemed unfair to the committee—that is, the Committee on Bankruptcy Administration of the Judicial Conference—to compel a debtor to accept a plan under Chapter XIII without equal compulsion upon secured creditors to accept the same plan.

This is a further reference to the question that Congressman Whitener was asking you, Mr. Denney. What would your view be to an amendment to this legislation that would provide that the secured creditors would be required to go along with a chapter XIII plan, where the court found that the debtor was not entitled to bankruptcy relief?

Mr. DENNEY. Well, I am not sure that I can answer that, because I hadn't thought about it. I want to—and of course I am here not in a personal capacity, and I might have a personal opinion as an attorney.

ney, but I am representing this association, and that part has not been discussed, so I am sorry, I am not in a position to answer that question.

Mr. ZELENSKO. Thank you, Mr. Denney.

Thank you, Mr. Chairman.

Mr. ROGERS. Thank you, both Mr. Denneys, for the benefit of your testimony, and we certainly appreciate having you here.

Mr. MAX DENNEY. Thank you, sir.

Mr. ROGERS. Mr. Wetzel?

Come forward here.

Mr. WETZEL. Might I have permission to bring with me Mr. Twinem, please, Mr. Chairman?

Mr. ROGERS. Yes; both of you come forward.

At this point, I will place into the record a statement of CUNA International, Inc.

(The statement referred to follows:)

STATEMENT OF CUNA INTERNATIONAL, INC.

CUNA International, Inc., is a non-profit association of credit union leagues. In this country, there are 48 state credit union leagues which represent approximately 22,000 credit unions. This statement is submitted on behalf of those credit unions in support of H.R. 1057.

A credit union is a non-profit mutual membership organization chartered for the purpose of promoting thrift and providing provident and productive loans. A credit union does not deal with the general public. It must have a common bond of membership and it can only deal with members. The members pool their savings and lend to each other. Each member of the credit union has one vote which he is free to exercise for the election of officers and for many other purposes. In order to become a member, an individual must pay a 25 cent admission fee and he must agree to subscribe to one 5 dollar share.

We in the credit union movement like to believe that credit unions exist for one purpose—that purpose is to serve the members. Traditionally, we have fulfilled a substantial need for those who have been unable to obtain credit. We like to believe that we have been responsible for proving to other lenders that the "average man", whether he is a factory worker, an enlisted man in the military, a teacher, a civil servant, or a welfare recipient, has the capacity and the character to repay his loans if he is dealt with fairly and counseled wisely.

To this end, we like to think of ourselves as more than just a savings and lending institution. We believe that we are also an educational institution and a considerable amount of our time is devoted to educating our members. Among the more important of our educational programs is the family financial counseling course which, in many cases, is available to credit union members through a correspondence course.

Since credit unions are membership organizations which do take the time to counsel with members and do assist them in arranging their finances, we feel quite strongly that the member in turn has an obligation to do everything possible to repay his debts to those with whom he shares a common bond of association or employment. It is primarily for this reason that we strongly support H.R. 1057.

This bill amends the Bankruptcy Act to permit the courts to deny straight bankruptcy relief in wage earner cases if Chapter XIII can be utilized by the debtor to amortize his indebtedness out of future earnings over a period of years. It amends Section 55b of the Bankruptcy Act, which deals with the first meeting of creditors, by providing that if the bankrupt is a wage earner within the meaning of Subsection 8 of Section 607 of the Bankruptcy Act the judge or referee shall determine whether the bankrupt has shown that it is not feasible for him to pay his debts under Chapter XIII of the Act. If the judge or referee determines that the bankrupt has failed to make such a showing, he may enter an order vacating the order of adjudication and dismissing the bankruptcy proceedings with notice to all of the bankrupt's creditors unless, within such time as the judge or referee shall fix, the petition be amended to comply with the requirements of Chapter XIII for the filing of a debtor's petition.

Our support of this bill is given with the realization that there are many factors which cause individuals to declare bankruptcy and that there is need for reform in many of the traditional legal concepts governing the relationship between a debtor and a creditor. The existence of these does not however detract from the need for the particular provisions contained in this bill.

We also realize that the substantial increase in the number of personal bankruptcies is of course partially related to the substantial increase in the use of consumer credit and to an increased knowledge on the part of the general public as to the existence of the availability of bankruptcy as a means of relief from financial problems. On the other hand, we are convinced that the general public does not have adequate knowledge about Chapter XIII. Nor does the legal profession. It is well known that it is much simpler for an attorney to advise his client to seek straight bankruptcy rather than a Chapter XIII proceeding since the attorney is generally more familiar with straight bankruptcy and since the amount of time expended by the attorney in a straight bankruptcy is considerably less than that expended in a Chapter XIII proceeding.

In view of these factors, this particular bill can serve as an educational device which will require attorneys, referees, and the general public to become more familiar with Chapter XIII proceedings and to use them more extensively. That this is possible has already been proved in that there are many judicial districts where Chapter XIII has been promoted by attorneys and referees and where the use of straight bankruptcy is therefore kept at a minimum.

We are of the opinion that the purpose of this bill is to screen out the unnecessary bankruptcy cases in which the debtor has sufficient earnings to handle his debts. The purpose is not to deny a discharge in bankruptcy if a wage earner needs this form of relief. This is a perfectly fair and logical goal. When a lender extends credit to a wage earner, it certainly considers the wage earner's ability to repay. If that ability can be used without undue hardship, it should be used.

As the Chairman of this Subcommittee has pointed out, there are many benefits which accrue to a debtor through the use of Chapter XIII. First and foremost is that the borrower avoids the stigmatic consequences of bankruptcy and retains his credit rating. This enables him to keep within the legitimate credit market for his future borrowing needs rather than falling prey to those creditors who prefer to deal with borrowers who have had the mantle of potential relief removed for six years by a straight bankruptcy discharge.

Among the many other benefits are the following:

(1) The so-called "Wage-Earner's Plan" suffers from a misnomer. Its benefits are available to the salaried employee, as well as the wage earner.

(2) Every exemption available to the debtor in straight bankruptcy is available to him under Chapter XIII proceedings.

(3) Any contract which the debtor has been enticed to enter by fraud or misrepresentation can be either reformed or annulled.

(4) In proper cases, interest and finance charges or unsecured creditors' claims can be reduced or eliminated.

(5) Certain types of executory contracts may be revised or rejected.

(6) During the dependency of the proceedings, collection suits, garnishment process and involuntary bankruptcy petitions can be suspended.

(7) Even after the plan has been approved and put into operation, deposits required of the debtor under the plan can be reduced in amount or the time for repayment can be extended if the debtor later experiences unforeseen hardships.

(8) At any time during the proceeding, if it becomes apparent that the debtor cannot in fact meet the requirements imposed upon him under the plan, the referee can restore the debtor's right to pursue straight bankruptcy.

(9) Finally, at the end of the three-year period, if the referee is convinced that the debtor made a good faith effort to abide by the plan, he can grant him a discharge even though the debtor may now have completed all of the payments.

In summary then we believe that this bill is a definite improvement over the present law which denies a judge or referee jurisdiction or discretion to use Chapter XIII in appropriate cases even though a debtor may be fully capable of paying his debts out of future earnings.

Mr. ROGERS. Our next two witnesses are representing the American Bar Association, Mr. Carroll R. Wetzel, chairman of the Section of Corporation, Banking and Business Law, and Mr. Linn K. Twinem, chairman of Consumer Bankruptcy Committee.

Now, we have a prepared statement from Mr. Wetzel.

STATEMENTS OF CARROLL R. WETZEL, CHAIRMAN, SECTION OF
CORPORATION, BANKING AND BUSINESS LAW, AND LINN K.
TWINEM, CHAIRMAN, CONSUMER BANKRUPTCY COMMITTEE OF
THE AMERICAN BAR ASSOCIATION

Mr. ROGERS. We will place your statement in the record, and you proceed to testify in your own manner.

(The statement referred to follows:)

STATEMENT BY CARROLL R. WETZEL ON BEHALF OF THE
AMERICAN BAR ASSOCIATION

My name is Carroll R. Wetzel. I am a member of the Philadelphia law firm of Dechert, Price & Rhoads and chairman of the Section of Corporation, Banking and Business Law of the American Bar Association.

For a number of years the Section of Corporation, Banking and Business Law has been disturbed by the rising flood of individual bankruptcies. Many of those bankruptcies have been found to be unnecessary. To screen out the needless or avoidable cases the Section recommended a change in the Bankruptcy Act. On May 24, 1965, the Board of Governors of the American Bar Association approved the recommendation of the Section by adopting the following resolutions:

"Resolved, That the American Bar Association approves the principal of H.R. 292*, 89th Congress, which would amend the Bankruptcy Act to provide that the Referee shall have discretionary authority to dismiss the voluntary bankruptcy proceeding of a wage earner who fails to show that adequate relief cannot be obtained in a Chapter XIII Wage Earner Plan."

"Resolved, That the Section of Corporation, Banking and Business Law is authorized to urge before the appropriate Committees of Congress the enactment of such legislation."

Part of the background for the Section's recommendation was that bankruptcy proceedings have reached the point of near scandal in some areas where numerous debtors have needlessly evoked the relief of a discharge from their obligations under straight bankruptcy proceedings. Studies conducted at Michigan State University, University of Arizona, University of Utah and elsewhere have shown that from 25% to 45% of the personal bankrupts could have paid their debts out of future earnings if they had been so inclined and properly advised. In addition, in many cases debtors are undoubtedly not made aware of their right to protection and relief under Chapter XIII of the Bankruptcy Act.

The problem continues to be of growing concern. In the fiscal year ending June 30, 1967, it is anticipated that more than 200,000 bankruptcy petitions will be filed and that nearly \$1,500,000,000 will be washed down the bankruptcy drain in no-asset bankrupt estates. More than 91% of all of the bankruptcy filings in this fiscal year will be in the non-business category.

Under the present Act any person, regardless of his financial condition or solvency, may petition for a discharge in straight bankruptcy and readily restrict the payment of his just debts to the assets turned over to the Bankruptcy Court. This amendment would retard the abuse of the bankruptcy procedure and encourage a constructive solution to debt problems, and would be in the interest of the general economy and of individual responsibility and morality.

The proposed amendment has been opposed on the basis that every person should have an unrestricted right to obtain a discharge in bankruptcy and that the proposed amendment would be unfair to wage earners. But, Congress provided for a distinction in treatment of wage earners in 1938 when Chapter XIII was added to the Bankruptcy Act. It has been regarded as a reasonable distinction and classification, now applicable to about 90% of all bankruptcy filings. Even so, no wage earner would be compelled to proceed under Chapter XIII, although if he did not do so in a proper case the Referee could dismiss his bankruptcy petition. Furthermore, a wage earner, to a greater extent than a business bankrupt, usually has obtained his credit on the basis and faith of his ability to pay out of future earnings. If he continues to have that ability to pay, it is only fair to his creditors that he should be expected to do so. While so doing, he has the right to enjoy the benefits of a wage earner plan and the protection of the Bankruptcy Court if he desires. Those debtors for whom it is not reasonably possible to pay their debts will continue to be entitled to a discharge in straight bankruptcy.

Individuals in business for themselves already enjoy an advantage in bankruptcy over the wage earner. The principals of a bankrupt corporation can immediately and repeatedly go back into business as a new corporate entity, and every corporation is entitled to go bankrupt. The wage earner who has been discharged in bankruptcy is not entitled to this relief for a six-year period. This fact is well known to certain classes of lenders and sellers who take advantage of the bankrupt wage earner who can find no relief from the payment of these new debts, no matter how desperate his situation may become. Because of this predicament in which a bankruptcy discharge can place a wage earner, if for no other reason, the granting of a discharge in bankruptcy should be available only when no other solution is reasonably possible.

These are some of the reasons why the American Bar Association has approved the principal of this bill. The proposal originated in the Consumer Bankruptcy Committee of the Section. The details of the bill will be covered by Linn K. Twinem, the chairman of that committee.

Mr. WETZEL. Mr. Chairman, in the interest of time, since this statement is in the record, I will not read it in full. I will attempt to summarize it for you.

Mr. ROGERS. Fine.

Mr. WETZEL. My name is Carroll Wetzel. I am a member of a Philadelphia law firm, and I am chairman of the Section of Corporation, Banking and Business Law.

For some years our section has been concerned by the statistics that have come to us with respect to a rising trend in individual bankruptcies. The number has gone up really quite alarmingly, and we have been concerned about the reasons for this and, hopefully, to determine some way of reducing it.

On the recommendation of our Committee on Consumer Bankruptcy, we recommended to the American Bar Association as a whole that it approve in principle the bill, H.R. 292, of the 89th Congress, which is identical with H.R. 1057 which we are considering today.

Action was taken by the Board of Governors of the American Bar Association on May 24, 1965, and our section was directed to urge the enactment of legislation of that type.

Studies have been conducted at Michigan State University, at the University of Arizona, the University of Utah, and elsewhere which have shown that from 25 percent to 45 percent of personal banknotes could have paid their debts out of future earnings if they had been so inclined, and if they had been properly advised. We believe that in many cases, individual banknotes are in fact not made aware of their right to their protection and relief under chapter XIII.

This problem is not going away. It is getting larger. In the fiscal year ending June 30, 1967, it is anticipated that more than 200,000 bankruptcy petitions will be filed, and that nearly \$1,500,000,000 will go down the drain in no-asset bankrupt estates. More than 91 percent of all the bankruptcy filings in this fiscal year will be in the non-business category.

I would like to mention one reason for this legislation which seems to me to have considerable validity which I have not heard mentioned this morning.

At the present time, an individual is entitled to a bankruptcy discharge only once every 6 years. There are, we all know, certain types of lenders, as has already been suggested here this morning, which do prey on certain individuals in the collection of their debts.

I can't imagine a worse plight for an individual to be in than to have received a bankruptcy discharge, and to be completely vulnera-

ble for the next 6 years. He has no relief of any kind whatsoever. If he had been fully advised of his rights, if there had been some method in which in the original filing of his petition he could have adopted a proper chapter XIII proceeding, he would not be in that position for the next 6 years.

Mr. ROGERS. Thank you.

Mr. Conyers?

Mr. CONYERS. May I ask—

Mr. WETZEL. Excuse me, sir. Before you ask me a question, may I ask permission to have Mr. Twinem add anything that he would care to add to what I have said, if he would care to, at this time?

Mr. ROGERS. Yes. I think that Mr. Twinem is an expert in this area of bankruptcy—should we say an expert in bankruptcy generally—so if you have any questions, propound them to both gentlemen.

Mr. CONYERS. I would like to just raise one consideration here, and I apologize for not having been able to hear previous testimony on the subject, but apparently, the suggestion is implicit that the chapter XIII wage earner plan is not being fully used at present.

Is this because the referees in bankruptcy are not alert to this situation, or are not able to discern into these cases and to make sure that this alternative procedure is being considered?

Mr. WETZEL. I will touch on that, sir, and then perhaps Mr. Twinem could add more specific details than I will be able to give.

It has been suggested here this morning, and properly so, that straight bankruptcy is a relatively easy, simple thing to administer. Counsel gets a hundred dollar fee, he files a paper, the referee has no great problems. He is paid, and that's that.

There is no doubt at all that chapter XIII imposes a greater burden on the attorney. It imposes a greater burden on the referee. It is not in fact attractive to the people who are obliged to administer it under the present system.

I think that is the simple answer to the question.

Mr. TWINEM. Mr. Conyers, you suggested or indicated that possibly the referees are not fully aware of the importance or the procedure provided under chapter XIII of the Bankruptcy Act. I don't think that's true, because I know the Judicial Conference has made a very studious and careful effort to encourage the use of chapter XIII, and the word has been passed certainly directly to the referees.

They are well aware of it, but there are two groups of referees, in my opinion, as I have studied this development, and one group, many of them are the oldtimers, the ones that have been on bankruptcy court for a long time, have a very definite feeling against chapter XIII, and it is a burden on them, and they don't like it, this principle.

They fought it along with some members of the National Bankruptcy Conference when chapter XIII was considered in 1938, they have never accepted it, and they abhor it, and will stay as far away from it as they possibly can.

On the other hand, there is a new group of referees that have been appointed more recently, who take more kindly to it; and where the referee does evidence a sincere interest in the development of chapter XIII, and the use of wage earner plans, it will work.

We have a referee in the audience now from Maine. He has been one that has encouraged the use of chapter XIII, and has a good many cases pending in his court.

You have a good referee in Michigan, in Flint, Mich. Referee Bouvier, who is filing a statement with this committee before the conclusion of your record, who believes very sincerely in the use of chapter XIII, and in the encouragement of its use.

And at the same time he feels that in many cases that he is a little bit frustrated, because there is nothing he can do to require its use, except to make the suggestion which can be totally ignored by the lawyer and by the client, if they see fit.

And you may hear from Judge Brown, Wesley Brown, tomorrow. He is a former referee in Kansas. He became interested in and enthusiastic about chapter XIII, and he developed a very good chapter XIII proceeding in Kansas, and he has since been elevated. I don't know whether this is the way to get to the Federal bench or not, but Wesley Brown went up that way, and Judge Allgood of Alabama, who was down in the cradle of chapter XIII, has also gone up to the Federal bench. Maybe that's the avenue.

But as I tried to make the point, if the referee is sincerely interested in chapter XIII, he can develop a good chapter XIII program.

If he abhors it, he will have very few, if any. It is surprising to look at the record comparatively throughout the country and see how few XIII's there are in some areas. You will find in New York, for example, that you get down below 1 percent, in some areas, and in other areas you will run up to as many as 88 percent of all of the personal filings will be under chapter XIII.

Mr. CONYERS. Mr. Chairman, I thank the gentlemen for their comments.

Mr. ROGERS. Yes. Thank you.

Mr. Poff?

Mr. POFF. Mr. Chairman, as the chairman knows, I am obliged to leave shortly, and I will ask only one question, if I may, but with the hope that the witnesses might be available tomorrow, if we need to continue their interrogation.

Mr. ROGERS. Yes. I understand Mr. Twinem will be available but Mr. Wetzel will not.

Mr. POFF. May I address this question, then, to Mr. Wetzel?

Mr. WETZEL. Yes, sir.

Mr. POFF. Mr. Wetzel, do you think it is feasible to apply the procedures of H.R. 1057 to corporate debtors as well as individual debtors?

Mr. WETZEL. I hadn't thought about that until the question was raised earlier this morning.

I have thought about it only during the last hour or so. I don't see how. Let me say that in all of this, I am speaking only personally, and I am delighted to speak. My only authority on behalf of the American Bar Association is to approve in principle the bill which is now before you.

It seems to me that the most valid distinction which can be made is the one that Mr. Kendall made between consumer credit and corporate business credit. I don't see how the type of program that is being contemplated here could, as a practical matter, be made to function with respect to a corporate business; by its very nature, the corporation is a business entity. It, as Mr. Kendall said, it is an entity which has assets, and liabilities, and loans are largely based on that.

The proper distinction does seem to me to be between corporations and individuals.

Your chairman asked various witnesses if they would think that this bill might be extended to all individuals, rather than just wage earners. That would seem to me to be entirely sensible, speaking for myself, but I don't see how you apply it to corporations.

Mr. POFF. Well, would the witness feel that other chapters of the Bankruptcy Act might serve essentially the same function with respect to corporate debt?

Mr. WETZEL. In a sense, chapter XI performs the same function, but as one of the members of your committee pointed out, there is no compulsion in chapter XI. He was quite correct in that. It is a voluntary procedure.

Now, how you would require a corporation to elect chapter XI, and what the technical results of that would be with respect to the future operations of the corporation, it is very difficult for me to say.

I can visualize this concept with respect to myself, but I have great difficulty visualizing it with respect to a corporate entity. That's all I can say, and I have only thought of it for a half an hour.

Mr. POFF. I suggest, Mr. Chairman, that if the subcommittee considers that possibility, it may want to invite testimony of experts, and in such case, maybe the witness would be available to supply his expertise in the field, if so requested by the subcommittee.

Mr. WETZEL. I would be delighted, sir. I am very sorry about tomorrow, but I have an engagement, several engagements back in Philadelphia, and I really must be there, if the committee would permit it.

Mr. ROGERS. Yes.

Mr. McClory.

Mr. McCLORY. Thank you, Mr. Chairman.

The committee received a statement today from Mr. R. E. Jackson, Chief of the Bankruptcy Division of the Administrative Office of the U.S. Courts. In that statement, he said that during fiscal 1966, 132,038 petitions in bankruptcy were filed of employees, who might have availed themselves of chapter XIII proceedings.

The statement also indicated that if one-third of this number had availed themselves of it, or approximately 44,000 had elected and completed successfully chapter XIII proceedings, that an additional total of from \$36 to \$40 million would have been received by creditors.

Now he goes on to point out, though, in his opinion, that if the chapter XIII proceeding is involuntary, instead of voluntary as it is presently, the incentive would not be there. He concludes that if H.R. 1057 is enacted, it seems likely that it may increase creditor losses, rather than decrease them.

I just point out he states that "an involuntary chapter XIII proceeding would very likely be looked upon by the debtor as a punishment, and all incentive to reform his spending habits would be destroyed."

I would like you gentlemen to comment on that statement, or that part of the statement by Mr. Jackson, if you would.

Mr. WETZEL. Well, sir, I will speak briefly. We are now in the question of morality and psychology, as was suggested a moment ago. I don't know how you decide whether a person who under some slight compulsion pays all of his debts feels better than if he didn't pay them at all. It seems to me I would feel better.

If I needed a little bit of help to get me to pay all my debts, I still think I would feel a little bit better if I paid them. I don't understand the other point of view, but I don't see how anybody can—

Mr. McCLODY. Well, would the creditor be better off? He is saying that the creditors would be worse off than they are today. Do you agree?

Mr. WETZEL. I beg your pardon. I misunderstood. I thought your question was directed to the point of view of the debtor.

Mr. McCLODY. It is both, but I just was asking you to comment on his statement. Of course, he does make the statement that there wouldn't be any incentive, and the debtor would look on it as punishment, but in addition to that effect, he says that the creditors would be worse off than they are now because actually they wouldn't complete these programs and the creditors wouldn't get their money.

Mr. WETZEL. I don't know how anyone proves such a statement one way or the other. It does seem to me that, in the long run, more creditors would get more money.

Mr. Twinem?

Mr. TWINEM. It seems to me that the proposition is based on a false premise, and I must insist from my point of view that in no case may we regard H.R. 1057 as providing for compulsory chapter XIII. I couldn't agree with the critics more that compulsory chapter XIII will not work. It is absolutely unworkable, in my opinion. It must be entirely voluntary on the part of the debtor. He must want chapter XIII. He must want the guidance and protection of the Bankruptcy Court enough to be willing to make the sacrifices required of him to go under chapter XIII.

H.R. 1057 merely would have the effect of screening out the unnecessary bankruptcy proceedings. If I have—how much time do you have to talk about this vital point? May I take 4 or 5 minutes?

Mr. ROGERS. You mean now or later?

Mr. TWINEM. Whenever you please, sir. But this is a vital point, and I want to go into the background and principles and philosophy of this legislation.

Mr. ROGERS. Surely. We recognize, and you recognize, that the time is about up today, and we want to hear you tomorrow, and you can go into this very extensively. There will be a lot of questions, no doubt, asked of you.

It depends upon whether we will have an opportunity to meet tomorrow afternoon, which we will try to work out.

Mr. Wiggins, do you have any questions?

Mr. WIGGINS. Just one question of Mr. Wetzel, since he must go back to Philadelphia.

What do you think the proper consequences should be, sir, if a debtor does not live up to the payment as proposed by the referee?

Mr. WETZEL. I hadn't thought about that, either, until you asked the other witness that this morning. It seems to me that that should depend on why he didn't live up to the plan. The referee in bankruptcy has authority to deny discharges, if the bankrupt does not behave in good faith.

I think all I can say in answer to the question is that in a general way the same principle should apply.

Mr. WIGGINS. I agree with the gentleman. Thank you very much.

Mr. ROGERS. Well, thank you. We appreciate both coming, and we will look forward to hearing you tomorrow.

The committee will now stand in recess until tomorrow at 10 o'clock, at which time we will hear the Honorable Wesley E. Brown and the Honorable Richard E. Poulos and Professor Vern Countryman, and others.

The committee stands in recess.

(Whereupon, at 12:17 p.m., the subcommittee recessed, to reconvene at 10 a.m., Thursday, May 25, 1967.)

WAGE EARNER PLANS UNDER THE BANKRUPTCY ACT

THURSDAY, MAY 25, 1967

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE No. 4 OF THE COMMITTEE OF THE JUDICIARY,
Washington, D.C.

The subcommittee met, pursuant to call, at 10:10 a.m., in room 2141, Rayburn House Office Building, Hon. Byron G. Rogers (chairman of the subcommittee) presiding.

Committee members present: Representatives Rogers, Whitener, Jacobs, McClory, Wiggins, and Poff.

Staff members present: Benjamin L. Zelenko, counsel; and Donald E. Santarelli, associate counsel.

Mr. ROGERS. The committee will resume its sitting and its hearings in connection with H.R. 1057 and H.R. 5771.

We are privileged to have with us this morning the Honorable Wesley E. Brown, judge of the U.S. District Court, the District of Kansas, whose home is Wichita, who is also a member of the Committee on Bankruptcy Administration of the Judicial Conference of the United States.

Come forward, Judge Brown. As I understand, you were at one time a referee in bankruptcy?

Judge BROWN. Yes, sir.

Mr. ROGERS. We are anxious to have the benefit of your views on this legislation.

STATEMENT OF HON. WESLEY E. BROWN, JUDGE OF THE U.S. DISTRICT COURT FOR THE DISTRICT OF KANSAS

Judge BROWN. Mr. Chairman, I am Wesley E. Brown, and I am judge of the U.S. District Court for the District of Kansas. I have been a judge of this court since April 1962.

Prior to that time I was a referee in bankruptcy for the District of Kansas from April 1958 to April 1962. I appear on behalf of the Committee on Bankruptcy Administration of the Judicial Conference of the United States in opposition to H.R. 1057 and H.R. 5771.

I am a member of this Bankruptcy Committee and have been such a member for approximately 4 years.

THE BANKRUPTCY COMMITTEE

The Bankruptcy Committee, which is composed of three circuit and four district judges, meets twice a year prior to the meetings of the Judicial Conference of the United States for the purpose of reviewing the administration of bankruptcy proceedings in the courts.

The Bankruptcy Committee examines such bankruptcy proceedings and makes recommendations to the Judicial Conference concerning the bankruptcy courts for Conference consideration and appropriate action.

These recommendations are formulated by the Director. Where appropriate, the Bankruptcy Committee acts only after consultation with the district judges and judicial councils of the circuits concerned. The Committee's actions relate to the following matters:

1. The authorization of new referee positions and changes in character of or salaries of existing referee positions. (Recommendations of districts and circuits involved are sought prior to Committee action in this respect.)

2. The territories, headquarters, and places of holding court of the referees.

3. The budget estimates for the bankruptcy courts.

4. The status of the special fund in the Treasury out of which all salaries and expenses are paid. This fund is maintained by filing fees and other payments made by parties to bankruptcy proceedings.

5. Proposed legislation to amend the Bankruptcy Act. The Committee's actions upon proposed legislation are premised upon requests from appropriate legislative committees. Conference direction, or in rare instances when its attention is called to a measure which does not involve legislative policy and which may adversely affect bankruptcy administration.

Its recommendation in such regards are reported to the Conference for consideration and direction.

6. The volume and character of the bankruptcy cases filed in the bankruptcy courts and the status of the referee's dockets.

7. The seminar program for the referees.

8. Costs of administration in bankruptcy cases and methods of achieving economy in administration.

9. The facilities of the bankruptcy courts, staffs, libraries, quarters, and similar arrangements.

STATEMENT LIMITATIONS

I wish to make it clear, Mr. Chairman, that nothing contained in my statement or in reply to any questions propounded to me is to be considered by any congressional committee either as an effort to interfere with matters involving congressional policy or as expressing any opinion as to whether or not the bill is constitutional.

PRIOR CONFERENCE AND BANKRUPTCY COMMITTEE ACTION

The Bankruptcy Committee was first concerned with the principles enunciated in H.R. 1057 when it was requested to express its views to the Conference with respect to H.R. 292 and S. 613, 89th Congress. H.R. 1057 and H.R. 292 are identical.

In its consideration of H.R. 292 and S. 613, the Committee gave consideration to whether or not we were involving ourselves with congressional policy.

We determined that, because of the effect of the bills on the administration of the Bankruptcy Act by the courts, the congressional

committee was entitled to the views of the Conference if the Conference desired to make its views known.

In the report of the Judicial Conference of the United States proceedings, March 18-19, 1965, the Conference upon the recommendation of the Bankruptcy Committee voted to disapprove S. 613 and H.R. 292.

The report stated in part:

While it is recognized that many straight bankruptcy cases can and should be administered as wage earner proceedings, it was the view of the Bankruptcy Committee that the proposals contained in these bills are discriminatory in singling out a low income group that would be compelled under Chapter XIII to pay their debts in full.

Other petitioners, not wage earners, could still avail themselves of straight bankruptcy proceedings and the benefits arising out of a discharge of debts.

Moreover, it seemed unfair to the committee to compel a debtor to accept a plan under Chapter XIII without equal compulsion upon secured creditors to accept the same plan.

To summarize the report, the objections may be listed in three categories:

1. It singles out the individual wage earner or a low-income man or woman to require payment of his or her debts in full.
2. A non-wage earner could be discharged of his or her debts.
3. Secured creditors are not required to accept the same plan.

HISTORICAL REFERENCE

The ultimate judgment which Congress must make with respect to H.R. 1057 requires at least a brief historical consideration of congressional exercise of its power "to establish * * * uniform laws on the subject of bankruptcies throughout the United States."

In passing, it may be noted that Congress has upon three occasions repealed bankruptcy acts previously adopted. The economic plight of many people, and the effect of this on the national economy caused Congress to enact a comprehensive bankruptcy act which has been referred to as the Chandler Act.

The courts in interpreting this act and its amendments to date have done so to effectuate the indicated congressional purpose.

I respectfully refer you to House Report 1409 and Senate Report 1916.

We summarize this purpose as follows:

1. To relieve an honest debtor from oppressive indebtedness and to permit him to start afresh.
2. To effect a prompt and economical liquidation and distribution of insolvent estates.
3. To establish and encourage a rehabilitation and reorganization procedure based upon compositions and extension of debts rather than liquidation.

Bankruptcies have increased over the years to a considerable degree. I have attached to this statement records of filings for review by the congressional committee. It should be remembered that statistical data may be interesting but courts deal with debtors and creditors on an individual basis.

These are "persons" who seek relief, not statistics.

Moreover, with regard to the dismay expressed by certain segments of the business community over the increasing number of bankruptcies, it is necessary to place that statistic in perspective.

Bankruptcies have only kept pace with the increase in consumer credit extended by business. The correlation is striking. We see from the Federal Reserve Bulletin that outstanding nationwide consumer credit, by which I mean individual obligations for household, family, and personal expenditures not including real estate mortgage loans, advanced from \$5.6 billion in 1945 to \$80.6 billion in 1965, or, if my mathematics is correct, an increase of 1,500 percent.

During that identical period, bankruptcy filings increased from 12,000 in 1945 to 180,000 in 1965, or a slightly lower percentage of 1,400 percent.

Under the Bankruptcy Act, "any person" (with exceptions not relevant here) shall be entitled to the benefits of this act as a voluntary bankrupt "but a wage earner" may not be adjudged as "an involuntary bankrupt."

This provision and others must be read into chapter XIII proceedings.

We add also that we know of no cases where, except on a voluntary basis, future earnings of an individual have been considered by the courts as assets for the future liquidation of current debts.

CHAPTER XIII (WAGE EARNERS)

With the brief background set forth above we turn now to chapter XIII of the Bankruptcy Act.

In its present posture chapter XIII proceedings deal only with—

1. Individuals as distinct from corporate, business associations, partnerships, and so forth;

2. Individuals who, on a voluntary basis, desire to enter into an arrangement or composition of their debts.

3. Individuals who are willing to pay their debts in accordance with the arrangement or composition but are also willing to pay all—

- (a) Court costs,
- (b) their attorney fees, and
- (c) the trustee fees;

4. Individuals who are willing to turn over their property and the control of future earning capacity to the court to accomplish the arrangement or composition.

The essential elements of a successful chapter XIII proceeding are—

1. A debtor with a job who desires to pay all or part of his debts and who will budget his living expenses to apply a part of his future earnings to the payment of past due claims;

2. Creditors who are willing to extend the time for payment of, or reduce the amount of, their claims—or both—to help rehabilitate the debtor;

3. The power in the courts to protect the debtor from the claims of creditors to permit payments to a trustee for pro rata distribution among creditors and to allow the debtor to use such of his property as is necessary to carry out his budgeted program and retain his job; and

4. Someone familiar with chapter XIII proceedings to advise and help the debtor prepare a plan acceptable to creditors and with resourcefulness enough to help him with his problems during the time the plan is in effect.

Before an appropriate plan under chapter XIII can be devised, the debtor must be willing to budget his earnings and discipline himself by reducing his standard of living. Thus—

1. If the debtor's budget discloses that he is living above his means, the standard of living must be reduced in order to permit essential funds for payment of obligations already incurred;

2. If the debtor's budget shows an excess over his current living expenses, this excess can be paid into the plan for the satisfaction of existing obligations to creditors; and

3. If the debtor's living expenses cannot be reduced and if the excess over and above current living expenses is so small that the creditors cannot be paid off within a reasonable time, then a straight bankruptcy proceeding is required if he is to be allowed a fresh start.

A few of the many problems which exist in the administration of chapter XIII cases may be summarized as follows:

1. Debtors do not always know the full extent of their indebtedness and often do not know the exact name of the creditor.

2. Common creditors are usually anxious to approve a plan because the financial picture of the debtor indicates clearly that it is the only way they can recover all or a portion of their claim.

3. Secured creditors often have an unrealistic view of the value of their security—and quite often the security is taken with a view that without it the debtor will not have a table to eat on, a bed to sleep on, or transportation to and from work.

4. Debtors often move without notice, change jobs, or have to amend the plan because of unforeseen circumstances, that is, sickness, discharge, accident, et cetera.

5. Employers will often refuse or are unable to cooperate with deductions of wages to assist in the plan.

The Federal Government is an example of this, gentlemen.

6. Debtors were required to pay secured claims in full when the security is nominal and for other reasons may terminate the plan when the secured creditor is paid, leaving the common creditor unpaid.

7. Debtors and creditors often seek to circumvent a plan by incurring additional debts while the plan is in existence.

We turn now to the effect of H.R. 1057.

H.R. 1057 applies to but one category of persons in financial distress—wage earners who by statutory definition are persons whose principal income is derived from wages, salaries, or commissions.

Regardless of the reasons or circumstances which created their financial predicament and regardless also of whether those reasons and circumstances should entitle the particular individual to a fresh start through a discharge of his debts under the Bankruptcy Act, H.R. 1057 has but a single criterion for its application: Does the debtor either have an existing job or is he capable of obtaining gainful employment?

If so, he is denied the right to seek a bankruptcy discharge and his only recourse is to submit some type of an undefined proposal to pay

his debts out of future earnings over an undefined period of time in some undetermined amount.

The problems of completing a wage earner plan when the debtor of his own volition desires to do so are serious enough but if the debtor were compelled against his will to propose a plan, these problems might well become unmanageable.

This practical aspect of administration cannot be better stated than in the testimony of Royal E. Jackson, Chief of the Bankruptcy Division of the Administrative Office of the U.S. Courts, given before the committee at this hearing.

For emphasis I quote a short portion of his views on this aspect:

Referees who have extensive experience with the Wage Earner Plan are aware of the great difficulty encountered with debtors who have an earnest desire to pay all their debts in full and voluntarily file Wage Earner's Plans. Many of them fall by the wayside and for one reason or another fail or are unable to live up to the conditions of the plan for a period of three years or so.

Ordinarily the courts do not consider a Wage Earner's Plan feasible unless the debtor can pay all creditors within a period of about three years.

With this in mind the committee foresaw great difficulty in forcing a debtor to propose a feasible plan and equally as much difficulty in coercing its execution.

Experience shows that in voluntary Chapter XIII cases many debtors change employment, move out of the court's jurisdiction, default in payments under the plan, or incur additional debts despite the court's admonition to the contrary.

These problems would likely be multiplied manyfold in dealing with a recalcitrant debtor.

H.R. 1057, while denying the benefit of the discharge provisions of the Bankruptcy Act to the gainfully employed, leaves those same rights fully available to all nonwage earners, the professional, the farmer, the merchant, the manufacturer, the individual proprietor, and others similarly situated.

All individuals in those categories retain their right to a fresh start when their financial distress occurred through no act of fraud on their own part. We question that this is consistent with the primary intent and purpose of the Bankruptcy Act.

THE PROBLEM OF THE SECURED CREDITOR

No arrangement or composition can be adequately dealt with without consideration of the secured creditor. Two problems exist:

1. Is the security adequate to pay the debt?
2. Is the security necessary to the wage earner in order for him to carry out the terms of the plan?

The first problem has been heretofore referred to. Namely, when the security is inadequate the secured creditor is in effect being paid under chapter XIII for an unsecured debt on a secured basis.

In other words, he receives his payments for the unsecured portion of the secured debt as a preference over other unsecured creditors.

The second problem has also been referred to and is simply that if the furniture and fixtures are necessary for the wage earner and his family to live and a car is necessary for his transportation to and from work, the repossession of such security generally prevents a workable plan.

The enforced use of a composition or extension of debts in a wage earner plan cannot succeed unless in instances mentioned above the

courts can adequately deal with secured creditors and such creditors can be required to participate in any such plan.

The model for such enabling legislation is, of course, reflected in corporate reorganizations as set forth in chapter X of the Bankruptcy Act.

I speak of the Kansas experience:

I have had now some firsthand experience with the workings of chapter XIII in Kansas and I hope I am objective in viewing it as one of the more successful programs in the Nation.

It is clear in our area that one of the principal appeals has been, and is, that the procedure is wholly voluntary and to the financially distressed debtor who chooses thus to pay his debts over an extended period of time rather than to cancel them through straight bankruptcy, it is an accomplishment for which he rightly takes a large measure of personal credit and enhanced self-respect.

This motivation must have been in the mind of the Congress in enacting chapter XIII, for the legislators very carefully drew the distinction between a bankrupt and a debtor under a wage earner plan.

For example, the case is not filed as a bankruptcy but as a chapter XIII proceeding and the individual is never referred to as the bankrupt but only as the debtor under a wage earner arrangement. Should the wage earner proceeding be one not of choice but rather of compulsion, this important distinction would cease to exist.

The stress of this voluntary aspect of the wage earner proceeding in Kansas has resulted in a very fine acceptance of the program by both employers and employees. The consequent financial benefit to creditors even in a State of our relatively small size is extremely impressive. By way of general background I would like it noted that 90 percent of the straight bankruptcy cases throughout the Nation produce no assets whatsoever for unsecured creditors and the remaining 10 percent of the bankruptcies which are in the asset category produce an average dividend to unsecured creditors of only 8 percent.

In fiscal year 1966 in Kansas, our chapter XIII trustees paid out a total of \$1,817,784 to creditors; \$1,046,374 of this was distributed to secured creditors, \$71,870 to priority creditors (usually tax obligations), and \$699,523 to unsecured creditors.

Now, it may be argued that those secured creditors who were paid through chapter XIII proceedings could have recovered their collateral in straight bankruptcy and thus avoided any loss, but the facts are simply to the contrary, and the experience of finance companies with repossessions is uniformly consistent in that the liquidation of the household furnishings, the TV, or the automobile, seldom brings enough to satisfy the debt and often leaves a deficiency.

This fact of economic life seems to be generally realized by the financial community in Kansas for, in the main, secured creditors are strong supporters of the wage earner program with, of course, some notable exceptions.

So I feel that the chapter XIII proceedings should be preserved as a voluntary measure. Its improvement and wider acceptance can be brought about through measures that do not convert it into something of a compulsory nature.

I am advised also by the Administrative Office as an aside from my remarks that chapter XIII, projected chapter XIII filings will in-

crease by almost 4,000 cases over the normal amount for a 14-percent increase in the coming fiscal year.

In summary, we respectfully call this committee's attention to the fact that we are talking about one-tenth of 1 percent of our total population who are involved in employee bankruptcies. It is actually less than that. In addition, the percentage rise in bankruptcies is no greater—in fact slightly less—than the increase in the extension of consumer credit.

Further, voluntary wage earner plans are enjoying a steady increase, are paying off a considerable number of creditors and, because of their voluntary nature, do not penalize an individual who is able and willing to work for the benefit of himself, his family, and society.

Lastly, H.R. 1057 discriminates against the wage earner and makes no provision for dealing adequately with the secured creditor.

Mr. Chairman, thank you for inviting me to appear. If you have any questions I will be glad to answer them to the best of my experience, and within my competence.

Mr. ROGERS. Now, do I understand, Judge, that you have statistics in connection with your statement which show total filings of all types of bankruptcies?

Judge BROWN. Yes.

Mr. ROGERS. We will file those for the record.

Judge BROWN. Yes; they are attached to my statement, copies of which, I think, have been given to your committee. I asked that they be distributed for your convenience, and for reference. There is a considerable amount of meat in what I have said, gentlemen. You may want to look at it.

(The documents referred to follow:)

TOTAL FILINGS OF ALL TYPES OF BANKRUPTCY CASES BY FISCAL YEARS ENDING
JUNE 30 OF EACH YEAR FROM 1900 THROUGH JUNE 30, 1966

1900	21,938	1923	41,304	1946	10,196
1901	19,007	1924	43,519	1947	13,170
1902	18,482	1925	45,641	1948	18,510
1903	16,875	1926	46,374	1949	26,021
1904	17,082	1927	48,758	1950	33,392
1905	16,946	1928	53,064	1951	35,193
1906	12,972	1929	57,280	1952	34,873
1907	14,160	1930	62,845	1953	40,087
1908	17,818	1931	65,335	1954	53,136
1909	18,018	1932	70,049	1955	59,404
1910	18,053	1933	62,256	1956	62,086
1911	19,338	1934	58,888	1957	73,761
1912	19,745	1935	69,153	1958	91,668
1913	20,930	1936	60,624	1959	100,672
1914	22,959	1937	57,485	1960	110,034
1915	27,632	1938	57,306	1961	146,643
1916	27,368	1939	50,997	1962	147,780
1917	24,838	1940	52,577	1963	155,493
1918	20,385	1941	56,332	1964	171,719
1919	14,048	1942	52,109	1965	180,323
1920	13,558	1943	34,711	1966	192,354
1921	22,812	1944	19,533		
1922	38,165	1945	12,862		

CASE FILINGS, FISCAL YEARS 1965 AND 1966

	Fiscal year 1965	Fiscal year 1966	Increase in 1966	Percent of increase
Total.....	180,323	192,354	+12,031	+6.7
X90 District of Columbia.....	96	91	-5	-5.2
Territories.....				
88 districts.....				
1st circuit.....	4,465	4,618	+153	+3.4
100 Maine.....	1,646	1,653	+7	+ .4
101 Massachusetts.....	1,498	1,576	+78	+5.1
102 New Hampshire.....	874	880	+6	+ .7
103 Rhode Island.....	390	457	+67	+17.2
104 Puerto Rico.....	57	52	-5	-8.8
2d circuit.....	8,627	9,239	+612	+7.1
205 Connecticut.....	1,436	1,405	-31	-2.2
206 New York, northern.....	2,180	2,398	+218	+10.0
207 New York, eastern.....	1,246	1,277	+31	+2.5
208 New York, southern.....	1,049	1,025	-24	-2.3
209 New York, western.....	2,384	2,762	+378	+15.9
210 Vermont.....	332	372	+40	+12.1
3d circuit.....	2,715	2,934	+219	+8.0
311 Delaware.....	68	75	+7	+10.3
312 New Jersey.....	1,513	1,675	+162	+10.7
313 Pennsylvania, eastern.....	503	478	-25	-5.0
314 Pennsylvania, middle.....	189	218	+29	+14.8
315 Pennsylvania, western.....	441	487	+46	+10.4
391 Virgin Islands.....	1	1		
4th circuit.....	6,789	7,005	+216	+3.2
416 Maryland.....	261	298	+37	+14.2
417 North Carolina, eastern.....	95	86	-9	-9.5
418 North Carolina, middle.....	123	149	+26	+21.1
419 North Carolina, western.....	69	71	+2	+2.9
420 South Carolina, eastern.....	204	152	-52	-25.5
421 South Carolina, western.....				
422 Virginia, eastern.....	2,723	2,900	+177	+6.5
423 Virginia, western.....	1,841	1,830	-11	-.6
424 West Virginia, northern.....	484	591	+107	+22.1
425 West Virginia, southern.....	989	928	-61	-6.2
5th circuit.....	23,883	23,532	-351	-1.5
526 Alabama, northern.....	6,579	6,321	-258	-3.9
527 Alabama, middle.....	1,641	1,684	+43	+2.6
528 Alabama, southern.....	1,757	1,666	-91	-5.2
529 Florida, northern.....	40	79	+39	+97.5
530 Florida, middle.....	490	621	+131	+26.7
531 Florida, southern.....	428	540	+112	+26.2
532 Georgia, northern.....	4,340	4,281	-59	-1.4
533 Georgia, middle.....	2,167	1,990	-177	-8.1
534 Georgia, southern.....	1,649	1,591	-58	-3.5
535 Louisiana, eastern.....	1,601	1,409	-192	-11.9
536 Louisiana, western.....	1,303	1,377	+74	+5.7
537 Mississippi, northern.....	229	265	+36	+15.7
538 Mississippi, southern.....	738	840	+102	+13.8
539 Texas, northern.....	456	431	-25	-5.5
540 Texas, eastern.....	57	53	-4	-7.0
541 Texas, southern.....	148	138	-10	-6.8
542 Texas, western.....	200	246	+46	+23.0
592 Canal Zone.....				
6th circuit.....	36,504	39,159	+2,655	+7.3
643 Kentucky, eastern.....	1,380	1,623	+243	+17.6
644 Kentucky, western.....	2,713	2,825	+112	+4.1
645 Michigan, eastern.....	4,619	5,214	+595	+12.9
646 Michigan, western.....	1,858	1,910	+52	+2.8
647 Ohio, northern.....	8,669	8,937	+268	+3.1
648 Ohio, southern.....	8,209	8,938	+729	+8.9
649 Tennessee, eastern.....	2,867	3,057	+190	+6.8
650 Tennessee, middle.....	2,024	2,524	+500	+24.7
651 Tennessee, western.....	4,165	4,131	-34	-.8

CASE FILINGS, FISCAL YEARS 1965 AND 1966—Continued

	Fiscal year 1965	Fiscal year 1966	Increase in 1966	Percent of increase
7th circuit.....	23,836	24,606	+770	+3.2
752 Illinois, northern.....	11,384	11,294	-90	-8
753 Illinois, eastern.....	955	968	+13	+1.4
754 Illinois, southern.....	2,202	2,381	+179	+8.1
755 Indiana, northern.....	2,001	2,165	+164	+8.2
756 Indiana, southern.....	3,634	3,904	+270	+7.4
757 Wisconsin, eastern.....	2,600	2,797	+197	+7.5
758 Wisconsin, western.....	1,060	1,097	+37	+3.5
8th circuit.....	11,865	13,060	+1,195	+10.1
860 Arkansas, eastern.....	530	630	+100	+18.8
861 Arkansas, western.....	108	152	+44	+40.7
862 Iowa, northern.....	698	735	+37	+5.3
863 Iowa, southern.....	1,012	990	-22	-2.2
864 Minnesota.....	3,231	3,554	+323	+10.0
865 Missouri, eastern.....	2,857	2,929	+72	+2.4
866 Missouri, western.....	2,016	2,518	+502	+24.9
867 Nebraska.....	989	1,130	+141	+14.3
868 North Dakota.....	216	246	+30	+13.9
869 South Dakota.....	208	176	-32	-15.4
9th circuit.....	48,350	53,744	+5,394	+11.2
970 Alaska.....	104	137	+33	+31.7
971 Arizona.....	3,341	3,563	+222	+6.6
972 California, northern.....	10,579	12,215	+1,636	+15.5
974 California, southern.....	23,077	25,330	+2,253	+9.8
975 Hawaii.....	329	361	+32	+9.7
976 Idaho.....	852	944	+92	+10.8
977 Montana.....	572	612	+40	+7.0
978 Nevada.....	901	1,059	+158	+17.5
979 Oregon.....	4,267	4,754	+487	+11.4
980 Washington, eastern.....	981	1,163	+182	+18.6
981 Washington, western.....	3,341	3,600	+259	+7.8
993 Guam.....	6	6	-----	-----
10th circuit.....	13,193	14,366	+1,173	+8.9
1082 Colorado.....	4,267	4,335	+68	+1.6
1083 Kansas.....	2,903	3,313	+410	+14.1
1084 New Mexico.....	1,069	1,059	-10	-9
1085 Oklahoma, northern.....	1,166	1,389	+223	+19.1
1086 Oklahoma, eastern.....	138	160	+22	+15.9
1087 Oklahoma, western.....	1,688	2,014	+326	+19.3
1088 Utah.....	1,475	1,580	+105	+7.1
1089 Wyoming.....	487	516	+29	+6.0

COMPARATIVE CH. XIII CASE FILINGS IN FISCAL YEARS 1965 AND 1966

	Fiscal year 1965	Fiscal year 1966	Net change	Percent of change
Total.....	28,027	28,261	+234	+0.8
X90 District of Columbia.....	2	6	+4	+200.0
Territories.....	-----	-----	-----	-----
88 districts.....	804	794	-10	-1.2
1st circuit.....	799	765	-34	-4.3
100 Maine.....	4	125	+121	+525.0
101 Massachusetts.....	1	-----	-1	-100.0
102 New Hampshire.....	-----	4	+4	+100.0
103 Rhode Island.....	-----	-----	-----	-----
104 Puerto Rico.....	-----	-----	-----	-----
2d circuit.....	48	56	+8	+16.7
205 Connecticut.....	9	14	+5	+55.6
206 New York, northern.....	6	10	+4	+66.7
207 New York, eastern.....	17	15	-2	-11.8
208 New York, southern.....	4	3	-1	-25.0
209 New York, western.....	11	11	-----	-----
210 Vermont.....	1	13	+12	+1200.0

See footnote at end of table.

COMPARATIVE CH. XIII CASE FILINGS IN FISCAL YEARS 1965 AND 1966—Continued

	Fiscal year 1965	Fiscal year 1966	Net change	Percent of change
3d circuit.....	111	144	+33	+29.7
311 Delaware.....	2	-----	-2	-100.0
312 New Jersey.....	97	122	+25	+25.8
313 Pennsylvania, eastern.....	7	12	+5	+71.4
314 Pennsylvania, middle.....	5	1	-4	-80.0
315 Pennsylvania, western.....	-----	19	+9	+100.0
391 Virgin Islands.....	-----	-----	-----	-----
4th circuit.....	777	1 829	+52	+6.7
416 Maryland.....	3	5	+2	+66.7
417 North Carolina, eastern.....	2	3	+1	+50.0
418 North Carolina, middle.....	8	1 35	+27	+337.5
419 North Carolina, western.....	8	1 20	+12	+150.0
420 South Carolina.....	19	15	-4	-21.1
421.....	-----	-----	-----	-----
422 Virginia, eastern.....	66	63	-3	-4.5
423 Virginia, western.....	605	1 641	+36	+6.0
424 West Virginia, northern.....	2	4	+2	+100.0
425 West Virginia, southern.....	64	43	-21	-32.8
5th circuit.....	10,727	10,322	-405	-3.8
526 Alabama, northern.....	5,181	4,936	-245	-4.7
527 Alabama, middle.....	1,201	1 1,209	+8	+7
528 Alabama, southern.....	1,422	1,293	-129	-9.1
529 Florida, northern.....	1	1	-----	-----
530 Florida, middle.....	1 56	15	-41	-73.2
531 Florida, southern.....	10	17	+7	+70.0
532 Georgia, northern.....	609	1 786	+177	+29.1
533 Georgia, middle.....	1,001	865	-136	-13.6
534 Georgia, southern.....	1 1,140	1,040	-100	-8.8
535 Louisiana, eastern.....	11	6	-5	-45.5
536 Louisiana, western.....	40	1 90	+50	+125.0
537 Mississippi, northern.....	1	-----	-1	-100.0
538 Mississippi, southern.....	34	42	+8	+23.5
539 Texas, northern.....	8	6	-2	-25.0
540 Texas, eastern.....	2	-----	-2	-100.0
541 Texas, southern.....	-----	1	+1	+100.0
542 Texas, western.....	10	15	+5	+50.0
592 Canal Zone.....	-----	-----	-----	-----
6th circuit.....	6,625	1 6,874	+249	+3.8
643 Kentucky, eastern.....	306	1 374	+68	+22.2
644 Kentucky, western.....	554	556	+22	+4
645 Michigan, eastern.....	289	1 392	+103	+35.6
646 Michigan, western.....	40	62	+22	+55.0
647 Ohio, northern.....	361	1 415	+54	+15.0
648 Ohio, southern.....	1 1,002	945	-57	-5.7
649 Tennessee, eastern.....	803	765	-38	-4.7
650 Tennessee, middle.....	263	1 412	+149	+56.7
651 Tennessee, western.....	1 3,007	2,953	-54	-1.8
7th circuit.....	959	1,089	+130	+13.6
752 Illinois, northern.....	220	296	+76	+34.5
753 Illinois, eastern.....	134	1 143	+9	+6.7
754 Illinois, southern.....	164	1 252	+88	+53.7
755 Indiana, northern.....	7	9	+2	+28.6
756 Indiana, southern.....	28	35	+7	+25.0
757 Wisconsin, eastern.....	271	1 284	+13	+4.8
758 Wisconsin, western.....	135	70	-65	-48.1
8th circuit.....	1,342	1,521	+179	+13.3
860 Arkansas, eastern.....	331	1 423	+92	+27.8
861 Arkansas, western.....	17	1 39	+22	+129.4
862 Iowa, northern.....	9	15	+6	+66.7
863 Iowa, southern.....	190	165	-25	-13.2
864 Minnesota.....	549	609	+60	+10.9
865 Missouri, eastern.....	1	3	+2	+200.0
866 Missouri, western.....	188	189	+1	+5
867 Nebraska.....	50	1 71	+21	+42.0
868 North Dakota.....	1	3	+2	+200.0
869 South Dakota.....	6	4	-2	-33.3

See footnote at end of table.

COMPARATIVE CH. XII CASE FILINGS IN FISCAL YEARS 1965 AND 1966—Continued

	Fiscal year 1965	Fiscal year 1966	Net change	Percent of change
9th circuit.....	14,593	4,543	-50	-1.1
970 Alaska.....	2	17	+5	+250.0
971 Arizona.....	167	1177	+10	+6.0
972 California, northern.....	1,476	11,713	+237	+16.1
974 California, southern.....	12,216	1,769	-447	-20.2
975 Hawaii.....	154	52	-2	-3.7
976 Idaho.....	100	1131	+31	+31.0
977 Montana.....	10	5	-5	-50.0
978 Nevada.....	9	23	+14	+155.6
979 Oregon.....	70	110	+40	+57.1
980 Washington, eastern.....	32	192	+60	+187.5
981 Washington, western.....	457	1464	+7	+1.5
993 Guam.....				
10th circuit.....	2,039	12,083	+44	-2.2
1082 Colorado.....	439	1468	+29	+6.6
1083 Kansas.....	1,245	1,321	+76	+6.1
1084 New Mexico.....	1233	167	-66	-28.3
1085 Oklahoma, northern.....	37	38	+1	+2.7
1086 Oklahoma, eastern.....	3		-3	-100.0
1087 Oklahoma, western.....	135	28	-7	-20.0
1088 Utah.....	45	59	+14	+31.1
1089 Wyoming.....	2	2		

High total for any year.

EMPLOYEE FILINGS IN FISCAL YEAR 1966

	Total filings	Employee filings	Ch. XIII filings	Ch. XIII percent of employee filings
Total.....	192,354	160,299	28,261	17.6
X90 District of Columbia.....	91	63	6	9.5
Territories.....				
88 districts.....				
1st circuit.....	4,618	3,640	794	21.8
100 Maine.....	1,653	1,453	765	52.6
101 Massachusetts.....	1,576	1,065	125	2.3
102 New Hampshire.....	800	681		
103 Rhode Island.....	457	436	4	.9
104 Puerto Rico.....	52	5		
2d circuit.....	9,239	6,598	56	.8
205 Connecticut.....	1,405	954	14	1.5
206 New York, northern.....	2,398	1,860	10	.5
207 New York, eastern.....	1,277	641	15	2.3
208 New York, southern.....	1,025	452	3	.7
209 New York, western.....	2,762	2,386	11	.5
210 Vermont.....	372	305	13	1.0
3d circuit.....	2,934	1,407	144	10.2
311 Delaware.....	75	48		
312 New Jersey.....	1,675	793	122	15.4
313 Pennsylvania, eastern.....	478	230	12	5.2
314 Pennsylvania, middle.....	218	123	1	.8
315 Pennsylvania, western.....	487	212	19	4.2
391 Virgin Islands.....	1	1		
4th circuit.....	7,005	5,963	1829	13.9
416 Maryland.....	298	195	5	2.6
417 North Carolina, eastern.....	86	46	3	6.5
418 North Carolina, middle.....	149	95	135	36.8
419 North Carolina, western.....	71	43	120	46.5
420 South Carolina, eastern.....	152	115	15	13.0
421 South Carolina, western.....				
422 Virginia, eastern.....	2,900	2,503	63	2.5
423 Virginia, western.....	1,830	1,645	1641	39.0
424 West Virginia, northern.....	591	504	4	.8
425 West Virginia, southern.....	928	817	43	5.3

See footnote at end of table.

EMPLOYEE FILINGS IN FISCAL YEAR 1966—Continued

	Total filings	Employee filings	Ch. XIII filings	Ch. XIII percent of employee filings
5th circuit.....	23,532	20,811	10,322	49.
526 Alabama, northern.....	6,321	6,023	4,936	82.0
527 Alabama, middle.....	1,684	1,599	1,209	75.6
528 Alabama, southern.....	1,666	1,603	1,293	80.7
529 Florida, northern.....	79	60	1	1.7
530 Florida, middle.....	621	381	15	3.9
531 Florida, southern.....	540	255	17	6.6
532 Georgia, northern.....	4,281	3,921	1,786	20.0
533 Georgia, middle.....	1,990	1,868	865	46.3
534 Georgia, southern.....	1,591	1,505	1,040	69.1
535 Louisiana, eastern.....	1,409	1,205	6	.5
536 Louisiana, western.....	1,377	1,056	190	8.5
537 Mississippi, northern.....	265	223		
538 Mississippi, southern.....	840	735	42	5.7
539 Texas, northern.....	431	154	6	3.9
540 Texas, eastern.....	53	9		
541 Texas, southern.....	138	40	1	2.5
542 Texas, western.....	246	174	15	8.6
592 Canal Zone.....				
6th circuit.....	39,159	35,642	6,874	27.7
643 Kentucky, eastern.....	1,623	1,465	1,374	25.5
644 Kentucky, western.....	2,825	2,587	556	21.5
645 Michigan, eastern.....	5,214	4,781	1,392	8.2
646 Michigan, western.....	1,910	1,736	62	3.6
647 Ohio, northern.....	8,937	7,739	1,415	5.4
648 Ohio, southern.....	8,938	8,136	945	11.6
649 Tennessee, eastern.....	3,057	2,851	765	26.8
650 Tennessee, middle.....	2,524	2,289	1,412	18.0
651 Tennessee, western.....	4,131	4,058	2,953	72.8
7th circuit.....	24,606	21,744	1,809	5.0
752 Illinois, northern.....	11,294	10,009	296	3.0
753 Illinois, eastern.....	968	804	1,143	17.8
754 Illinois, southern.....	2,381	2,098	1,252	12.0
755 Indiana, northern.....	2,165	2,016	9	.4
756 Indiana, southern.....	3,904	3,671	35	.9
757 Wisconsin, eastern.....	2,797	2,289	1,284	12.4
758 Wisconsin, western.....	1,097	857	70	8.2
8th circuit.....	13,060	10,904	1,521	13.9
860 Arkansas, eastern.....	630	566	1,423	74.7
861 Arkansas, western.....	152	102	139	38.2
862 Iowa, northern.....	735	600	15	2.5
863 Iowa, southern.....	990	790	165	20.9
864 Minnesota.....	3,554	2,915	609	20.9
865 Missouri, eastern.....	2,929	2,570	3	.1
866 Missouri, western.....	2,518	2,153	189	8.8
867 Nebraska.....	1,130	873	71	8.1
868 North Dakota.....	246	207	3	1.4
869 South Dakota.....	176	128	4	3.1
9th circuit.....	53,744	41,662	4,543	10.9
970 Alaska.....	137	111	17	6.3
971 Arizona.....	3,563	2,471	1,177	7.1
972 California, northern.....	12,215	10,454	1,713	14.0
974 California, southern.....	25,330	18,532	1,769	7.0
975 Hawaii.....	361	295	52	17.6
976 Idaho.....	944	814	1,131	16.1
977 Montana.....	612	511	5	.9
978 Nevada.....	1,059	886	23	2.6
979 Oregon.....	4,754	3,514	110	3.1
980 Washington, eastern.....	1,163	1,034	192	8.9
981 Washington, western.....	3,600	3,037	1,464	15.3
993 Guam.....	6	3		
10th circuit.....	14,366	11,865	12,083	17.6
1082 Colorado.....	4,335	3,276	1,468	14.3
1083 Kansas.....	3,313	3,082	1,321	39.9
1084 New Mexico.....	1,059	890	167	18.8
1085 Oklahoma, northern.....	1,389	1,242	38	3.1
1086 Oklahoma, eastern.....	160	122		
1087 Oklahoma, western.....	2,014	1,700	28	1.6
1088 Utah.....	1,580	1,208	59	4.9
1089 Wyoming.....	516	345	2	.6

¹ High total for any year.

BANKRUPTCY FILINGS BY CLASS

Fiscal year	Ch. XIII	Employee	Nonbusiness	Business	Total bankruptcy case filings
1939-----	¹ 1,639				150,997
1940-----	3,260	36,843	39,073	13,248	52,577
1941-----	4,433	42,348	44,713	11,619	56,335
1942-----	4,100	40,180	42,251	9,858	52,109
1943-----	2,007	27,020	28,782	5,929	34,711
1944-----	1,249	15,460	16,752	2,781	19,533
1945-----	1,248	10,010	11,051	1,811	12,862
1946-----	1,371	7,618	8,566	1,630	10,196
1947-----	2,354	9,396	10,234	2,938	13,170
1948-----	3,315	12,546	13,537	4,973	18,510
1949-----	5,111	17,772	19,144	6,877	26,021
1950-----	6,007	22,933	25,040	8,352	33,392
1951-----	6,924	25,984	27,806	7,387	35,193
1952-----	7,397	26,527	28,331	6,542	34,873
1953-----	8,670	31,253	33,315	6,772	40,087
1954-----	9,634	40,889	44,248	8,888	53,136
1955-----	9,864	46,163	50,219	9,185	59,404
1956-----	9,535	48,784	52,608	9,478	62,086
1957-----	11,549	59,053	63,617	10,144	73,761
1958-----	13,391	73,379	80,265	11,403	91,668
1959-----	12,993	81,516	88,943	11,729	100,672
1960-----	13,599	89,639	97,750	12,284	110,034
1961-----	19,723	119,117	131,402	15,241	146,643
1962-----	22,880	120,742	132,125	15,655	147,780
1963-----	24,329	127,156	139,190	16,303	155,493
1964-----	27,292	141,550	155,209	16,510	171,719
1965-----	28,027	148,965	163,413	16,910	180,323
1966-----	28,261	160,299	175,924	16,430	192,354

¹ Figures obtained from report of Attorney General.

*Bankruptcy cases filed by fiscal years and by quarters,
1940 through June 30, 1946*

<i>Fiscal years and quarters</i>	<i>Cases commenced</i>	<i>Fiscal years and quarters</i>	<i>Cases commenced</i>
1940-----	52,577	1944:	
1941:		First-----	5,919
First-----	13,682	Second-----	5,001
Second-----	13,219	Third-----	4,427
Third-----	15,439	Fourth-----	4,186
Fourth-----	13,992	Total-----	19,533
Total-----	56,332		
1942:		1945:	
First-----	13,576	First-----	3,524
Second-----	12,883	Second-----	3,205
Third-----	12,667	Third-----	3,123
Fourth-----	12,983	Fourth-----	3,010
Total-----	52,109	Total-----	12,862
1943:		1946:	
First-----	11,208	First-----	2,451
Second-----	8,552	Second-----	2,507
Third-----	7,710	Third-----	2,629
Fourth-----	7,241	Fourth-----	2,609
Total-----	34,711	Total-----	10,196

*Bankruptcy cases filed by fiscal years and by quarters,
1947 through June 30, 1952*

<i>Fiscal years and quarters</i>	<i>Cases commenced</i>	<i>Fiscal years and quarters</i>	<i>Cases commenced</i>
1947:		1950:	
First -----	2,577	First -----	8,056
Second -----	2,844	Second -----	7,355
Third -----	3,712	Third -----	8,826
Fourth -----	4,037	Fourth -----	9,155
Total -----	13,170	Total -----	33,392
1948:		1951:	
First -----	3,949	First -----	8,605
Second -----	4,031	Second -----	8,293
Third -----	5,055	Third -----	9,184
Fourth -----	5,475	Fourth -----	9,111
Total -----	18,510	Total -----	35,193
1949:		1952:	
First -----	5,649	First -----	8,141
Second -----	5,670	Second -----	8,081
Third -----	7,065	Third -----	9,456
Fourth -----	7,637	Fourth -----	9,195
Total -----	26,021	Total -----	34,873

*Bankruptcy cases filed by fiscal years and by quarters,
1953 through June 30, 1957*

<i>Fiscal years and quarters</i>	<i>Cases commenced</i>	<i>Fiscal years and quarters</i>	<i>Cases commenced</i>
1953:		1956:	
First -----	8,656	First -----	14,313
Second -----	9,186	Second -----	13,995
Third -----	10,834	Third -----	16,781
Fourth -----	11,411	Fourth -----	16,997
Total -----	40,084	Total -----	62,086
1954:		1957:	
First -----	11,349	First -----	16,160
Second -----	11,880	Second -----	17,354
Third -----	14,933	Third -----	19,966
Fourth -----	14,974	Fourth -----	20,281
Total -----	53,136	Total -----	73,761
1955:			
First -----	14,444		
Second -----	13,804		
Third -----	15,439		
Fourth -----	15,717		
Total -----	59,404		

*Bankruptcy cases filed by fiscal years and by quarters, 1958 through
June 30, 1963*

<i>Fiscal years and quarters</i>	<i>Cases commenced</i>	<i>Fiscal years and quarters</i>	<i>Cases commenced</i>
1958:		1961:	
First -----	20, 264	First -----	32, 766
Second -----	20, 351	Second -----	33, 318
Third -----	25, 218	Third -----	40, 085
Fourth -----	25, 835	Fourth -----	40, 474
Total -----	91, 668	Total -----	146, 643
1959:		1962:	
First -----	24, 408	First -----	37, 441
Second -----	23, 336	Second -----	35, 316
Third -----	26, 273	Third -----	37, 794
Fourth -----	26, 655	Fourth -----	37, 229
Total -----	100, 672	Total -----	147, 780
1960:		1963:	
First -----	24, 225	First -----	35, 911
Second -----	24, 171	Second -----	35, 705
Third -----	29, 797	Third -----	40, 874
Fourth -----	31, 841	Fourth -----	43, 008
Total -----	110, 034	Total -----	155, 493

*Bankruptcy cases filed by fiscal years and by quarters, 1964 through
June 30, 1966*

<i>Fiscal years and quarters</i>	<i>Cases commenced</i>	<i>Fiscal years and quarters</i>	<i>Cases commenced</i>
1964:		1966:	
First -----	41, 632	First -----	46, 678
Second -----	40, 239	Second -----	44, 918
Third -----	45, 457	Third -----	49, 919
Fourth -----	44, 391	Fourth -----	50, 839
Total -----	171, 719	Total -----	192, 354
1965:			
First -----	42, 816		
Second -----	41, 861		
Third -----	47, 250		
Fourth -----	48, 396		
Total -----	180, 323		

Mr. ROGERS. First, judge, I want to express my appreciation to you in taking time away from your business and coming to Washington, and participating in the Judicial Conference, as it relates to bankruptcy matters. No doubt your experience as a referee and as a judge gives you insight into this problem that we are trying to explore today. I assure you that we asked for your recommendations. We do not feel that you are trying to influence congressional action in this area.

I note that one of the problems that you point out on page 3 of your statement concerns the status of the special fund in the Treasury, out of which all salaries are paid, and this fund is maintained from the filing fees, and so forth.

Do you feel that if a compulsory chapter XIII is required of wage

earners, that there would be added costs in connection with the administration of these bankruptcy filings?

Judge BROWN. It is very speculative, Mr. Chairman. In the first place it may reduce the number of employee bankruptcy that would be filed. And this, I think, is one of the things that is probably desired by the proponents of the bill, quite frankly.

It might do that; however, the Treasury fund at the last look was in very good shape, I might add. I think we had some \$9 million surplus, and I don't know whether—I just can't project. It is hard to do, with so many various aspects of our economy.

It is almost like determining the weather. In the first place, you stop to think that our population is increasing and all sorts of matters involving the financial aspects of the credit community exist.

If our wartime enterprises are either increased or decreased, this has an effect on our economy. You can see what all-out conflict does to bankruptcy, if you look at the figures. They went down in 1950, with the Korean affair. They apparently have not gone down so much now.

During World War II, they were down very much. I think my old friend who was a referee there when I became one, Judge Sloan, who was a former member of our supreme court of the State, I think when he started in the forties, he had 48 bankruptcies in Kansas.

We have about 5,000.

Mr. ROGERS. Well, in other words, what you are saying is that as the economy may rise or fall, the bankruptcies fluctuate accordingly. And as you pointed out, in the last 20 or 25 years, with the rise in consumer credit, there has been a steady increase in the number of bankruptcy filings, but not in any greater proportion than that by which the economy itself has expanded.

Judge BROWN. That is the indicated statistical figure, and I don't try to take it into the increase in population, nor the increase in how our population moves around. There are many factors but this was just an interesting one.

Mr. ROGERS. Well, now, of course, there has been some discussion as to expanding the coverage of H.R. 1057 beyond wage earners to include everyone except a corporate bankrupt.

Have you given any thought to that, in the studies by the Judicial Conference, as to whether or not it should be expanded to include others than wage earners?

Judge BROWN. Well, I can only tell you, to say that I have not given any thought to this. When having copies of this made up by the Administrative Office, they mentioned the fact that this question had been asked by the committee yesterday when I was not here.

I would point out to the committee that under the present act, we have what is known as a chapter X, XI, XII, and XIII. Chapter XI deals primarily with the noncorporate reorganization of individual businesses. Chapter X, of course, is the corporate reorganization and it is a very effective means if you have the need for it or the desire.

The typical example of its usefulness originated and probably the highest example is the Missouri Pacific Railroad, which after so many years, paid out in full, under a proper chapter X.

The other is that in real estate problems, you have the chapter XII, and then you have the chapter XIII. Now, to extend this really, who are we talking about? I am not quite sure. If we are talking about the

person who has income, the professional man, he has income from his work, I would say I would be interested in seeing someone tell some doctor or lawyer or someone else that he had to work for 3 years or longer in the future by donating so much of his fees or business to a plan before he could be given a chance of a fresh start by virtue of a real problem.

We had a dentist, if you want an example, gentlemen, who decided—in Kansas, and a very capable one—who got involved in some business dealings beyond his competence. He had signed a bunch of notes for people. Well, he had nothing to do. Every time somebody walked into his office, that owed him a little money, he either had to go on a cash basis, or they were going to get garnisheed for the money he owed them, and besides that, he had debts, just on comparative basis, for a young man, astronomical.

I remember the case very well. I was a referee at the time, and it was a problem.

Now, I have not given it the kind of thinking as to its effect, but I do make this observation, with which you are all more familiar than I. Whenever you try to force the people to do something, particularly the American people, you may lead them to water, but you can't make them drink.

Mr. ROGERS. Well, now, that leads to the next question, about secured creditors. As you point out on page 7 of your statement—

Judge BROWN. Yes, sir.

Mr. ROGERS (continuing). A secured creditor is not required to accept the plan. In chapter XIII actions—in the cases which you have had experience, have you encountered much resistance from secured creditors? When a plan is submitted do they have to take their proportionate share, or is the plan usually submitted to give them a preference?

Judge BROWN. Well, the plan always gives the secured creditor a preference. As I recall the act, it requires some preference for the secured creditor, and the preferred creditor, in the sense that the secured creditor with his security has either the right to realize on his security, by an action to recover it; the problem only comes up, generally speaking, when the secured creditor has inadequate security, and we are talking just the same way about these secured creditors that we talk about others.

Now, I don't want anything I say to be interpreted that I have any feeling against people who loan money. I do not. And I have no feeling in opposition to security.

They are in business, the same as anyone else. They sell money. That is the only difference.

Now, the problem comes, as I started to say, where someone makes a loan on a TV set, which he has bought for \$350, and the day he takes it out of the place, it has got about a hundred dollar value on it, if he wants to resell it. Or he gets an automobile, or he gets household furniture, and if the security is based on this, and the secured creditor demands that he have his security back, he really does not want it back, lots of times.

What he wants is to get paid—for which none of us have any criticism of him; it is just the fact of life that if you are going to have a plan that is successful, he is not entitled to be paid for more than the security which he has.

In other words, a thousand dollar loan on household furniture worth \$200, he should be an unsecured creditor for \$800, and a secured creditor for \$200 and get paid off the top for the \$200, not the thousand dollars.

Mr. ROGERS. Well, don't these problems involve the question of what the percentage of recovery shall be which becomes the duty and responsibility either of the referee or the judge to make?

Judge BROWN. Well, after a hearing, usually, when a plan comes in, your trustee presents it to the referee, at least in our operations in Kansas.

He presents the problem to the referee. If the security—it is merely a question of how much priority the secured creditor gets in the payments. In Kansas, we have a decision whereby, generally speaking, secured creditors—it is called the *Odell* decision, and it has some problems about it, but under the *Odell* decision, secured creditors are paid for the value of the amount of the security, not the value of their security.

Do you understand my distinction?

Mr. ROGERS. Yes.

Judge BROWN. And this is the problem. In a chapter X proceeding, for instance, if the security is not there, the courts may go in and delay the payments that are not quite in accordance with the terms of the original contract, they extend them over a longer period of time, and things of that kind.

The problems of a plan for the individual are astronomical, gentlemen. You just take a referee who sits there and has a plan, and he has two men who make \$6,000 a year. One of them has seven children, and one of them has one.

Mr. ROGERS. And the referee would have to make these momentous decisions, as they relate to almost every petition that is filed?

Judge BROWN. Well, that is right.

Mr. ROGERS. And it would add a greater burden to his responsibility and, of course, additional costs.

Judge BROWN. It would do that, sir, and in addition, of course, he does not have the benefit of the incentive of the man who wants to do it on a voluntary basis.

I have a letter in my file which I brought with me, which the referee handed me, one of my referees handed me before I came up here. It is from a wage earner, and it is supposed to be unsolicited.

If you would like to see it I will be glad to leave it with the committee.

Mr. ROGERS. We will be pleased to receive it for consideration for inclusion in the record, Judge.

Judge BROWN. All right.

Mr. ROGERS. Now, do you have any ideas of whether or not we should compel secured creditors to accept certain wage earner plans that may be submitted?

Judge BROWN. Well, we run into many problems in this regard, and I think that there should be the authority in a plan, in any plan of this kind, to deal with secured creditors and I am not quite as precise as I would like to be, because I have only gone through this, I went through this about 3 years ago.

I mentioned that the model is a chapter X reorganization program, based on the individual problem, and many of the provisions can, with slight amendment, be put into the chapter XIII proceedings.

I would say they should be, and I think that they would benefit by it really tremendously, really. In other words, secured creditors are as diverse as the individual debtor. You have all kinds of secured creditors. You have creditors, secured creditors, who are more than sympathetic to the borrower, and who make it a policy to be.

But they still are in business, and most of them have as a part of their charter one famous line; "This corporation is organized for profit," and this is the way it should be.

Mr. ROGERS. Thank you, Judge. Mr. Whitener?

Mr. Jacobs?

Mr. JACOBS. Judge, first I would like to thank you for both your scholarly formal presentation and willingness to make sacrifices to come here. There is one point in your statement which interests me a great deal.

Let me preface my reference to it and questions about it with a quotation from a witness who appeared, I believe, on yesterday before this subcommittee, representing the American Bankers Association, a Mr. Curtis Kendall, and I shall quote from his statement.

He says—

The facts are that of the total personal bankruptcy filed in my state for the fiscal year ending June 30, 1966, 79 percent were chapter XIII petitions while for the entire fifty states, only 16 percent of personal petitions were filed under chapter XIII.

And then if I may refer on page 26 of your formal statement to a sentence in which you said, referring to chapter XIII proceedings—

Its improvement and wider acceptance can be brought about through measures that do not convert it into something of a compulsory nature.

I am very interested in measures that might be adopted. My colleague Mr. Whitener asked Mr. Kendall how he accounted for the disproportion to the national average share of chapter XIII petitions in his area there in Alabama. I did not entirely understand how he accounted for it, and I just wondered if you could elaborate as to how we might improve the voluntary feature and the desirability of that feature to more debtors.

Judge BROWN. Well, of course, if you are talking about Judge Seybourne H. Lynne's territory in Alabama, in the northern part of it, I think it is—is that right? And Judge Clarence Allgood who was a referee also before he became a Federal judge, you are talking about the oldest area in the United States where, even before they had wage earner plans, they utilized the Bankruptcy Act to accomplish this under the equitable powers of the court—very successfully.

And it still has the biggest chapter XIII wage earner plan volume. Most of it has to be by education. First there has to be a certain acceptance by the credit community.

Second, there has to be a knowledge that the plan is available. The Judicial Conference of the United States has recommended this, and our referees have advocated it. I did, as a referee, and the trustees that are appointed speak to credit bureaus and speak to employee associations. This development has its effect, because it gives the people a

certain pride in the accomplishment of it, but it takes some knowledge and some facility.

It is covered a little bit in my reference in my statement, in the fact that someone who is acquainted with chapter XIII, when a man comes into him who is oppressed by his debts and needs a fresh start, and looks at it and he gets a budgetary requirement, we have forms that are used.

I wrote a little primer, gentlemen, a number of years ago, and it was printed which has the forms, the problem. I did it as a referee, and I did it, I think, in conjunction when I was on a committee, one of Mr. Twinem's committees, of the American Bar Association, for the purpose of trying to get a uniform procedure for chapter XIII.

Under the present way, of course, it becomes a voluntary basis, but where it is successful, and where it gets started, if it is not stopped, it was stopped a little while in some of the circuits until the Supreme Court, in the *Perry* case, outlined the fact that the 6-year limitation on taking bankruptcy, straight bankruptcy was not applicable to an extension case.

This happened, and in our circuit, we have not had this problem. They had it with a referee, once, and I was the referee, but they changed my views.

(The decision referred to, *Perry v. Commerce Loan Company*, is set out at pages 138-155.)

Mr. JACOBS. In your opinion, Judge, is there anything that this subcommittee might recommend to Congress by way of legislation that would improve the knowledge of people in this country generally about the advantages of chapter XIII proceedings?

Is there anything you can think of that we could do to change the laws and facilitate this educational effort?

Judge BROWN. The field of proposed legislation in the capacity I appear today, I would hope that you would not ask me to enter into that field. I don't think in my judicial capacity I have, or as a member of this committee I should make an individual recommendation to you, although I might say I have done it inadvertently with reference to the chapter X proceeding, but I don't feel that at this time a general statement, without precise implementing thoughts, would be of any great service to this committee.

I will do anything for you, gentlemen, when—within my competence. However, I have a position in which I feel it inappropriate for me to make recommendations of this kind. I would hope that if you have some recommendations, as always, our Committee and at the request of your Judiciary Committee, if you submit it to us, we will certainly give it every consideration.

This is in the nature of doing the very thing that I want to be sure I do not interfere with. I have great respect for our system, and I hardly think it advisable for me to make recommendations with respect to laws which I may have to interpret.

Mr. JACOBS. Thank you very much for your help.

Judge BROWN. I hope you understand.

Mr. JACOBS. I understand your position.

Mr. ROGERS. Mr. Poff?

Mr. POFF. Mr. Chairman, thank you. I assure the witness that I understand, and I respect and admire the position he has taken. I think it is entirely appropriate. I think it is appropriate, too, that the judiciary should advise and consult with the legislative branch.

You were good enough that you did not intend to trespass but I do not regard it as a trespass. I regard it as an offer of help, and welcome it as such.

We are all acting toward the same end, and whatever knowledge and expertise may be brought to bear upon this subject serves our mutual purpose.

Some of the questions I had expected to ask the distinguished witness have already been preempted yet as I understand the thrust of your testimony, the major criticism in the first instance, at least, is that having selected the wage earner, a person in the lower wage bracket, we have committed some act of discrimination.

Now my question is, if this is a fact—and parenthetically I say that no discrimination was intended by the author of the bill—I ask the question, would that discrimination be limited if the amendment to which you addressed yourself a moment ago is adopted? That is the amendment to expand the reach of the legislation to all but commercial corporations?

Judge BROWN. Well, to answer your question, I tried to make it clear that in our analysis of the bill, in the first instance, the committee analysis of the bill, we had to do it with an historical reference, and the purpose which this body has indicated, when the Chandler Act was adopted.

And I made that in my remarks. If you are going to amend the policy of Congress with respect to the right of the individual to a fresh start under a straight bankruptcy, with due regard, I think that it should not be done by one piece of enabling legislation in one portion of the Bankruptcy Act, but it should require an appropriate study by this body of its ultimate effect on the entire bankruptcy picture. And in this regard, there is a question as to whether or not if we made the bankruptcy act unavailable to anyone, I make it broad in the sense so that it would not be limited to just the wage earner.

The very first principle of the Bankruptcy Act, to give a man a fresh start, would be avoided.

Mr. PORR. In all those cases where the petitioner was unable to show that he would be unable, without hardship to his family over a period of time, to discharge the debts he has accumulated?

Judge BROWN. Yes, there are instances which arise, but what you are saying is, in those instances in which a man can be required to mortgage his future, if I may use the term, his future earnings, his future capacity, to pay debts which have been now incurred and are not being paid.

Not that he does not do this by contract in our economy today, all the time. Anyone recognizes that. But this is a matter of contract of the individual. And what you are saying, to do it on an involuntary nature, I only want to point out the pitfalls.

There are millions of people in this country who would not be involved in bankruptcy situations at all if they could possibly help it, and will go to any extent not to be.

And there are quite a number, presently, I think around probably 32,000, out of the 160,000 employees, or thereabouts, who voluntarily want to pay their debts, and want by the assistance of the court to make payments; and they are willing to pay 120 percent, approx-

imately, of their created obligations, from future earnings, in order to pay them.

That is over a 3-year period. They can borrow money and pay them on those type of loans, slightly higher. A slightly higher percent in interest rates. There are all these problems. I don't—I just think that if I may enter this generality, I would hope that the committee would review the historical purpose of the Bankruptcy Act before amending it by one provision of this kind that has to be read in connection with all other provisions of the act.

The Bankruptcy Act as it presently exists, gentlemen, is a sophisticated legal document, but I think it serves a very good purpose. And I think it serves the credit community with a very good purpose. But we have always had trouble legislating morality in this country.

Mr. POFF. Well, one of the purposes—

Judge BROWN. I hope I have answered your question.

Mr. POFF. Well, I must say not entirely, and yet I realize it is difficult to give an answer. I might structure it differently. If the bill is amended in this particular, would it make it less objectionable to you?

Judge BROWN. Who are we talking about, again?

Mr. POFF. We are talking about expanding its coverage to all those except commercial corporations.

Judge BROWN. The farmer, the professional man, the person who lives off of the income from stocks or bonds, the person who—

Mr. POFF. Any person who is entitled to the benefits of the Bankruptcy Act.

Judge BROWN. Well, and require, change the act to require the provisions that are now effected, here you would have to change the provisions that they could not be made involuntarily bankrupt, and they could not have the advantages of the act, unless there was a determination that they could not pay their bills.

Mr. POFF. As your testimony indicates, that would necessarily be incorporated in the amendment that might achieve the purpose I stated.

Judge BROWN. If this is the desire of the committee, I have nothing to say about it. I think if this is your desire, I think this is a matter of congressional policy.

Mr. POFF. Yes, and the bill itself is a matter of congressional policy.

Judge BROWN. Well, but you asked us to—

Mr. POFF. My question was, Would it make it less objectionable to you?

Judge BROWN. If you want a personal statement, and not the committee's statement, again you are asking me for my view.

Mr. POFF. Yes, sir.

Judge BROWN. I agree with the original policy enunciated by Congress when it adopted the Chandler Act. I think it is a good policy, and I think it is effective. Anything which deters from that policy, without a careful work, I think that unless there is this careful study, it is inappropriate, because it leads to problems in the judicial administration of the Bankruptcy Act.

Mr. POFF. Well, Judge, let's leave that phase of it, and pass to another. I see I am not going to get an answer.

Judge BROWN. Mr. Poff, you are not going to get me to try to change your congressional policy.

Mr. POFF. Judge, how would it affect your personal attitude—and I realize you cannot speak for the committee on all these questions, since you could not possibly have anticipated them, I am sure—what would be your personal attitude about the advisability of including commercial corporations as well as natural persons?

Judge BROWN. Well, of course, commercial corporations are included in the sense that chapter X provides that and chapter X gives this. In other words, under chapter X, in a corporate reorganization, the creditors may come in and ask for a reorganization, and there is no magic about this.

All it needs is management, money, and a product. And if you have got those three, and why then, there is a possibility of a corporate reorganization.

Mr. POFF. In other words, what you are saying, as I understand it, is that it would be irrelevant to amend the bill to include corporations specifically, inasmuch as they are already covered substantially under chapter X.

Judge BROWN. Chapter X and chapter XI.

Mr. POFF. And chapter XI?

Judge BROWN. And chapters XI and XII if it is real estate. Both, of course, are voluntary under the act.

Mr. POFF. Yes. As a predicate to a question I would like to ask now, let me read, if I may, from title 11, subchapter 8, section 1046, of the United States Code.

Judge BROWN. I will get my copy. What is the section you are reading from?

Mr. POFF. Do you have the Bankruptcy Act, or the code?

Judge BROWN. I have the Bankruptcy Act.

Mr. POFF. Well, I do not have the act before me.

Judge BROWN. Just give me the code number, and I will find it.

Mr. POFF. Yes, section 1046 of title 11, that is subchapter 8. That is section 646 of the Act.

Judge BROWN. Yes, I have it.

Mr. POFF. That section reads in part:

A plan under this chapter (1) shall include provisions dealing with unsecured debts generally, upon any terms; (2) may include provisions dealing with secured debts severally, upon any terms; (3) may provide for priority of payment during the period of extension as between the secured and unsecured debts affected by the plan.

Do you feel that this language gives a court sufficient flexibility and discretion in the event secured creditors are participating in the chapter XIII plan?

Judge BROWN. If they can be required, yes. I mean, it is a very general provisions, and if they accept the plan. But, of course, you have to have creditor acceptance in any of these plans.

Mr. POFF. Yes, you have to have the majority of creditors in number and amount.

Judge BROWN. I think that is right.

Mr. POFF. Now when you speak of requiring the secured creditor to submit to the plan, do you mean by that recommendation to recommend the repeal of the present requirement that a majority of number and amount creditors must consent to the plan?

Judge BROWN. If you are going to require the debtor to come up with a plan, then there must be some power in the court to require acceptance of the plan.

Mr. POFF. That is not true of the chapter XIII as it is now written, of course?

Judge BROWN. No, but it is under chapter X. In other words, the court there approves the plan submitted, and finds whether or not it is fair and feasible, as I recall.

You are asking me now a legal question, and I am talking off the top of my head, only as an accommodation to you, sir.

Mr. POFF. Yes, sir. We all have the right to revise and extend our remarks.

Judge BROWN. Well, I don't want to be in a position where I have to take the time to revise and extend my remarks.

Mr. POFF. I like to avoid that little duty, too, but sometimes I find it necessary.

Judge BROWN. I was invited here for your help, and I will gladly submit to your questions, but you must let me hedge them when I feel that they are not adequate, when I am not giving you an adequately researched, precise, answer.

Mr. POFF. Well, now in the case of a judge of the District court, I concur that it is proper to refer to that as hedging. I have noticed, however, when the same conduct is described vis-a-vis politicians, it is called something else; namely, fence straddling.

I am prepared to extend that appellation, too.

Judge BROWN. Well, I am entirely at your mercy, and whatever you call it I will not be critical of it.

Mr. POFF. Fine. Very good. I have really only one further question, and it is just a technical supplement to a statement that you made on page 27. Your statement is that voluntary wage earner plans are enjoying a steady increase, and the statistics supplied to the committee bear out that fact.

It is not also a fact, however, that as a percentage of total employee filings, there is a steady decrease?

Judge BROWN. Oh, no. I think employee filings, have increased. I thought you said decreased.

Mr. POFF. No; I say as a percentage of total filings, is not there a decrease over the years?

Judge BROWN. You mean of chapter XIII over the number?

Mr. POFF. Yes, sir. I am afraid I did not express it very well.

Judge BROWN. I would request that you get that information from the administrative office. I think that I can only say to you that our most recent figures would indicate a 14-percent increase in chapter XIII filings, and not that great an increase in pure employee filings. So that there is some probability by the end of this fiscal year that your chapter XIII file will exceed in proportion the number of employee filings.

Mr. POFF. I see. Well, I thank the gentleman for his willingness to appear, and I think you have made a very useful contribution to our hearings.

Judge BROWN. Well, your task is never an easy one. I have great respect for it. I just don't want to encroach upon it.

Mr. POFF. I thank you, sir.

Mr. ROGERS. Mr. McClory?

Mr. McCLODY. Thank you, Mr. Chairman.

Judge Brown, I appreciate your testimony and your contributions to this committee, and particularly your desire to see that the Congress carries out the original intent and purpose of the bankruptcy law as enacted. I notice on your statement in connection with the historical reference to this subject that the Congress declared that it should establish "uniform laws on the subject of bankruptcy throughout the United States."

Now the thing that concerns me with regard to the immediate problem is the great lack of uniformity in the use of these laws which appears throughout the varying districts. I have noticed, for instance, the appendix, the supplement to your statement, in which you make reference to the total number of filings, and the utilization of chapter XIII, and I find that in some jurisdictions, it is not utilized at all, and in other jurisdictions, it is used generously.

I note that you have done a very good job, and the court in the State of Kansas, in encouraging the utilization of chapter XIII, whereas, in other areas, they have not done such a good job. I would judge that one of the main purposes and one of the, I think, principal impacts of the legislation which we have under consideration is to require the courts to make some kind of a determination and to develop some kind of a uniformity so that we treat debtors and creditors pretty much alike in the 50 States of the United States.

I would like to have your comment on how you think this lack of uniformity from zero to 82 percent, I guess can be achieved through this voluntary existing system that we have.

Judge Brown. Well, Congressman McClory, the Bankruptcy Act is written to accept the various creditor laws of the States. Your Federal courts—and I say your Federal courts advisedly—have the requirement of interpreting in connection with the Bankruptcy Act and with all law, as a matter of fact, the law of some 50 different States as debtor-creditor relationships exist in those States.

There are many other phases and factors that enter into whether or not they are chapter XIII's. If you will look, I think you will find they have practically none in New York, but they have a very different garnishment law in New York, and I'm sure Mr. Twinem who is much more familiar and has been a witness, I noted, and will be a witness again, can explain this to you out of the depth of his wide experience.

This is true also in Texas. I think you will find very few garnishment laws in Texas that affect the employee or the wage earner. This is the reason, one of the reasons for probably many, for the diversity. But we have tried through the States—now most States have uniform commercial codes.

Kansas just adopted the uniform commercial code. This is a code to get some uniformity, but we have the problem of interpreting this relationship in the light of the laws of the States.

Mr. McCLODY. Well, doesn't this follow? It seems to me that it does follow. It seems that there is a lack of uniformity on the part of the referees in bankruptcy advising or suggesting or encouraging utilization of chapter XIII, so that this great disparity does not just occur because of a difference in individual State laws.

We have had testimony before the committee already that almost half of the total amount of credit, of installment credit, of purchaser consumer credit, is generated by the commercial banks, and of course, they are in general just in the same business of lending money to consumers as they are to businesses or corporations, and other types of loans. Thus we are not dealing with a specialized situation which has sometimes come under attack as far as high interest rates or carrying charges, or things like that, but we are dealing here almost to the extent of half of these \$72 billion of credit that is outstanding with the regular commercial banking institutions, and it would seem to me that they should be entitled to some uniform practice, which is it seems to me would be required under this amendment. Thus even after the referee has acted in requiring a showing that the debtor could not pay his debts under chapter XIII, he would have the uniform right to decide that he could have straight bankruptcy here.

Do you disagree with that?

Judge BROWN. Well, it depends on how far you want to extend Federal regulations of credit. This is that simple. As it is now established, the States regulate the credit community of their States, except insofar as the Bankruptcy Act cuts across State debtor-creditor rules and your uniformity is, of course, in establishing that the various States will have the rights that they do have.

It is the constitutional provision you refer to which enables Congress to make these enactments, and it is true, wherever you have the judgment of individuals, there is some dissimilarity, perhaps, in that judgment.

That would be true in connection with the manner in which nationwide corporations or enterprises who are in the business of selling money, or providing the financial basis for our country, and I am sure it is well known that without them, we would not have the tremendous economy we have today.

There is nothing wrong with what they do, but they must apply themselves to the laws of the various States, under the present concept of the Bankruptcy Act.

This again is where we get into the problem that I am trying to avoid, not because I don't have views, gentlemen, that I could express personally, but I appear here in a different capacity, and like the members of your committee, the committee on Bankruptcy Administration, probably has as many different views as there are members of the committee on various different things, but we come up with a composite judgment.

Mr. McCLORY. I appreciate that. I am not trying to get you to say anything that you did not come here intending to say, but at the same time, I want to interpret your testimony in the light of the purpose of this legislation. I can't help but recognize from your attachment to your own testimony, and from your own desire to carry out a congressional purpose of uniformity, that we have a system which is nonuniform at the present time. I think that nonuniformity is damaging both to a creditor and debtor, and I would say I just can't help but make that observation, and I can't help but find support for that observation if what you have related, plus the information which has been furnished us by the Administrative Office of the U.S. Courts is true.

Judge BROWN. There is not any question about it. There is no question but what in the application of creditor-debtor law, the State law is applicable. We have 50 different States, and while many of the provisions are made, they are applicable.

Mr. McCLODY. And in the administration of the bankruptcy laws, it is also nonuniform in the various judicial districts of the Nation?

Judge BROWN. In the administration of bankruptcy, there may be a different philosophy which is different, there may be a different application, decisions which we work with; this is entirely appropriate.

There is difference in circuits. We have a provision by which when there is a division in circuits, that the Supreme Court may reach down and reconcile those differences. They did in the *Perry* case which you have heard me refer to.

Mr. McCLODY. Thank you.

Mr. ROGERS. Thank you, Judge. We certainly appreciate your coming and giving us the benefit of your testimony, and we appreciate the experience that you have had, and you have shared it with us here today.

Judge BROWN. Very well.

Mr. ROGERS. You are excused.

The next two witnesses, I understand, are to testify together. The Honorable Richard E. Poulos and Professor Vern Countryman, who will both come forward, please. They represent the national bankruptcy conference.

As I understand, each of the gentlemen has a prepared statement, and with their permission, I will insert them in the record at this point; and you may epitomize and go forward in the manner that you think best that you can inform us in connection with this matter.

(The documents referred to follow:)

STATEMENT OF PROFESSOR VERN COUNTRYMAN, HARVARD LAW SCHOOL ON
H.R. 1057 AND H.R. 5771

I am a Professor of Law at Harvard Law School. I have taught bankruptcy law since 1946, save for a four-year period, 1955-1959, when I practiced law in Washington, D.C. I am also Chairman of the Committee on Chapter XIII and Consumer Bankruptcy of the National Bankruptcy Conference and I appear here today on behalf of the National Bankruptcy Conference.

The Conference is opposed to H.R. 1057 and to H.R. 5771, which are identical. The proponents of these bills seek to justify their proposal by (1) the phenomenal increase in bankruptcies in recent years and (2) an assertion that most bankrupts could pay their debts if they wished to do so.

There is no question about the increase in bankruptcy filings. They have gone from an all-time low of some 10,000 in 1946 to more than 192,000 in 1966 and preliminary figures indicate that they will exceed 200,000 in 1967. This increase, moreover, is to be attributed largely to consumer bankruptcies. While business bankruptcies have gradually increased from some 1,600 in 1946 to more than 16,000 in 1966, they now constitute only 8.5% of total filings where they constituted 16% in 1946.

Consumer bankruptcies, in the same period, have multiplied almost twenty times from 8,500 to almost 176,000, from 84% of the total to 91.5%. And of these consumer bankrupts, more than 90% are classified as employees, who would be eligible for Chapter XIII.

So there is no question about the remarkable increase in bankruptcy filings, nor that most of the increase is by employees, whose filings have also multiplied twenty times (from 7,600 in 1946 to 160,000 in 1966) in the past twenty-one years. But I am aware of no studies which will support the assertion made in support of these bills that most of those employee bankrupts could pay their debts if only they were willing to do so.

I am aware of one sample study which finds that the typical bankrupt has a family of five, assumes that an "adequate" income for such a family is \$3171 and a "comfortable" income is \$4133, and on the basis of this assumption concludes that from 49% to 28% of all bankrupts in Genesee County, Michigan, could pay their debts. *Dolphin, An Analysis of Economic and Personal Factors Leading to Consumer Bankruptcy* (1965). I am aware of another sample study that finds an average income among bankrupts of \$4489, assumes that 40% of this income could be applied to debts, and concludes therefore that from 25% to 50% of all bankrupts in Utah could pay their debts. *Misbach, Personal Bankruptcy in Utah* (1964). I am aware of a third sample study which finds that the average monthly income of bankrupts is \$484, and concludes that if 20% of that income were applied to debts 39% of all Seattle bankrupts could pay and if 25% of income were applied to debts 56% could pay. *Brosky, A Study of Personal Bankruptcy in the Seattle Metropolitan Area* (1965). And I am aware also of a fourth sample study which assumes that one-fourth of a bankrupt's income can be applied to debts, but which reaches no conclusion as to what percentage of bankrupts would thus have been able to pay off their debts. *Reed, Personal Bankruptcies in Oregon* (1967).

But I am also aware of seven other sample studies of consumer bankruptcies which reach no such pat conclusions, but which conclude instead that the entire problem of consumer credit and the causes of consumer bankruptcies needs considerable additional study before any revolutionary changes in the bankruptcy law will be in order. *Stabler, The Experience of Bankruptcy* (1966); *Jacobs, The Family in Financial Crisis* (1965); *Schaber, Voluntary Bankruptcy—A Growing Consumer Bankruptcy Problem* (1959); *Harms, Some Aspects of Business Policies and Procedures in Relation to Personal Bankruptcy in the Wichita Area* (1961); *Myers, The Consumer Bankrupt in Maryland* (1961); *Murphy and Edwards, Bankruptcy Survey Report* (1964); *Brunner, Personal Bankruptcies in Ohio* (1965).

While I am not an economist, I have given considerable thought to the reason for the increase in consumer bankruptcies. It cannot be attributed to the increase in population, which has increased by about one-third (from 141,936,000 in 1946 to about 196,000,000 in 1966). Nor can it be attributed to unemployment, which was 2,270,000 in 1946 and 2,875,000 in 1966 and has ranged between 1.6 and 4.7 million during the interim period. Neither is there a direct relation between rising bankruptcies and increasing gross national product or expenditure, which has slightly more than tripled (from \$211.1 billions in 1946 to \$739.6 billions in 1966).

But certain expanding items in the gross national product or expenditure seem to me significant. As reported by the Federal Reserve Board, consumer credit, exclusive of home mortgages, has increased tenfold, from \$8.38 billions in 1946 to \$94.8 billions in 1966, and so have home mortgages, from \$23 billions in 1946 to \$225.4 billions in 1966. When we add to this the fact that disposable personal income after taxes has only slightly more than trebled, from \$147 billions to \$505.3 billions, it is apparent that consumer resources have not kept pace with consumer credit commitments.

This, it seems to me, is a pretty fair indication of the reason for the rise in consumer and employee bankruptcies. It also casts serious doubt on the assertion that most employee bankrupts could pay their debts if they wanted to do so. I would also add that it raises serious questions about consumer credit practices, both on the part of the debtors and on the part of those who extend the credit. But these are all matters which require further examination before firm conclusions can be reached, which is the judgment of most of those who have made sample studies of the problem thus far.

H.R. 1057 and H.R. 5771 would require any bankrupt "whose principal income is derived from wages, salary or commissions" (the definition of "wage earner" contained in § 607(8) of Chapter XIII) to persuade the bankruptcy referee that "adequate relief" could not be obtained under Chapter XIII and, if he fails to do so, the bankruptcy proceeding is to be dismissed unless he amends his petition to convert the case to a Chapter XIII proceeding. This proposal seems objectionable to the National Bankruptcy Conference for several reasons.

The basic scheme is to authorize the bankruptcy court to force wage earners from straight bankruptcy to Chapter XIII, or at least to deny them access to straight bankruptcy when they fail to persuade the court that they cannot carry out a Chapter XIII plan. This scheme is similar to, but even more objectionable than, a proposal of some thirty-five years ago that we adopt the English practice

of suspending straight bankruptcy discharges until the debtor has paid off, or at least substantially reduced, his existing debts from his future earnings. That proposal provoked vehement opposition in Congressional hearings—it is, to my knowledge, the only proposed bankruptcy amendment to be characterized by witnesses as “UnAmerican” (Joint Hearings before subcommittees of House and Senate Judiciary Committees on S. 3866, 72d Cong., 1st Sess., pp. 546, 753 (1932)—and never emerged from Committee. What emerged instead were the provisions of Chapters XI and XIII by which any debtor, regardless of the nature of his future earnings, could *voluntarily* commit those earnings to the payment of his existing debts.

Basically, the objections to the suspended discharge proposal were threefold, and they are more than equally applicable to H.R. 1057 and H.R. 5771.

First, the involuntary feature is “contrary to the genius of our institutions” (Joint Hearings, *supra*, p. 641). We have outlawed peonage and other forms of involuntary servitude and have largely outlawed imprisonment for debt. After three experiments with a bankruptcy law which conditioned the debtor's discharge on creditor consent, we have rejected that device in favor of an unobstructed discharge for the bankrupt who honestly surrenders his existing assets. We can hardly be expected now to approve a system whereby the debtor's opportunity for rehabilitation is to be delayed for a period of bondage during which his future earnings are sequestered for the benefit of his existing creditors.

Second, *voluntary* composition and extension agreements have been successfully employed as a common law device, under an 1874 amendment to the Bankruptcy Act of 1867, under § 12 of the Bankruptcy Act of 1898, and under Chapters XI and XIII as added by the Chandler Act of 1938. But an *involuntary* composition or extension forced upon a debtor seeking straight bankruptcy can be expected to work about as well as compulsory counseling of a spouse bent on separation or divorce. While voluntary compositions and extensions have worked under Chapters XI and XIII, the debtor who is forced into Chapter XIII could not reasonably be expected to have the same incentive or to make the same effort to produce the earnings necessary successfully to perform under the plan.

The third objection to the suspended discharge proposal, which applies with even greater force to these bills, was that it discriminated against individual, non-corporate debtors. The individual bankrupt needs his discharge and, if it were suspended, must perforce attempt to meet the terms of suspension in order to get it. But most corporate bankrupts do not even bother to apply for a discharge. The stockholders can walk away from the bankrupt corporate shell without fear of unpaid corporate debts for which they were never personally liable. These bills preserve this discriminatory feature and more. Only individuals “whose principal income is derived from wages, salaries or commissions” would be required to commit their future income to past debts in order to obtain a bankruptcy discharge. No similar limitation is to be placed on corporations, or self-employed individuals or unemployed individuals with income from investments or pensions.

It is for these reasons that the National Bankruptcy Conference is opposed to H.R. 1057 and H.R. 5771. We are not opposed to a greater use of Chapter XIII as a voluntary device. We are aware that while employee filings have increased from 7,600 in 1946 to 160,000 in 1966, the number of these filings under Chapter XIII was only 1,370 in 1946 and 28,260 in 1966 (about 18% of all employee filings in both years). We are aware also that in 1966 there were more than 1,000 Chapter XIII filings in only six states—Alabama, California, Georgia, Kansas, Ohio and Tennessee—and more than 500 in only six more—Illinois, Kentucky, Maine, Minnesota, Virginia and Washington—so that in the great majority of states Chapter XIII is not significantly employed.

But, while we share an interest in expanding the use of Chapter XIII, we do not believe that these bills providing for an involuntary system will accomplish that purpose. Even on a voluntary basis, as it now is in the few states where Chapter XIII is used, less than half of the voluntary petitions lead to a confirmed plan (28,260 filings and 10,530 confirmations in 1966); the balance are either dismissed or end in an adjudication in straight bankruptcy. And of the plans confirmed, we know that many are never successfully completed, although these failures are not reported in the official bankruptcy statistics.

We believe that Chapter XIII will only work as a voluntary proceeding and that the way to encourage its use in more states and to improve the performance record where it is used is to persuade more debtors voluntarily to employ it. Since twenty-eight years' experience with the Chapter have revealed substantial defects calculated to discourage its use, it seems to us that the better part of wisdom is to correct those defects which now make Chapter XIII unattractive.

Accordingly, the National Bankruptcy Conference has approved amendments to Chapter XIII to deal with what seem to us to be the three most obvious defects. We hope to have those amendments in the form of a draft bill to submit to this subcommittee within the next few days. In summary, the problems with which they will deal, and the manner in which they will deal with them is as follows:

1. DEFICIENCY CLAIMS

Any wage earner debtor in such desperate straits as to be considering a choice between a petition in straight bankruptcy and one under Chapter XIII is very likely already to be in default under a security agreement covering his automobile or household furniture or appliances. One possibility here is that the secured creditor may foreclose and sell before the debtor can get his petition filed, so that the debtor will carry with him into whatever procedure he chooses a deficiency claim. Another possibility is that, even if the debtor's petition precedes the foreclosure sale, his equity in the property may be so small and his remaining obligation under the security agreement so onerous that it would not be feasible to attempt to include the secured obligation in a wage earner plan even if he elected to file in Chapter XIII rather than in straight bankruptcy. Here again, he will in effect carry with him, into whatever procedure he elects to pursue, a deficiency claim.

Now if we confine ourselves to these two possibilities for the moment, we all know that the deficiency claim can be a brutally large one. This is particularly true in what is perhaps the most common instance, the deficiency claim under an automobile purchase contract.

The bank or the finance company which holds the paper on the automobile will not have equipped itself either efficiently to dispose of the auto or to hold it while attempting disposition. Too often the solution is a quick sale to a used car dealer at a price which does not approach even the wholesale prices for used cars quoted in the dealers' "Bluebook"—with a correspondingly large deficiency claim.

The state law which is or soon will be applicable to such transactions in all states but Louisiana gives the debtor precious little protection in this situation. Under § 9-504(3) of the Uniform Commercial Code, the foreclosure may be by public or private sale; the creditor may bid in the property himself at any public sale and also at any private sale if the collateral is of a type "customarily sold in a recognized market or . . . the subject of widely distributed standard price quotations." Unless the collateral "is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market," the creditor must be careful to give the debtor "reasonable notification" of the time and place of sale. But if he does that, the debtor's only other basis for complaint is that the sale is not "commercially reasonable." But the debtor is advised by another provision of the Code, § 9-507(2) that, "The fact that a better price could have been obtained by a sale at a different time or in a different method from that selected by the secured party is not of itself sufficient to establish that the sale was not made in a commercially reasonable manner."

If the debtor is wise enough to file in straight bankruptcy, the fact that the state law gives him little protection against inflated deficiency claims is of no concern to him. With or without assets in the estate, the bankruptcy discharge will cover the inflated claim as well as non-inflated claims. Whether or not the deficiency claim is inflated will be a matter of concern to other creditors only—and then only in that very small minority of cases (12% in 1966) where there are assets to distribute to creditors.

If, on the other hand, the debtor has opted for Chapter XIII, the unsecured deficiency claim must be included in the plan and must be treated on an equal basis with all other unsecured claims (§646). Hence, the fact that the deficiency claim is now a matter of concern, not only to the other creditors, but to the debtor as well.

The first proposal of the National Bankruptcy Conference would give the debtor and the other creditors the protection in Chapter XIII which state law does not afford. It would authorize the court, whenever a secured creditor presented a deficiency claim based on a sale of collateral before or after the position was filed, to determine the value of the collateral after notice and hearing, and to allow the deficiency claim only in the amount by which the indebtedness and costs of sale exceed the value so determined, or the sale price, whichever is higher.

This is no new or heroic remedy, and it involves no novel techniques. Such provisions are not uncommon in state laws dealing with the foreclosure of realty

mortgages and in this form have survived constitutional test. *Gelfert v. National City Bank*, 313 U.S. 221 (1941); *Honeyman v. Jacobs*, 306 U.S. 539 (1939); *Richmond Corp. v. Wachovia Bank*, 300 U.S. 124 (1937). And at least one state—California—which goes further to prohibit deficiency judgments entirely on purchase money mortgages on realty extends that prohibition to deficiency judgments on chattel mortgages also where both a realty and a chattel mortgage are given to secure the combined purchase price of both types of collateral. *Calif. Code Civ. Proc. §580b*. Certainly there is nothing new in requiring the bankruptcy court to value the collateral. Even if the valuation of secured claims against a continuing business under §77 and Chapter X be regarded as essentially different, the court is now authorized to value collateral in straight bankruptcy proceedings by §57h. And it does so also in Chapter XI and XIII proceedings where those Chapters are interpreted (correctly, I believe) to mean that an inadequately secured creditor has two claims—one secured and one unsecured.

2. THE SECURED CREDITOR'S VETO

Another possibility, not considered above in connection with secured claims against a wage earner debtor contemplating filing a petition under the Bankruptcy Act, is that he may wish to preserve his equity under the security agreement. He may wish to do so merely because that equity is substantial or it may be that the collateral, such as an automobile or trade tools, is essential to his livelihood. At the same time it may be apparent that a wage earner plan is feasible only if payments to the secured creditor, like those to unsecured creditors, can be extended. Or perhaps it may be obvious that all claims, secured and unsecured, must be reduced.

A plan which affects unsecured creditors can be confirmed if accepted by a majority in number and amount, but if secured creditors are "dealt with" by the plan it must be separately accepted by each secured creditor (§ 652).

While the decisions are not as clear as could be wished, the prevailing view seems to be that a secured creditor is dealt with by the plan, and thus has a veto power over it, if the plan proposes any variation in the terms of the secured obligation—and this without regard to the extent to which those terms are in fact secured by the collateral. *In re Pappas*, 216 F. Supp. 819 (S.D. Ohio, 1962); *In re Copes*, 206 F. Supp. 329 (D. Kan., 1926); *In re O'Dell*, 198 F. Supp. 389 (D. Kan., 1961). See also *In re Clevenger*, 282 F. 2d 756 (7th Cir. 1960); *Interstate Finance Corp. v. Scroggins*, 265 F. 2d 889 (6th Cir. 1959); *In re Duncan*, 33 F. Supp. 997 (E.D. Va., 1940). Cf. *In re Wilder*, 225 F. Supp. 67 (M.D. Ga., 1963). Since there is no limitation of good faith or reasonable cause on the secured creditor's exercise of his veto, he may for reasons quite unrelated to the fairness of the plan effectively block any plan which in any way varies the terms of his claim. This leaves, as the only alternative, a plan which does not deal with his claim at all, but its failure to embrace that claim may render it impossible for the debtor to carry through under the plan.

In other proceedings under the Bankruptcy Act where creditor consent is necessary, the case of the unreasonably recalcitrant creditor has been anticipated. Section 77e, which requires acceptance of a railroad reorganization plan by two-thirds in amount of each class of creditors, also provides that the judge may confirm the plan without such acceptance "if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the . . . claims of those rejecting it" and that "such rejection is not reasonably justified in the light of the respective rights . . . of those rejecting it and all the relevant facts." This provision was held constitutional and applied in *Reconstruction Finance Corporation v. Denver & Rio Grande Western Railroad Co.*, 328 U.S. 495 (1946). Similarly in Chapter X, where § 179 requires acceptance of a corporate reorganization plan by two-thirds in amount of each class of creditors, an exception is made in § 216(7) for any dissenting class if the plan or the order confirming the plan provides "adequate protection for the realization by them of the value of their claims against the property of the debtor dealt with by the plan and affected by such claims."

The second proposal approved by the National Bankruptcy Conference would borrow from these provisions. It would authorize the Chapter XIII court to confirm a plan without the acceptance of any creditor or class of creditors whose acceptance would otherwise be required if the court finds that the plan adequately provides for the realization by such creditor or class of creditors of the value of its claim or claims against the property and future earnings of the debtor and provides for equal treatment for each creditor of the same class.

3. UNCONSCIONABLE CLAIMS

In all states but Louisiana, where the Uniform Commercial Code has not been adopted, and California and North Carolina, where § 2-302 is omitted, bankruptcy courts now may or will soon be able to invoke state statutory law to deal with unconscionable sales contracts. Section 2-302(1) of the Uniform Commercial Code provides:

"If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result."

Since this provision appears in Article 2 of the Code, dealing with sales of goods, it presumably is applicable only to contracts for the sale of goods—including sales of goods on secured credit. While there is a developing case-law doctrine of unconscionability which presumably will not be so limited, that doctrine is not yet established in most jurisdictions.

We see no reason to believe that debtors dealing with lenders of money or sellers of services are in any less need of protection from unconscionable contracts than debtors dealing with sellers of goods—particularly since it is well known that the same financing agency may draft the contract for all three such transactions.

Accordingly, the third proposal approved by the National Bankruptcy Conference is to add to Chapter XIII a provision modeled on U.C.C. § 2-302(1), save that it will permit the court to apply the unconscionability test to any claim against the debtor regardless of the underlying consideration.

It is contemplated that, as applied in any insolvency proceeding, the provision may reach to unconscionability as against other creditors as well as against the debtor, and that the proper way to "avoid any unconscionable result" may be to subordinate the overreaching creditor's claim to those of other creditors. Corresponding qualifications are proposed, accordingly, for § 646 to permit the subordinated creditor or creditors to be treated as a separate class, and for § 652 to permit voting by classes.

Since the end result of the application of these proposals will usually be to produce a class consisting of one or a few very disgruntled creditors, it was deemed prudent to apply to such creditors' veto power, as well as to the secured creditors' veto power, the provision authorizing the court to confirm despite the veto on a finding that the plan adequately recognizes the vetoing creditors' claims on the property and future earnings of the debtor and treats all creditors in the same class equally.

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These are the National Bankruptcy Conference proposals. We believe that they are salutary provisions which stand on their own merits and which should be added to Chapter XIII quite without regard to their effect upon the frequency with which that Chapter is used. As they also are aimed at credit abuses for which there is now no effective remedy in wage earner proceedings, we believe that they would have the effect of encouraging resort to such proceedings rather than to straight bankruptcy. And finally, we do not consider it the least of their merits that the protection which they would give against credit abuses accrues not only to the debtor but also to those creditors who have dealt fairly with him.

STATEMENT OF PROF. VERN COUNTRYMAN, HARVARD LAW SCHOOL

MR. COUNTRYMAN. Thank you, Mr. Chairman. I am a professor of law at the Harvard Law School. I have taught bankruptcy since 1946, save a 4-year period, from 1955 to 1959, when I practiced law in Washington, D.C.

I am also chairman of the committee on chapter XIII and consumer bankruptcy of the national bankruptcy conference, and I appear here today on behalf of the national bankruptcy conference.

I have submitted a rather lengthy written statement to the committee. I will try to abbreviate my oral statement.

The national bankruptcy conference is opposed to H.R. 1057 and to H.R. 5771, which are identical bills. The proponents of these bills seek to justify their proposal by, one, the phenomenal increase in bankruptcies in recent years, and, two, an assertion that most bankrupts could pay their debts if they wished to do so.

There is no question about the increase in bankruptcy filings. They have gone from an alltime low of some 10,000 in 1946 to more than 192,000 in 1966 and preliminary figures indicate that they will exceed 200,000 in 1967.

This increase, moreover, is to be attributed largely to consumer bankruptcies. While business bankruptcies have largely and gradually increased from some 1,600 in 1946 to more than 16,000 in 1966, they now constitute only 8.5 percent of total filings where they constituted 16 percent in 1946.

Consumer bankruptcies in the same period have multiplied almost 20 times from 8,500 to almost 176,000, from 84 percent of the total to 91.5 percent. And of these consumer bankrupts, more than 90 percent are classified as employees, who would be eligible for chapter XIII.

So there is no question about the remarkable increase in bankruptcy filings, nor that most of the increase is by employees, whose filings have also multiplied 20 times—from 7,600 in 1946 to 160,000 in 1966—in the past 21 years.

But I am aware of no studies which will support the assertion made in support of these bills that most of those employees bankrupt could pay their debts if they were willing to do so.

Now I had referred in my written statement, and I will not repeat in my oral one, to some 11 sample studies which have been made of consumer bankruptcies in recent years.

Most of them do not reach a conclusion that any given percentage of employee bankruptcies could pay all their debts if they wanted to. Most of them instead conclude that the entire problem of consumer credit and the causes of consumer bankruptcies needs considerable additional study before any revolutionary changes in the Bankruptcy Act will be in order.

Their conclusion, I think, gets to the question raised yesterday by Mr. Jacobs about the whole business of "happy money" in our society.

While I am not an economist, I have given considerable thought to the reason for the increase in consumer bankruptcies and I have seen that it cannot be attributed to the increase in population, which has increased only about one-third during the 21-year period while consumer bankruptcies were multiplying 20 times.

Nor can it be attributed to unemployment, which was 2.2 million in 1946 and 2.8 million in 1966. Neither is there a direct relationship between rising bankruptcies and increasing gross national product or expenditure which has only slightly more than tripled while the bankruptcies were multiplying 20 times.

But certain items in the gross national product or expenditure do seem to me to be significant. As reported by the Federal Reserve Board, consumer credit, exclusive of home mortgages, has increased tenfold, in the 21-year period I am talking about, from \$8.3 billion in 1946 to \$94.8 billion in 1966, and home mortgages have also increased tenfold from \$23 to \$225 billion.

When we add to this total increase in consumer credit the fact that disposable personal income after taxes, which is what this credit has

to be repaid from, has only slightly more than trebled, it seems apparent that consumer resources have not kept pace with consumer credit commitments.

This, it seems to me, is a pretty fair indication of the reason for the rise in consumer and employee bankruptcies. It casts serious doubt on the assertion that most employee bankrupts could pay their debts if they wanted to do so.

I would also add that it raises serious questions about consumer credit practices, both on the part of the debtor and on the part of those who extend the credit. But these are all matters which require further examination before firm conclusions can be reached, which is the judgment, as I indicated earlier, of most of those who made sample studies on consumer bankruptcies.

The basic scheme of the two bills which the committee is now considering is to authorize the bankruptcy court to force wage earners from straight bankruptcy so chapter XIII, or at least to deny them access to straight bankruptcy when they failed to persuade the court that they could not carry a chapter XIII plan.

That scheme is very similar to, but even more objectionable than, a proposal made some 35 years ago to this committee that we adopt the English practice of suspending straight bankruptcy discharges until the debtor has paid off or at least substantially reduced his existing debts from his future earnings.

That proposal provoked vehement opposition in congressional hearings. It is, in fact, the only proposed bankruptcy amendment which to my knowledge has been characterized by witnesses, as "un-American," and that proposal never emerged from committee.

What emerged instead were the provisions of chapters 11 and 13 by which any debtor, regardless of the nature of his future earnings, could voluntarily commit those earnings to the payment of his existing debts.

Basically, the objections to the suspended discharge proposal were three, and all three are more than equally applicable to the bills before the committee today.

First, the involuntary feature was, as witnesses characterized it 35 years ago, contrary to the genius of our institutions. We have outlawed peonage and other forms of involuntary servitude, and have largely outlawed imprisonment for debt. After three experiments with a bankruptcy law which conditioned the debtor's discharge on creditor consent, we in 1898 rejected that device, in favor of an unobstructed discharge for the bankrupt who honestly surrenders his existing assets.

We can hardly be expected now to approve a system whereby the debtor's opportunity for rehabilitation is to be delayed for a 3-year period of bondage, during which his future earnings are sequestered for the benefit of his existing creditors.

Second, voluntary composition and extension agreements have been successfully employed as a common law device, under an 1874 amendment to the Bankruptcy Act of 1867, under section 12 of the Bankruptcy Act of 1898, and under chapters XI and XII as added by the Chandler Act of 1938.

But an involuntary composition or extension forced upon a debtor seeking straight bankruptcy can be expected to work about as well as compulsory counseling of a spouse bent on separation or divorce.

While voluntary compositions and extensions have worked under chapters XI and XIII, the debtor who is forced into chapter XIII could not reasonably be expected to have the same incentive or to make the same effort to produce the earnings necessary successfully to perform under the plan.

Now you heard Mr. Twinem say yesterday, and I have heard him say before, that these bills do not contemplate an involuntary procedure. The debtor is perfectly free to go into chapter XII or not to go into chapter XIII. The only condition is that if he does not go into chapter XIII, he can't go into straight bankruptcy, either, and he cannot get a bankruptcy discharge.

This sort of freedom seems to me comparable to the equal freedom of the rich and the poor to sleep under bridges; for those who have only one choice, it is not much freedom.

The third objection to the suspended discharge proposal, which applies with even greater force to these bills, was that it discriminated against individual, noncorporate debtors. The individual bankrupt needs his discharge and if it were suspended, must perforce attempt to meet the terms of suspension in order to get it.

But most corporate bankrupts do not even bother to apply for a discharge to which they are entitled. The stockholders can walk away from the bankrupt corporate shell without fear of unpaid corporate debts for which they were never personally liable.

These bills preserve this discriminatory feature and more. Only individuals whose principal income is derived from wages, salaries, or commissions, would be required to commit their future income to past debts in order to obtain a bankruptcy discharge.

No similar limitation is to be placed on corporations, or self-employed individuals or unemployed individuals with income from investments or pensions.

Now I am aware from what has been said previously in these hearings that Congressman Poff is contemplating an amendment which would extend these bills to all natural persons eligible for bankruptcy.

I believe that that raises questions which have not yet been considered. It would for instance, extend this proposal to individuals who are engaged in business as sole proprietorships and partnerships. And then the question for the bankruptcy referee would be, "Should I require this man to continue his business, in order to pay off his debts?"

That it seems to me is an extremely difficult decision to ask the referee to make, but if you get that far, then how do you distinguish the corporate business from the noncorporate business?

I listened with some amazement yesterday to a banker witness, Mr. Kendall, who explained to you that corporate debts were different from others, because a bank which loans money to a consumer is interested in his future income, but a bank which loans money to a corporation is only interested in its balance sheet.

I think Mr. Kendall must be a very unique banker indeed. I have represented a number of businessmen, who were borrowing money from banks, and I always found that the banker was at least as interested in the income statement as he was in the balance sheet, and that there, as in the case of the consumer, he was lending primarily against the estimated future earnings of the business, and he was interested in the assets only as a last resort, which he hoped he would never have to resort to.

It is for these three reasons then that the National Bankruptcy Conference is opposed to these bills. We are not opposed to a greater use of chapter XIII as a voluntary device. We are aware that while employee filings have increased from 7,600 in 1946 to 160,000 in 1966, the number of these filings under chapter XIII was only 1,370 in 1946 and 28,260 in 1966 (about 18 percent of all employee filings in both years).

I have been advised by the administrative office since I got here for these hearings that preliminary figures indicate that chapter XIII filings for 1967 will increase to about 32,000, and this will represent a greater proportion of all employees filing any sort of a petition under the Bankruptcy Act than the 18 percent to which I have referred, and that perhaps this increase is due to the recent decision of the Supreme Court in the *Perry* case, to which Judge Brown referred.

(The decision referred to, *Perry v. Commerce Loan Company*, is set out at pages 138-155.)

We are also aware that as matters now stand in 1966, there were more than 1,000 chapter XIII filings in only six States—Alabama, California, Georgia, Kansas, Ohio, and Tennessee—and more than 500 in only six more—Illinois, Kentucky, Maine, Minnesota, Virginia, and Washington—so that in the great majority of States chapter XIII is not significantly employed.

But while we share an interest in expanding the use of Chapter XIII, we do not believe that these bills providing for an involuntary system will accomplish that purpose.

Even on a voluntary basis as it now is in the few States where chapter XIII is used, less than half of the voluntary petitions lead to a completed plan.

As I believe someone else has previously pointed out, there were some 28,000 filings in 1966, but only 10,500 successful chapter XIII plans.

We believe that chapter XIII will only work as a voluntary proceeding, and that the way to encourage its use in more States and to improve the performance record where it is used is to persuade more debtors voluntarily to employ it.

Since 28 years of experience with Chapter XIII has revealed substantial defects calculated to discourage its use, it seems to us that the better part of wisdom is to correct those defects which now make chapter XIII unattractive.

Accordingly the National Bankruptcy Conference has approved amendments to chapter XIII to deal with what seem to us to be the three most obvious defects. We hope to have those amendments in the form of a draft bill to submit to this subcommittee within the next few days. In summary, the problems with which they will deal, and the manner in which they will deal with them is as follows:

The first problem is that of deficiency claims. Any wage earner debtor in such desperate straits as to be considering a choice between a petition in straight bankruptcy and one under chapter XIII is very likely already to be in default under a security agreement covering his automobile or household furniture and appliances.

One possibility here is that the secured creditor may foreclose and sell before the debtor can get his petition filed, so that the debtor will carry with him into whatever procedure he chooses a deficiency claim. Another possibility is that, even if the debtor's petition precedes the foreclosure sale, his equity in the property may be so small and his

remaining obligation under the security agreement so onerous that it would not be feasible to attempt to include the secured obligation in a wage earner plan even if he elected to file in chapter XIII rather than in straight bankruptcy.

Here again he will in effect carry with him, into whatever procedure he elects to pursue, a deficiency claim.

Now if we confine ourselves to these two possibilities for the moment, we all know that the deficiency claim can be a brutally large one. This is particularly true in what is perhaps the most common instance, the deficiency claim under an automobile purchase contract.

The bank or finance company which holds the paper on the automobile will not have equipped itself either efficiently to dispose of the auto or to hold it while attempting disposition. Too often the solution is a quick sale to a used car dealer at a price which does not approach even the wholesale prices for used cars quoted in the dealers' "Blue-book," with a correspondingly large deficiency claim.

The State law which is or soon will be applicable to such transactions in all States but Louisiana (and I am referring to the Uniform Commercial Code, which has been adopted everywhere else) gives the debtor precious little protection in this situation.

Under the Code, the foreclosure may be by public or private sale. The creditor may bid in the property himself at any public sale and also at any private sale if the collateral is of a type customarily sold in a recognized market or the subject of widely distributed standard price quotations.

Unless the collateral is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market, the creditor must be careful to give the debtor reasonable notification of the time and place of sale.

But if he does that, the debtor's only other basis for complaint is that the sale is not commercially reasonable.

But the debtor is advised by another provision of the Code that the fact that a better price could have been obtained by a sale at a different time or in a different method from that selected by the secured party is not of itself sufficient to establish that the sale was not made in a commercially reasonable manner.

If the debtor is wise enough to file in straight bankruptcy the fact that the State law gives him little protection against inflated deficiency claims is no concern to him.

With or without assets in the estate, the bankruptcy discharge will cover the inflated claim as well as a noninflated claim. Whether or not the deficiency claim is inflated will be a matter of concern to other creditors only—and then only in that very small minority of cases (12 percent in 1966 and that is about par for the course) where there are any assets to distribute to creditors.

If on the other hand the debtor has opted for chapter XIII the unsecured deficiency claim must be included in the plan and must be treated on an equal basis with all other unsecured claims. Hence the fact that the deficiency claim is inflated is now a matter of concern, not only to the other creditors, but to the debtor as well.

The first proposal of the national bankruptcy conference would give the debtor and the other creditors the protection in chapter XIII which State law does not afford. It would authorize the court, whenever a secured creditor presented a deficiency claim based on a sale of

collateral before or after the petition was filed, to determine the value of the collateral after notice and hearing, and to allow the deficiency claim only in the amount by which the indebtedness and costs of sale exceed the value so determined, or the sale price, whichever is higher.

This is no new or heroic remedy, and it involves no novel techniques. Such provisions are not uncommon in State laws dealing with the foreclosure of realty mortgages and in this form have survived constitutional test.

Certainly there is nothing new in requiring the bankruptcy court to value the collateral. Even if the evaluation of secured claims against a continuing business under 77 and chapter X be regarded as essentially different, the court is now authorized to value collateral in straight bankruptcy proceedings by 57h.

And it does so also in chapters XI and XIII proceedings where those chapters are interpreted—correctly, I believe—to mean that an inadequately secured creditor has two claims—one secured and one unsecured, as Judge Brown described in his testimony earlier.

A second problem with which we would deal, which I have not considered above in connection with the wage earner contemplating a petition under the Bankruptcy Act, is that he may wish to preserve his equity under the security agreement. He may wish to do so merely because that equity is substantial. Or it may be that the collateral, such as an automobile or trade tools, is essential to his livelihood.

At the same time it may be apparent that a wage earner plan is feasible only if payments to the secured creditor like those to unsecured creditors, can be extended. Or perhaps it may be obvious that all claims, secured and unsecured, must be reduced.

A plan which affects unsecured creditors can be confirmed if accepted by a majority in number and amount, but if secured creditors are dealt with by the plan it must be separately accepted by each secured creditor dealt with. In other words, each of them has a veto under the plan.

While the decisions are not as clear as could be wished, the prevailing view seems to be that a secured creditor is dealt with by the plan, and thus has a veto over it, if the plan proposes any variation in the terms of the secured obligation—and this without regard to the extent to which those terms are in fact secured by collateral.

In other proceedings under the Bankruptcy Act where creditor consent is necessary, the case of the unreasonably recalcitrant creditor has been anticipated. Section 77e, which requires acceptance of a railroad reorganization plan by two-thirds in amount of each class of creditors, also provides that the judge may confirm the plan without acceptance "if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the * * * claims of those rejecting it," and that "such rejection is not reasonably justified in the light of the respective rights * * * of those rejecting it and all the relevant facts."

This provision was held constitutional and applied in *Reconstruction Finance Corp. v. Denver & Rio Grande Western Railroad Co.* Similarly in chapter X, where 179 requires acceptance of a corporate reorganization plan by two-thirds in amount of each class of creditors, an exception is made in 216(7) for any dissenting class if the plan or the order confirming the plan provides "adequate protection for the realization by them of the value of their claims against the

property of the debtor dealt with by the plan and affected by such claims."

The second proposal approved by the National Bankruptcy Conference would borrow from these provisions. It would authorize the chapter XIII court to confirm a plan without the acceptance of any creditor or class of creditors, and this includes secured creditors, whose acceptance would otherwise be required if the court finds that the plan adequately provides for the realization by such creditor or class of creditors of the value of its claim or claims against the property and future earnings of the debtor and provides for equal treatment for each creditor for the same class.

Our third proposal deals with the matter of unconscionable claims.

In all States but Louisiana, where the Uniform Commercial Code has not been adopted, and California and North Carolina, where the section to which I will refer is omitted, bankruptcy courts now may or will soon be able to invoke State statutory law to deal with unconscionable sales contracts, and I have set out on page 14 of my statement the section from the Uniform Commercial Code which authorizes them to throw out unconscionable claims. But this provision applies only to contracts for the sale of goods, including, to be sure, sales of goods on secured credit.

We see no reason to believe that debtors who are dealing with lenders of money or sellers of services are in any less need of protection from unconscionable contracts than debtors dealing with sellers of goods—particularly since it is well known that the same financing agency may draft the contract for all three such transactions.

Accordingly, the third proposal approved by the National Bankruptcy Conference is to add to chapter XIII a provision modeled on UCC section 2-302(1) save that it will permit the court to apply the unconscionability test to any claim against the debtor regardless of the underlying consideration to a sale of goods, a sale of services, or a loan of money.

These are the National Bankruptcy Conference proposals. We believe that they are salutary provisions which stand on their own merits, and which should be added to chapter XIII quite without regard to their effect upon the frequency with which the chapter XIII is used. As they also are aimed at credit abuses for which there is now no effective remedy in wage earner proceedings, we believe that they would have the effect of encouraging resort to such proceeding rather than to straight bankruptcy.

And finally, we do not consider it the least of their merits that the protection which they would give against credit abuses accrues not only to the debtor but also to those creditors who have debt fairly with him.

Thank you, Mr. Chairman.

Mr. WHITENER (presiding). Well, Professor Countryman, I would like to thank you for your statement, and I am sure the members of the subcommittee will have some questions of you and Mr. Poulos, but at this point, we will have to recess the hearing until 2 o'clock, in view of the fact that the House is now going into session.

So we will now recess until 2 p.m.

(Whereupon, at 12 noon the subcommittee recessed, to reconvene at 2 p.m. the same day.)

AFTERNOON SESSION

The subcommittee met, pursuant to recess, at 2:12 p.m., in room 2141, Rayburn House Office Building, Hon. Andrew Jacobs, Jr., presiding.

Committee members present: Representatives Jacobs, Wiggins, and Poff.

Staff members present: Benjamin L. Zelenko, counsel, and Donald E. Santarelli, associate counsel.

Mr. JACOBS. The hearing will come to order.

Professor Countryman was about to respond to questions after his testimony this morning, and perhaps, if it is the pleasure of the witness, it might be well to proceed with the Honorable Richard E. Poulos, and if you would give your testimony, and, as the chairman would say, proceed in your own manner.

**STATEMENT OF RICHARD E. POULOS, REFEREE IN BANKRUPTCY,
PORTLAND, MAINE**

Mr. POULOS. My name is Richard E. Poulos. I am from Portland, Maine, where for the last 11 years I have been a full-time referee in bankruptcy, specializing in the administration of wage earner proceedings under chapter XIII of the Bankruptcy Act.

I have been invited by the National Bankruptcy Conference to appear as a witness at this hearing to oppose H.R. 1057 and H.R. 5771 now under consideration.

In essence these bills seek to convert chapter XIII into a compulsory program and thereby eliminate the resistance encountered from the legal profession and the referees in the jurisdictions where such proceedings are rarely employed. In my mind, this is the key feature of the bill, not so much the compulsion as against the debtor.

As an advocate of chapter XIII I am in complete accord with the objective of this legislation of making the use of the amortization program more uniform and extensive throughout the Nation. But my experience with this program in Maine has demonstrated that mandatory measures are entirely unnecessary and indeed impractical and unworkable if that objective of the bill is desired.

In any consideration of chapter XIII it is important to appreciate that it was conceived in 1932 after various studies by the Department of Justice and other sources discovered that most wage earners were anxious to pay their debts but were often forced to file bankruptcy as a last resort, in order to save their jobs if a wage garnishment occurred.

Congressman Chandler in hailing the enactment of this chapter described it as "a measure designed to aid the debt-laden man or woman before he or she falls prey to the loan sharks."

This objective could be effectively accomplished under this program because, as he explained, a person may pay his debts in reasonable installments "free from garnishment, execution, attachment, penalties, or excessive cost, under the protection of the Federal court, and the court will purge his debts of all usury."

It was not until 1952, however, that such proceedings were inaugurated in Maine by Charles A. Pomeroy now senior justice of the Maine Superior Court who was then referee in bankruptcy.

But despite initial skepticism and opposition from creditors and attorneys, the volume of new proceedings increased quickly. In 1956 a total of 107 wage earner proceedings, representing 17 percent of the total volume of business was reached.

Five years later, in 1961, the volume of new proceedings increased to 560 or 45 percent of the total filings. Since then wage earner proceedings have constituted one-half of a—1 new business, with an average of 800 cases a year.

Maine is now not only by far the leading State in New England in such matters—1966 volume: Maine 765; all other New England States, 46—but also enjoys a high position nationally, as far as total volume is concerned, and more significantly, we rank third as to the percentage of such cases in relation to the entire volume of business.

Around 2,100 wage earner proceedings are now pending, involving 30,000 claims, totaling some \$3 million with an annual distribution to creditors of nearly \$1 million, in cases where nothing would have been paid if straight bankruptcy had been filed.

As a result of this program, therefore, Maine has successfully arrested the spiraling volume of straight bankruptcy matters which prevails in nearly all other parts of the Nation.

A successful development of wage earner proceedings depends primarily on five critical factors:

1. Recognition of the outstanding benefits of such proceedings to debtors, creditors, and the general community. This is very basic.
2. Simplification of work for the attorneys representing the debtor. In my mind, if somehow the Bankruptcy Act could be amended to simplify the work of attorneys in these matters, we will go a long way in achieving the uniform use of chapter XIII throughout the country.
3. Effective control over secured creditors.
4. Sound and efficient administration after confirmation of the plan, which is after the initial and generally final involvement of the court, under the supervision of a skilled, standing, trustee geared to effect voluntary compliance by debtors. In Maine I have a Harvard law graduate who is a trustee. He is protecting the interests of these oppressed people.
5. A referee dedicated to the concept of rehabilitation and protection of debtors and fair and equitable distribution to creditors.

Without elaboration, the principal benefits of a wage earner plan to debtors are as follows: Now I list nine items, and I have done this deliberately, because I gave a speech some years ago before a credit union, and I noted repeatedly that if a wage earner did not comply with his plan, in that he was incurring new debts, or he wasn't making his payments regularly as he proposed, I dismissed the plan, and people would say, "So what? The worse that could happen is that the man would be in the same position as before he filed his case." But these debtors appreciate what these benefits are, and if we hold hearings as to whether or not a person's case should be dismissed, these wage earners show up with their wives and children, and they beg the court to keep the plan in operation—what are the benefits?

Before describing these benefits, however, it should be noted that not all cases involve plans proposing a 100-percent payment. And if you look at your bill, as amended, it seems to refer only to such plans. But really there is no reason why under the proposal a referee could

not sit back and say, "Ten percent of your debts have to be paid by extension if you wish a discharge."

The benefits of chapter XIII are as follows:

1. An extension of some 3 years for payment of debts. If a person has, say, \$2,500 worth of bills, we have a little chart telling us immediately that this person should pay \$16 a week, and if his income is adequate, we know immediately that the plan will be fairly feasible.

2. No wage attachments or repossessions are permitted. On application, however, burdensome executory contracts can be rejected, usually without damages. We have cases where families buy encyclopedias for their children, costing them \$400 or \$500. The children are usually 1 or 2 years old. They won't be able to read for 10 years. These companies are happy if these books are returned in full satisfaction of the account.

3. Elimination of all interest and finance charges on all claims classified as unsecured, as determined by the court.

This is the biggest benefit to the public, because if we have a small loan or financed sale of \$2,000, the interest or finance charges in 3 years will amount to as much as a thousand dollars.

If an alleged secured claimant is invalid by operation of law, a secured status is denied. They are then in the same category as other unsecured claims and no interest is allowed.

4. Determination of all disputed claims under control and supervision of the trustee and the court. If usury is involved the powerful provisions of section 656(b) are invoked. And 656(b) imposes a mandatory obligation on the court, regardless of what the debtor or his counsel may wish to do about that claim, and the obligation is on the court for the creditor to prove to me that the claim is free of usury.

5. Consolidation of payments to central agency—trustee—where detailed records, open to interested persons, are maintained.

6. Flexibility of plan to allow for suspension and reductions of payments as permitted by the court after notice to creditors.

7. Supervision of purchases of necessities under program geared to avoid further accumulation of debts.

8. Discharge of all debts upon completion of the plan.

9. The moderate cost of this program: If a person owes \$2,000 in our State the average cost of administration is around 10 to 15 percent, so if we have a hundred percent plan, that means the person pays back \$2,000 plus 15 percent, which means a total of \$2,300, and it is important to emphasize that the cost of this administration is borne entirely by the debtor.

In extending these benefits we overcome the criticism advanced by most attorneys and referees that chapter XIII is essentially a coercive collection procedure solely for the benefit of creditors, many of whom hold illegal and unconscionable claims.

It is this prevailing impression or attitude about chapter XIII that is the underlying reason for its extensive unpopularity and the erroneous belief that straight bankruptcy is a better and more effective remedy for financially distressed wage earners.

There is no better education to a referee in bankruptcy than to have a person go through bankruptcy and then 2 years later have him file a proceeding under chapter XIII. This gives us a specific example of the person who has achieved his discharge from bankruptcy a

few years back and, all too often we find that a great number of the bills which he had in the prior bankruptcy are included in the subsequent chapter XIII case. There are various devices that are employed whereby wage earners, or the people going through bankruptcy are compelled, or persuaded to rewrite their obligations after bankruptcy, so when they leave that case, it isn't long before they owe as much after bankruptcy as before.

So they pay the \$50 filing fee to the court, and \$200 or \$250 fee to counsel, and they get a piece of paper called a discharge which is not very effective, and then they don't get the relief that they have paid for this particular protection under the act, and what happens, it reflects upon the bar and it reflects upon the Federal courts, that these people are being protected adequately under the Bankruptcy Act.

A program dispensing such benefits is not enough. It has been our experience in Maine that an extensive use cannot be achieved unless the procedure and work for the attorneys representing debtors is considerably simplified.

Under our present act, chapter XIII is as complex and technical as chapter XI and, therefore, foreign to most attorneys.

It is rather ridiculous to expect attorneys representing wage earners to be as informed as persons specializing in chapter XI representing large organizations earning many thousands of dollars.

So what we have had to do—the referee and trustees—is to provide and improvise and make modifications in our procedures as well as taking other steps to facilitate the processing of such cases by these attorneys, and one way we do it is, as soon as the case is filed in court, the petition and the plan—and our plans are all filed with the petition—they come in at the first meeting and the attorney for the wage earner practically says nothing, and it is the court and the trustee who interrogate the debtor, and we make all of the decisions concerning the acceptance and confirmation of that plan.

As a consequence it is now as easy, if not easier, for attorneys to process chapter XIII cases than straight bankruptcy proceedings, because all they do is file the case in court, and they are no longer involved in that proceeding.

It may be of interest to the committee that I don't pay very much to the attorneys for debtors for counsel fees. When I first became a referee in 1956, the prevailing fee for the attorneys was \$75, which under section 659 is paid first out of the funds paid into the plan by the debtor.

I was informed that unless the fee was increased that the wage earner plan in Maine would be dead. I waited around to see what would happen. To my surprise, the wage earner plan grew, and it grew because the public demanded it. It grew because the attorneys realized there were very outstanding benefits to the debtors. It grew because the plan was simplified, and the processing of these cases became easy, and now I have increased the fee to a hundred.

Lastly, in order to keep all creditors reasonably satisfied, we have succeeded in balancing the conflicting interests of secured and unsecured creditors so that a fair and equitable distribution of the assets is attained.

In this respect we have developed procedures resulting in a court-supervised renewal of the secured obligation so that unsecured cred-

itors need not wait for as much as 2 years before receiving a significant distribution.

I am not going to go into detail on this, but this is what Judge Brown was talking about this morning, and what Professor Countryman indicated.

If the committee has any questions in this field, I will be happy to attempt to give an answer.

It is these features of chapter XIII that has made it sufficiently attractive to debtors, creditors, and attorneys that it is extensively used in Maine. I am convinced that if similar procedures were followed in other jurisdictions, we would experience a sharp increase in chapter XIII proceedings without the necessity of imposing compulsory requirements on debtors.

Much of what is done in Maine is admittedly novel and controversial. I am satisfied, however, after an exhaustive study of the legislative history and provisions of chapter XIII that our approach is legally correct and can be supported. Massive litigation between the trustee and the small loan industry is now pending in Maine to determine this point. It would seem to me more appropriate, however, that critical questions should be resolved legislatively.

What powers does the trustee have? Is he simply a disbursing agent? Do we take the money from the debtor and hand it to the creditors blindly, or does he have the same responsibilities as the trustee under the first seven chapters of the Bankruptcy Act?

The status and rights of secured creditors, especially as to the matter of burden of establishing a secured status, the extent of security, amount of installment payments, amount and rate of interest and, above all, the power of the court to enjoin a nonassenting secured creditor from enforcing his lien, provided, of course, that we did such in a manner as not to deprive him of property without due process of law.

One of our problems, if you are a referee for any length of time, is that you become appalled by the type and nature of the claims that are filed. Probably the first 8 or 9 years, we paid on claims as scheduled—the debtor would file his petition and attach his schedules listing the creditors and addresses, with the product that was purchased and the amount due. I have changed that policy now and we require the filing of claims pursuant to section 57n within the 6-month period, and it is amazing to see how little the debtors know about what they owe, and as we see these claims come in, it is absolutely horrifying to find the high number of illegal and unconscionable aspects that should be disallowed.

But where is the money coming from to conduct any litigation in this court insofar as the debtor is concerned? He is impoverished. The trustee has no money, and the court has no money. I think this is the basic reason why the referees in bankruptcy say, "We don't want any part of chapter XIII, because it is too difficult for the court to conduct and administer a program that is fair and honorable."

So we have these problems, and it seems to me they should be resolved through corrective legislation in order that a fair, reasonable, and administratively convenient amortization program can be attained which attorneys and referees can process in good conscience for the

equal benefit of debtors and all creditors. I am fully satisfied that only by this approach will the desired objective be reached.

Mr. JACOBS. Thank you.

Professor Poulos and Professor Countryman, this committee finds itself in your debt very much, and I believe that there will be a number of questions that Mr. Poff will care to ask, and I think I would like to reserve questioning that I might make for now.

Congressman Poff?

Mr. POFF. Thank you, very much, Mr. Chairman. I will not have a great number of questions. They are addressed to Mr. Poulos.

First, referring to page 6, do you think the trustees should have the same powers in chapter XIII proceedings as they have in straight bankruptcy proceedings?

Mr. POULOS. There is no doubt in my mind that he should have.

Mr. POFF. Chapter XIII does not grant those explicitly, does it?

Mr. POULOS. No, there is only one court case that says the trustee does have such powers. I interpret the act that he does have such powers. It is a very controversial point.

Mr. POFF. If other referees were as bold as you are to experiment, they could increase the number of chapter XIII proceedings in their courts as well, couldn't they?

Mr. POULOS. Except that it takes anywhere from 60 to 75 hours a week and I incur quite a bit of scorn to sit there and make these decisions, and I wouldn't want most referees to endure that hardship.

Mr. POFF. It is not only a matter of personal courage, then, but an appetite for hard work, and I must say I commend you for—

Mr. POULOS. Excuse me. When you are involved in this type of work, you realize that something has to give, and I specialize on chapter XIII cases, and I have to neglect somewhat my straight bankruptcy work, and one of the aspects of the referee's position is its uniqueness. We are not dealing in a case where A is suing B. We are dealing with a case involving any number of conflicting interests, and it is very difficult for a conscientious referee to scrutinize these cases to see if there is fraud, and there is a terrific burden on him to see that these cases are administered properly, and if I am devoting my time to chapter XIII, I don't have time to devote to these other cases which are really just as important.

Mr. POFF. In the list of benefits to debtors which you outlined on pages 3 and 4 of your statement, your number A refers to the discharge.

I wonder if you would care to expand upon that a little. That question, of course, is in two parts, really: The discharge which is granted upon payment of all requirements under the plan, and those discharges which might be granted at the conclusion of the 3-year period notwithstanding that all payments have not been made.

Mr. POULOS. We have the 660 provision in the act which is full compliance, so if we have full compliance the discharge is academic except in those cases where the referees interpret the law that claims must be filed. So if we have a 6-months' provision where claims must be filed, then the discharge in our closing the case in accordance with 660 is very meaningful.

We also have provision 661, which is substantial compliance, that if a person has made a sincere effort and unusual circumstances

exist that he could not pay his bills, then I believe from my research we have the authority to give that person an effective discharge.

However, if the case is dismissed because of noncompliance, then he gets no discharge.

Mr. POFF. What is involved, of course, is the question of whether or not he can pay, is it not?

Mr. POULOS. On the part of the debtor?

Mr. POFF. Yes.

Mr. POULOS. Yes; that is true.

Mr. POFF. On page 7, your paragraph number 5—

Mr. POULOS. I have crossed that out. There are certain revisions I made. That is the *Perry* case.

Mr. POFF. May I say, that I have enjoyed Mr. Poulos' testimony and appreciate his statement. Thank you, Mr. Poulos.

Mr. POULOS. Thank you.

Mr. JACOBS. Mr. Wiggins?

Mr. WIGGINS. Yes.

Mr. Poulos, in your experience you have doubtless used many petitions for absolute discharge from bankruptcy, and many of those I expect you have felt should have been handled under the chapter XIII proceeding.

Is that true?

Mr. POULOS. In my experience now, we have around 52 or 53 percent of all our cases filed under chapter XIII. There is only a small percentage of cases that are now filed in straight bankruptcy that would really warrant any chapter XIII procedures, and the practice now is that the attorneys are pretty gun shy, that if they have a case that looks on its face as if it should be under XIII, they usually approach the court either in advance or come to the bench and they explain on the record that the client has been fully advised of the chapter XIII procedures, and that there are special circumstances as to why the person wishes to go through bankruptcy.

I go beyond that. I interrogate the bankrupt, and in most instances, we are fully satisfied that straight bankruptcy is the best answer.

Of course, there are a few cases where this happens, and the person should be in XIII, and in that area—there is no question about it—we are powerless to do anything about it.

Mr. WIGGINS. Do I understand that you feel it would be an unwarranted grant of power to give you the discretionary authority to transfer these?

Mr. POULOS. I do, Congressman, because I will interrogate a straight bankrupt. I may very well have him convinced that chapter XIII is the best remedy.

I tell the lawyer, "Talk with your client and see if you can't convert from straight bankruptcy."

If the attorney is not interested, he goes back and talks to his client and may give him reasons why he shouldn't go under XIII.

I have done that several times, and not one time has one of those persons come back to go through XIII.

Mr. WIGGINS. I think maybe the situation in your court is sufficiently unique that your experience and practice would not be generally applicable elsewhere, because the evidence we have received, and some of my own personal knowledge indicates that most referees are not

trying to drive petitioner into chapter XIII, they are just trying to get rid of their caseload every day, and not spending the time, 60 hours, as you are, to perhaps find a better way.

Have you had an opportunity to discuss with your colleagues who occupy similar positions whether or not in their opinion they would be able to use the discretionary authority that might be given them?

Mr. POULOS. Well, I haven't discussed it to any extent, but I have given some thought to it. My impression is that if any such legislation were enacted it would not be effective because the attorney is the key factor, and if the attorney is not sympathetic to chapter XIII, clients would come to him for relief under the Bankruptcy Act.

Very likely, if the attorney is uncertain about being able to prove that chapter XIII is not an adequate form of relief, he would advise his clients to come back in 2 or 3 months.

In the meantime, the clients would be instructed to accumulate sufficient money for a counsel fee and if additional bills were incurred, they would have a better chance of being allowed to go through straight bankruptcy.

I think this is an area where creditors could get hurt as a result of this legislation.

Mr. WIGGINS. Have you done anything special in your portion of Maine to acquaint the bar with the mechanics of the chapter XIII proceedings?

Mr. POULOS. I think from my statement—

Mr. WIGGINS. I realize what you have done in court, but perhaps with bar associations?

Mr. POULOS. No; we have not done that. We do not try to promote chapter XIII. We try to leave it entirely on a voluntary basis. Our greatest effort has been trying to simplify work for the attorneys. Once we have that simplified, the public is so interested in the program that they insist on going through that process.

Mr. WIGGINS. I think it is also something this committee should concern itself with, that we avoid hitting a man before he gets there in the first place, and trying to simplify the process for him after he gets there.

I fully agree with you that if one or two creditors insist on their pound of flesh now. They often place the man's job in jeopardy, and then his back is to the wall and then he must have some relief.

Now, what kind of exemption statutes are there in Maine that would protect a man's salary?

Mr. POULOS. Very poor. Maine is one of those States where a person can be imprisoned for his debts. As far as wage garnishment is concerned, I think the exemption is \$30, and in many instances companies have policies that if it happens more than twice he is automatically fired.

So a threat of wage attachment forces these people into bankruptcy.

Mr. WIGGINS. Yes, I believe that is true. These are not matters entirely in the jurisdiction of the Congress, but I would think that the policy of the employers to fire or threaten to fire employees because of an isolated garnishment proceeding should be a matter that is appropriately discussed by labor-management teams and made a matter of bargaining, if necessary, with some of the Nation's major employers to prevent the situation.

Also, exemption statutes for wages should be reviewed in all the 50 States to broaden their exemption, to place the burden on a prospective creditor.

They may not be able to look to a man's wages before the transaction is made.

Do you generally agree with that?

Mr. POULOS. Pretty much. I am not going to disagree with you, but this is not just the only area about which I am concerned.

When we look at these bankruptcy cases over a period of years, we sit back and reflect on the matter, "Why are these people coming into this court?" And after some more consideration, I have concluded that it is because of the high cost of credit on long-term indebtedness on unusually large amounts of money.

There was a study back in the 1930's by the Russell Sage Foundation, the Department of Commerce, and the Department of Justice under Solicitor General Thacher, which showed that in many instances people owed as many as four or five small loan companies at a time, so as much as 20 percent of their income was applied to interest alone, that in many instances the monthly installment for interest and principal was greater than their monthly income, so if this continues on for any length of time, their financial strength is so sapped that if anything happened, such as a pregnancy or divorce or wage attachment these people need immediate relief.

You talk about employers not firing people, or possibly improving the exemption laws. That is just a small part of it.

When chapter XIII was originally conceived in 1932, the idea was that as soon as a person had a sufficient number of bills that rather than go to the consumer finance industry for purposes of consolidation, that he should go into the bankruptcy court under chapter XIII.

If, however, unfortunately he did become involved to the extent that a lot of his income was being applied to interest, that chapter XIII should be sufficiently broad to see to it that the interest stopped so that the principal could be repaid.

Mr. WIGGINS. I have just two other questions, sir.

Did I understand your answer to Congressman Poff's question that it is your practice that if a debtor under chapter XIII in your judgment willfully is not complying with the plan that he should be denied discharge?

Mr. POULOS. We do not permit wage earners to use the Federal court as a shield against creditors. We have an elaborate system to assure prompt and regular payments. We have a young man who spends all his time reviewing these cases on a weekly basis, and if he sees a person has not made his weekly payment, immediately a letter goes out asking why.

Our procedure is such that a second letter goes out if no payment comes in.

The third time, there is a petition to dismiss, and if they don't show up, those petitions are allowed by default.

If they do show up, we try to find out why he didn't inform us of his difficulty, his problem.

At that time, if a person is acting in good faith, we—

Mr. WIGGINS. Does that petition bar a subsequent petition, sir?

Mr. POULOS. Not legally. We had one person who filed about five or six petitions under chapter XIII within a period of 5 years, but I am not going to tolerate any wage earners abusing the system, so if they come in once, unless there have been unusual circumstances, I then rule, after the case may be accepted by creditors that this is not a feasible proceeding, and the case is dismissed.

I won't confirm it.

Mr. WIGGINS. What if he comes back with a petition for absolute discharge?

Mr. POULOS. He would be under the 6-year provision.

Mr. WIGGINS. And if he is not?

Mr. POULOS. Then he goes through bankruptcy.

Mr. WIGGINS. Has your practice in Maine required additional staffing in your court to handle all of these works that you testified to? And if so, do you have any experience on the added cost of administrative expenses?

Mr. POULOS. That is a very good question.

As far as court staff is concerned, the answer is none. As far as the trustee is concerned, however, some additional staffing has been required. In addition to the regular three clerks, an assistant has been retained to supervise the office in his absence and to make sure that the wage earners are making their payments regularly. Moreover, we have an unusual situation in Maine where the trustee has had to hire three or four counsel to assist him in reviews before the district court and eventually the court of appeals on questions of vast importance in wage earner proceedings.

Also, in complying with the guidelines and consensus of the Judicial Conference, certified accountants have been retained to make an unqualified certified audit of the trustee's affairs. Lastly, our program results in additional costs for appraisal of real and personal property and a court stenographer.

In one way or another, the entire cost for these services is paid by the wage earners. Around \$1 per month per case is deducted from the periodic payments made by the wage earner to satisfy the terms of the plan. A great part of the costs, however, are now defrayed from the interest earned from time deposits of undistributed money. Last year we earned \$9,000 from that source, which was used to finance some of the pending litigation.

Mr. WIGGINS. Has it been adequate except for the extraordinary fact of the litigation—

Mr. POULOS. If we do not have expensive litigation, I would say the trustee needs a staff of five people and no more, and once this litigation is over, I think we will be able to process these cases very, very simply at a very low cost of administration.

Mr. WIGGINS. Do you know what your administrative expenses are—

Mr. POULOS. Chapter XIII?

Mr. WIGGINS. Yes.

Mr. POULOS. Thirteen percent.

Mr. WIGGINS. How does that compare with other courts, sir?

Mr. POULOS. It corresponds to costs of 20 percent existing in other areas. One reason ours is lower is that I don't pay counsel that much money. In one area they allow a counsel fee of \$200, and there is no significant increase in chapter XIII cases.

Mr. WIGGINS. Thank you very much for your testimony.

Mr. JACOBS. Mr. McClory?

Mr. McCLORY. Thank you, Mr. Chairman.

I was very favorably impressed by your statement, Judge Poulos, and also because of the constructive suggestion that you make for the better operation of chapter XIII.

Also, I can comment on the very good showing, the very favorable utilization of chapter XIII that you have made in your court and in the State of Maine.

Earlier testimony before the committee indicated that counsel were reluctant to utilize chapter XIII because of the complications of the factors to which you made reference, sir. Also it was charged that there was a desire for attorneys to get their fee and get out of the case, and so there was a tendency to recommend and utilize straight bankruptcy.

Certainly, I think that any condition like that should be overcome by recommending an appropriate practice that can be followed, such as the practice that you have adopted of using the services of a trustee who is knowledgeable with regard to this subject.

I gather that useful legislative changes, or, at least, changes in court rules or practices could be adopted through the pattern which is set in the Maine courts.

Mr. POULOS. It may be of interest to you, Congressman, that really, the legislative history of chapter XIII—as I pointed out, this was conceived in 1932, and the first use of XIII was in Birmingham, Ala., where a judge, practically on the following day of enactment of section 74, appointed a special referee, Valentine Nesbitt, and he employed pretty much the principles which I have followed, and it was unfortunate that the National Bankruptcy Conference when they were so extensively involved in studying and redrafting the amendments which led to the enactment of the Chandler Act, took the basic principles of chapter XIII as developed by Referee Nesbitt and adapted those principles to the terminology and structure of chapter XI.

I think that was one of the bad mistakes that was made. It complicated this procedure so much that attorneys are reluctant to get involved in such a technical procedure.

Mr. McCLORY. Mr. Countryman, I would like to comment on your statement, as well, and state that as one member of the committee, I will look forward to receiving the legislative proposals which you say are forthcoming from you in the next few days. I assume that these are the recommendations of the National Bankruptcy Conference?

Mr. COUNTRYMAN. They will be, sir; yes.

Mr. McCLORY. I wanted to ask about this: You make reference to some figures and percentages in your statement that, for instance, the increase in consumer borrowing has gone up from \$8 billion to \$94 billion, and that disposable income has increased from \$147 billion to \$505 billion. And then you state that this indicates that consumer resources are not keeping pace with consumer credit commitments.

I note the increase in consumer credit is \$86 billion, and these consumers have four and a half times as much money as they had at the time that this period started.

Do you think that it has to increase percentage-wise each time?

Mr. COUNTRYMAN. Well, of course, disposable consumer income goes to all expenditures after taxes which a consumer has, and it seems obvious to me that if consumer credit alone is going up 10 times, and disposable income is going up—I made it slightly over three, but it may be four and a half—

Mr. McCLORY. The dollar amount is going up four and a half times, while the percentage increase is going up this large amount.

Is that dangerous, do you think?

Mr. COUNTRYMAN. It seems to me obvious that there is not a proportionate increase in the amount of money which the consumer has to pay off the credit.

Actually the interest alone on this consumer credit is now about \$13 billion a year, and it does seem obvious to me that consumers are committing a much larger proportion of their total disposable income to repaying consumer credit than they ever did before, and that this increase is proceeding apace year after year.

I don't offer this as a complete solution. As I said in my statement, this is a matter that needs much more study.

Mr. McCLORY. Is there another way to buy these products, or do you think we should buy fewer automobiles, television sets, and appliances?

Mr. COUNTRYMAN. I think fewer of them should not be bought. It might not appeal to the sellers.

Mr. McCLORY. How about the Administration? This is deflationary, isn't it?

Mr. COUNTRYMAN. They probably won't like it.

I have been told by a number of executive officers of small-loan companies that one of the most serious problems in bankruptcies is that other small-loan companies, never the one I am talking to, will continue to loan money to a man after it is perfectly obvious that he is no longer a good credit risk, and that way he is saddled with such debt that chapter XIII is not feasible.

If you look at the files of bankruptcy cases such as Referee Poulos sees everyday—

Mr. McCLORY. Do you know what the percentage of loss is on these small-loan companies?

Mr. COUNTRYMAN. Yes, sir; in a general way and close enough way, I have seen many reports in the Wall Street Journal about what the industry tells itself about its percentage of loss, I have interviewed many of them and asked them what percentage of their total receivables, total outstanding loans must be written off as bad debts, and I have never gotten an estimate of higher than one-half of 1 percent, and I have gotten many lower than that, down to .2 of 1 percent, so I don't believe that it is a serious problem for the lending industry save that they quite understandably hate to lose any, but in terms of the number of bankrupts we are talking about, and I think we ought to multiply the number of bankruptcies by four to take account of their families; it is a serious problem for them.

Mr. McCLORY. I am afraid the junior representatives would be very discouraged if the committee were to take action which would reduce the number of automobiles which are produced by the UAW-CIO, and appliances, and I want to make this observation in commenting on your testimony that we are trying to produce something that is constructive here, and therefore, I, for one, will welcome the recommendations from your conference.

Mr. COUNTRYMAN. Thank you, sir.

Mr. JACOBS. The chair wishes to thank the witness for appearing and express his own judgment that your testimony has been enhanced by the clarity of it and therefore I think your testimony has been most beneficial.

Professor Countryman, there is a bill before Congress now which, I must confess, is in my other committee, concerning the outlawing of so-called professional credit advisers.

I wonder if you had an opinion about such legislation and, if so, sir, whether you would care to share it.

Mr. COUNTRYMAN. These are the debt poolers. Yes, on the whole I think that is a rather overheroic remedy, Mr. Congressman, which is inspired by many of the abuses of which some of the professional debt poolers have been guilty, but I would rather see an attempt to regulate the abuse than to abolish this type of service, because I believe most debtors need that sort of service.

In some communities they can get it from community supported agencies, but in a very great number of communities they cannot.

I know that a number of States have adopted legislation outlawing debt pooling entirely or defining it as the practice of law so that no one but attorneys can do it.

As I say, I think the remedy goes too far, and that a better remedy would be to regulate against abuse than prevent what seems to me on the whole to be an essential and desirable service.

Mr. JACOBS. Referee Poulos, would you care to comment on that point, as to whether, for example, any such professional or so-called professional service of that kind would be of benefit to your administration?

Mr. POULOS. I think it would be very much.

I pretty well agree with Professor Countryman on this, but under no circumstances should this debt pooling operation be exclusive, because the organization, although it can counsel and help people in that area and possibly avoid their getting into serious financial difficulties and ending up in bankruptcy court, nevertheless they are not completely empowered to disallow usury or other things along that line.

Mr. JACOBS. Again, on behalf of the committee, I wish to thank both of the witnesses.

(The following materials were subsequently submitted for inclusion in the record by Professor Countryman:)

LAW SCHOOL OF HARVARD UNIVERSITY,
Cambridge, Mass., June 5, 1967.

Mr. BENJAMIN L. ZELENKO,
Counsel, U.S. House of Representatives, Committee on the Judiciary, Rayburn
House Office Building, Washington, D.C.

DEAR BEN: I enclose the proposals of the National Bankruptcy Conference for amendments to Chapter XIII to which I referred in my testimony of May 25. You will recall that in my testimony I referred to three substantial changes proposed in Chapter XIII. As is usually the case, some peripheral adjustments are also necessary. The attached proposals covers both.

The substantial changes are:

(1) New § 647(1), which would authorize the court, where deficiency claims are presented, to determine the value of security sold and fix the amount of the deficiency claim on the basis of that valuation or the sale price, whichever is higher.

(2) New § 647(2) which would authorize the court to limit or disallow unconscionable claims. The language of this subsection is taken from § 2-302(1) of the Uniform Commercial Code.

(3) New § 652(b)(1), authorizing the court to dispense with the consent otherwise required from any creditor or class of creditors if it finds that the plan fairly provides for such creditor or class of creditors in view of their comparative claims upon the debtor's property and future earnings of the debtor. The idea underlying this subsection is borrowed from §§ 77e and 216(7) of the Bankruptcy Act.

The peripheral changes are as follows:

(1) Clarification of § 614 as to the court's power to enjoin actions to enforce claims and to make clear that actions to enforce secured claims which are neither dealt with by the plan nor excluded as unconscionable shall not be stayed after a plan is confirmed save on the condition that the debtor thereafter complies with the terms of the secured debt.

(2) Amendment of § 652a(1) [formerly § 652(1)] to provide for voting by classes of secured creditors. Since the court might under new § 647(2) find that a claim was unconscionable against other creditors, whether or not unconscionable against the debtor, the proper way to "avoid any unconscionable result" under that subsection might be to subordinate the overreaching creditor's claim to those of other creditors. Hence, it is necessary to provide for classes of unsecured creditors.

(3) Section 652(b)(2) is merely clarifying—if a secured creditor does not consent to the plan and the necessity for his consent is not eliminated under § 652(b)(1), his claim is not to be dealt with by the plan.

(4) Section 652(c) is thought desirable to make clear that where a secured claim is dealt with by a plan, but the plan is not fully performed, the secured claim shall not thereafter be affected by the plan or by any discharge granted the debtor pursuant to § 661 on a finding that the debtor's failure to perform was "due to circumstances for which he could not be justly held accountable."

(5) Sections 660 and 661 are amended to make clear that any discharges granted in Chapter XIII proceedings will cover not only claims dealt with by the plan but also claims excluded from the plan as unconscionable.

(6) Section 661 is also amended, in conformity with the Supreme Court's opinion in *Penny v. Commerce Loan Co.*, 383 U.S. 392 (1966), to make clear that while a debtor who fully pays his debts under an extension plan may be discharged under § 660 despite a prior straight bankruptcy discharge in a proceeding initiated within the previous six years, a debtor who has received such a prior straight bankruptcy discharge and who fails fully to perform under an extension plan may not be granted a discharge under § 661 on a finding that his failure to perform "was due to circumstances for which he could not be justly held accountable."

(7) Section 666 in its present form provides for disposition of the proceedings if the plan is not accepted by creditors. Since new § 652(b)(1) would authorize the court to dispense with the consent otherwise required in some circumstances, it is necessary to amend § 666 so that it refers only to a lack of consent by those creditors whose consent is required under § 652.

In view of my testimony about the relationship between the rise in consumer credit and the rise in bankruptcy proceedings, and the doubt expressed on this point by Congressman McClory, I would be grateful if the enclosed clipping from the *Wall Street Journal* could be included in the record of the hearing.

If I can be of any further assistance, please do not hesitate to call on me.

Best regards,

VERN COUNTRYMAN,
Professor of Law.

SEC. 614. The court may, in addition to the relief provided by section 11 of this Act and elsewhere under this chapter, enjoin [or stay] until final decree the commencement or continuation of suits in *any jurisdiction on all claims against the debtor, including those not dealt with by and those excluded from the plan.* [other than suits to enforce liens upon the property of a debtor, and] *but the court may, only upon notice and for cause shown, enjoin [or stay] until final decree any act or the commencement or continuation of any proceeding to enforce any lien upon the real or personal property of a debtor. Such injunction of any act or proceeding to enforce a lien not dealt with by the plan and not excluded therefrom pursuant to paragraph (2) of section 647 of this Act may be continued after confirmation of the plan only upon condition that the debtor shall, (1) in such manner and at such time as the court may fix, make all payments on the secured debt which became due without acceleration*

before confirmation, and (2) comply with the security agreement or applicable law as to payments becoming due thereafter without acceleration.

SEC. 647. Notwithstanding section 646 of this Act—

(1) where a deficiency claim is proved by any secured creditor who has enforced his security by sale of his collateral before or after the filing of the petition, the court shall, on application by the debtor and after hearing upon notice to such creditor, determine the fair value of the collateral at the date of sale and allow the deficiency claim only in the amount by which the indebtedness with interest and costs exceeds the fair value of the collateral or the sale price, whichever is higher; and

(2) on application by the debtor and after hearing upon notice to the creditor concerned, the court may determine that a claim, secured or unsecured, is unconscionable or contains unconscionable terms, and may disallow such claim and order it excluded from the plan, or allow the claim without the unconscionable terms, or so limit the claim as to avoid any unconscionable result.

SEC. 652. *a.* If a plan has not been so accepted, an application for the confirmation of the plan may be filed with the court within such time as the court shall have fixed in the notice of such meeting, or at or after such meeting and after, but not before—

(1) it has been accepted in writing by each secured creditor whose claim is dealt with by the plan and, (a) if unsecured creditors are [affected] dealt with generally by the plan, by a majority in number and amount of all such creditors whose claims [have been] are proved and allowed before the conclusion of the meeting [which number shall represent a majority in amount of such claims, and], or (b) if unsecured creditors or classes of such creditors are dealt with separately by the plan, by each such creditor separately dealt with, or by a majority in number and amount of each class of such creditors separately dealt with, whose claims are proved and allowed before the conclusion of the meeting. [by the secured creditors whose claims are dealt with by the plan]; and

(2) the debtor has made the deposit of moneys required of him under this chapter and under the plan.

b. Notwithstanding paragraph (1) of subdivision *a* of this section—

(1) the court may confirm the plan without the acceptance of any creditor or class of creditors if it finds that the plan adequately provides for the realization by such creditor or class of creditors of the value of its claim or claims against the property and future earnings of the debtor and provides for equal treatment for each creditor of the same class; but

(2) if a secured creditor does not accept the plan and the court does not make a finding pursuant to paragraph (1) of this subdivision that the plan adequately provides for the realization of the value of this claim, the provisions of the plan dealing with his rights shall be excluded from the plan and he shall not be deemed to be affected thereby.

c. If the debtor defaults in any of the terms of a plan which deals with secured debt, or if such plan terminates by reason of the happening of a condition specified in the plan, the rights of any secured creditor in his collateral shall not thereafter be affected by the plan or by any discharge granted in the proceeding pursuant to section 661 of this Act.

SEC. 660. Upon compliance by the debtor with the provisions of the plan and upon completion of all payments to be made thereunder, the court shall enter an order discharging the debtor from all his debts and liabilities provided for by the plan or excluded from the plan pursuant to section 647 of this Act, but excluding from the order of discharge such debts as are not dischargeable under section 17 of this Act held by creditors who have not accepted the plan.

SEC. 661. If at the expiration of three years after the confirmation of a plan the debtor has not completed his payments thereunder, the court may nevertheless, upon the application of the debtor and after hearing upon notice, if satisfied that the failure of the debtor to complete his payments was due to circumstances for which he could not be justly held accountable, enter an order discharging the debtor from all his debts and liabilities provided for by the plan or excluded from the plan pursuant to section 647 of this Act, but excluding from the order of discharge such debts as are not dischargeable under section 17 of this Act held by creditors who have not accepted the plan. The court shall nevertheless not order a discharge under this section if clause (5) of subdivision *c* of section 14 of this Act would have barred a discharge in a bankruptcy proceeding initiated on the date of the petition filed under this chapter.

SEC. 666. If the statement of the executory contracts and the schedules and statement of affairs, as provided by [paragraph (1)] *subdivision a* of section 624 of this Act, are not duly filed, or if a plan is not proposed at the meeting of creditors or within such further time as the court may fix, or if the plan is withdrawn or abandoned prior to its acceptance, or if the plan is not accepted *by those creditors whose acceptance is required under section 652 of this Act* at the meeting of creditors or within such further time as the court may fix, or if the deposit required under this chapter and under the plan is not made or the application for confirmation is not filed within the time fixed by the court, or if confirmation of the plan is refused, or if after confirmation [,] a debtor defaults in any of the terms of the plan, or if the plan terminates by reason of the happening of a condition specified in the plan, the court shall— . . .

LAW SCHOOL OF HARVARD UNIVERSITY,
Cambridge, Mass., July 19, 1967.

HON. BYRON G. ROGERS,
U.S. House of Representatives,
Washington, D.C.

DEAR REPRESENTATIVE ROGERS: During my testimony on behalf of the National Bankruptcy Conference in opposition to H.R. 1507 and 5771 before your subcommittee on May 25, I suggested that the nearly twentyfold increase in consumer bankruptcies from 1946 to 1966 (from 8,500 to almost 176,000) was apparently closely related to the following developments during the same twenty-one year period, as reported by the Federal Reserve Board:

(1) Consumer credit, exclusive of home mortgages, has undergone a more than tenfold increase (from \$8.38 billions to \$94.8 billions).

(2) Home mortgages have undergone a corresponding increase (from \$23 billions to \$225.4 billions).

(3) Disposable personal income after taxes has only more than trebled (from \$147 billions to \$505.3 billions).

From this I concluded that consumer resources have not kept pace with consumer credit commitments.

Shortly after the hearings closed, I read an account in the May 31 *Wall Street Journal* of a study of the relation of family debt service to family income made by Mr. John A. Gorman, Associate Chief, National Income Division, U.S. Department of Commerce, which demonstrated that the average debt service obligations had gone from 11% of average family income in 1949 to 22% in 1966. I sent the *Wall Street Journal* article to Mr. Zelenko, with the request that it be included in the record of the hearing.

Since that time I have been in touch with Mr. Gorman for more complete data, which he has kindly supplied with the advice that his data has also been revised since publication in the *Journal* to take account of revisions in national income accounts.

From the data supplied to me by Mr. Gorman for the years 1949 through 1966, and from my own calculations for the years 1946 through 1948, I have compiled the enclosed two-page Table. That Table demonstrates that, although the total disposable personal income after taxes has more than trebled during the past twenty-one years, the percentage of family income committed to consumer debt service has also more than trebled—from 6% to 22%. I would be most grateful if this Table could also be included in the record of the hearings.

It seems obvious, Mr. Chairman, that while consumer bankruptcies have grown apace, so have consumer credit commitments. I find these facts difficult to reconcile with the argument that the increase in consumer bankruptcies constitutes a grave threat to the foundations of consumer credit. At the hearings, in response to an inquiry, I hazarded an estimate that bad debt losses on consumer credit do not amount to $\frac{1}{2}$ of 1%. I would be surprised if the supporters of H.R. 1057 and H.R. 5771—essentially, the extenders of consumer credit—could prove me wrong.

At this point, I say that they have not made their case. And they should be required to make it before we abandon our long-standing policy of relief and rehabilitation for honest debtors and substitute for it a three-year period of involuntary bondage.

Thank you for your consideration.

Sincerely,

VERN COUNTRYMAN,
Professor of Law.

FAMILY DEBT SERVICE AND INCOME

[In millions of dollars]

	Debt service				
	Debt retirement		Interest		Total
	Consumer credit	Home mortgages	Consumer credit	Home mortgages	
1946	6,582	1,788	602	1,219	10,191
1947	9,878	2,163	965	1,385	14,391
1948	12,748	2,606	1,372	1,606	18,332
1949	14,829	3,042	1,694	1,798	21,363
1950	17,552	3,378	2,199	2,073	25,202
1951	22,005	4,227	2,443	2,448	31,123
1952	24,260	4,697	2,820	2,779	34,556
1953	26,491	5,097	3,552	3,106	38,246
1954	28,911	5,361	3,786	3,590	41,648
1955	31,754	5,790	4,388	4,150	46,082
1956	34,807	6,712	5,062	4,774	51,355
1957	37,438	7,520	5,449	5,447	55,854
1958	37,901	8,159	5,553	6,102	57,715
1959	40,076	8,700	6,053	6,934	61,763
1960	43,129	9,207	6,844	7,893	67,073
1961	44,728	10,111	7,055	8,900	70,794
1962	47,397	11,113	7,557	9,956	76,023
1963	51,622	12,300	8,415	11,132	83,469
1964	57,188	13,400	9,447	12,383	92,418
1965	63,185	14,300	10,607	13,826	101,918
1966	68,167	15,300	11,921	15,170	110,558

FAMILY DEBT SERVICE AND INCOME

	Number of families ¹	Average family income	Average debt service	Debt service as percent of income
1946	43,300,000	\$3,696	\$235	6
1947	44,700,000	3,799	321	8
1948	46,300,000	4,085	396	10
1949	47,800,000	3,945	447	11
1950	48,900,000	4,232	515	12
1951	49,500,000	4,577	629	14
1952	50,200,000	4,747	688	15
1953	50,500,000	5,001	757	15
1954	51,200,000	5,028	813	16
1955	52,200,000	5,275	883	17
1956	52,800,000	5,553	973	18
1957	53,600,000	5,756	1,042	18
1958	54,600,000	5,839	1,057	18
1959	55,300,000	6,100	1,117	18
1960	56,100,000	6,240	1,196	19
1961	57,300,000	6,360	1,235	19
1962	57,900,000	6,654	1,313	20
1963	58,400,000	6,930	1,430	21
1964	59,500,000	7,325	1,553	21
1965	60,300,000	7,780	1,690	22
1966	60,900,000	8,300	1,833	22

¹ Includes unattached individuals.

[From the Wall Street Journal, May 31, 1967]

WORRY OVER DEBT—PAYMENTS ON BORROWING EAT UP A GROWING PART OF CONSUMERS' INCOME—SOME ANALYSTS FEAR TREND COULD DAMPEN BUSINESS; LOAN DELINQUENCIES RISE

(By Alfred L. Malabre, Jr.)

WHO HOLDS ALL THE SAVINGS?

NEW YORK.—“A high level of consumer debt usually causes no difficulty if business is expanding. The trouble begins when you have a recession.”

A senior economist at the nonprofit National Bureau of Economic Research here made this comment almost three years ago. At the time, the overall debt burden of American consumers was expanding rapidly, giving rise to fears that such borrowing was getting out of hand. The economy, however, also was expand-

ing rapidly then, and so most business analysis expressed little immediate concern about the debt situation.

But times change. Today's economy no longer expands rapidly. The latest figures indicate, in fact, that the long business expansion well may have ended last year. Gross national product, the nation's total output of goods and services, declined slightly in the first quarter, after eliminating "growth" due to higher prices. Moreover, economists generally detect no evidence of any economic revival in the current quarter.

In this new environment, is the relatively high level of consumer debt becoming an economic handicap that could aggravate any recession?

A DAMPENING INFLUENCE

An increasing number of economists in and out of Government believe so. These analysts fear that consumer debt in coming months may exert a dampening influence on economic activity. They anticipate a time in the months ahead when consumer incomes may no longer be rising so rapidly, if at all. And they conclude that consumers, in such circumstances, may have considerable trouble paying off their debts and may be highly reluctant to contract new ones, or even to spend their cash.

For example, Avram Kisselgoff, chief economist for Allied Chemical Corp., feels there is "no doubt that the role of consumer debt will be increasingly to restrain economic growth" as the year goes on. Mr. Kisselgoff expects that sales of such durable goods as autos and appliances will be particularly hurt by the debt load. Traditionally, the economist explains, families burdened by heavy debt payments tend to cut back first on purchases of goods that may not be urgently needed, such as a new car or a new television set.

How much of a burden has consumer debt become?

A recent unpublished study by John Gorman, a Commerce Department economist, suggests that debt is an ever-increasing burden for Americans. The trend is traced in the table below. The figures, based on Mr. Gorman's study, show the portion of consumers' after-tax income being taken up by interest charges and repayments on mortgages and instalment loans. Pre-World War II figures for this debt "servicing" are not available.

	Average family income	Average debt service	Debt service as percent of income
1966.....	\$8,300	\$1,833	22.0
1965.....	7,780	1,690	21.7
1964.....	7,325	1,553	21.2
1961.....	6,220	1,223	19.6
1958.....	5,670	1,044	18.4
1955.....	5,090	870	17.0
1952.....	4,570	679	14.8
1949.....	3,860	441	11.4

Mr. Gorman estimates that "well over 75%" of last year's debt service figure represents payments on debt contracted in previous years. This situation, the economist says, helps explain the continuing rise of the debt service level through last year's tight money period, in which loans generally were harder to obtain. Mr. Gorman expects that the debt service figure will continue to increase through 1967, both in absolute terms and as a percentage of family income. But he guesses that the dollar increase will be smaller than in recent years.

There already is evidence that consumers are becoming more cautious about debt. In March, the latest month available, consumer installment credit outstanding climbed at an annual rate of less than \$3.2 billion, after adjustment for seasonal factors. This gain was down sharply from an annual rate of increase of nearly \$8 billion in March 1966. Some economists predict, moreover, that total credit outstanding will actually begin to decline later this year. The last time such a decline occurred was in early 1961, near the bottom of the 1960-61 recession.

REFINANCING HOMES

Another indication of consumer reluctance to take on new debt, some analysts say, is an apparent decline in the number of Americans resorting to mortgaging their homes to finance purchases of non-housing items. Through the early years of this decade, home mortgage borrowing climbed sharply while actual spending for new homes changed little from year to year. This trend suggested to economists that increasingly consumers were refinancing their homes to get funds for purchases of everything from autos to pleasure boats. Recently, however, the trend of mortgage borrowing has closely followed the trend of new-home spending, analysts note.

Many economists caution that any leveling off or decline in consumers' income could cause debt service, as a percentage of family income, to balloon in coming months—however hesitant consumers may become to take on new debt. As an economist at New York's First National City Bank observes: "Many consumers are locked in by their previous borrowing, whatever happens to their earnings this year."

To be sure, consumer income continues to rise. In April, the income level reached a record annual rate of \$614.1 billion, seasonally adjusted. However, the March-to-April rate, increase of \$1.4 billion was the smallest month-to-month gain in more than a year. Between February and March, the income level climbed more than twice as much as in the latest period.

At the same time, some economists note, there are growing signs that consumers are running into more trouble trying to keep up with their loan repayment schedules. A survey by the American Bankers Association shows that consumers were 30 days or more behind in payments on 1.75% of instalment bank loans outstanding at the end of April. This was the highest April "delinquency rate" since 1961, near the low point of the 1960-61 recession. The rate in April 1966 was 1.64%. An officer at Chase Manhattan Bank here comments: "Consumers obviously are pretty well loaned up."

The consumer debt situation would be much more of a problem if the unemployment rate were not so low. At 3.7% of the labor force in mid-April, U.S. joblessness has been holding at an unusually low level, most analysts agree. In the early 1960s, the rate remained above the 5% level. If joblessness should begin to climb in coming months, as some economists fear may happen, consumer debt problems would rapidly worsen.

"The low unemployment rate has tended to keep consumer debt from becoming a much bigger problem," remarks Alan Greenspan, president of Townsend-Greenspan & Co., a New York-based business consultant.

The unemployment situation, some analysts say, will depend to a great extent on what happens in the Vietnam war. These analysts contend that unemployment would probably be starting to climb now if the war weren't going on. They argue that expanding Government spending on the war is keeping U.S. economic activity at an artificially high level.

Allied Chemical's Mr. Kisselgoff comments: "If we didn't have such enormous spending for Vietnam, we would have a full-fledged recession on our hands right now." It should be added, of course, that most economists are convinced that in the long run the economic benefits of peace in Vietnam would far outweigh any short-term problems caused by a curtailment of military spending.

Some economists who are relatively unconcerned about the rise of consumer debt note that consumer savings also have climbed substantially in recent months. In the first quarter of this year, consumers' savings amounted to 6.5% of consumers' after-tax income, considerably higher than the 5.9% rate in the previous three months.

Other analysts, however, contend that the people who hold most of the savings are not the same individuals who are in debt. Statistics that would confirm this theory are sketchy, but a study by the Survey Research Center of the University of Michigan suggests that savings in the U.S. indeed are highly concentrated. Half the nation's 60 million families have less than \$1,000 in savings, even including stocks and bonds, the center found in a survey conducted late last year. And only 16% of U.S. families have more than \$10,000 in such savings.

"Most of the persons in debt have little savings," concludes George Katona, head of the center. "Savings in this country continue to be highly concentrated."

The next witness is Mr. Andrew J. Biemiller, director of the department of legislation for the AFL-CIO, and the witnesses who are here on behalf of Mr. Biemiller, will you identify yourselves?

Mr. DOHERTY. First of all, I am James F. Doherty, and on behalf of Mr. Biemiller, I would like to apologize for his inability to be here, but he is involved with the pending railroad dispute.

Mr. JACOBS. We take notice of that.

Mr. DOHERTY. I am accompanied here by Miss Anne Draper, who is an economist with the AFL-CIO, and Miss Evelyn Dubrow, who is the chairman of the AFL-CIO consumers committee and also a legislative representative with the International Ladies Garments Workers Union.

STATEMENT OF JAMES F. DOHERTY, LEGISLATIVE REPRESENTATIVE, AFL-CIO, ACCOMPANIED BY ANNE DRAPER, ECONOMIST, AFL-CIO, AND EVELYN DUBROW, LEGISLATIVE REPRESENTATIVE, ILGWU AND AFL-CIO CONSUMERS COMMITTEE

Mr. DOHERTY. Mr. Chairman, my name is James F. Doherty. I am appearing today in opposition to H.R. 1057, a bill to amend the Bankruptcy Act with respect to the use of chapter XIII.

Mr. Chairman, this bill would foreclose a wage earner from obtaining the benefit of a discharge in bankruptcy unless he can prove that he is unable to make a chapter XIII arrangement to pay his debts out of future earnings.

Since we in the AFL-CIO represent 13.5 million wage earners and their families, we feel it our duty to inform the Congress of our strong feelings about the bill. Our responsibility is emphasized by 1963 Northwestern National Life Insurance survey, which shows that the typical bankrupt grosses between \$4,000 and \$6,000 a year. In short, the typical bankrupt is a worker.

Our obligations rest in three main categories. The bill contrary to the principles of our bankruptcy laws, precludes an honest debtor from a discharge of the burdens of his debt. The bill discriminates against a wage earner, denying him privileges which are left available to all other debtors including corporations.

Lastly, the bill does not cure the economic evil of supereasy credit, the dominant cause of wage earner bankruptcy, but encourages easier credit still by placing another collection weapon in the hands of the already too-heavily armed creditor.

The bill prevents an affected wage earner from exercising his rights to a discharge of his debts.

According to one leading authority, the bankruptcy law of the United States has for its fundamental object, "the securing of possession of an insolvent's assets and the procuring of their equitable division among creditors, preventing and avoiding attempts of one creditor to obtain unfair advantage over other creditors therein; and second, the liberation of worthy debtors from the burden of unpaid debts."

The idea of "liberation of worthy debtors from the burden of unpaid debts" as an essential purpose of bankruptcy is ingrained in our law. It operates, as the Supreme Court said in a 1918 decision "to aid the unfortunate debtor by giving him a fresh start in life."

The Court went on to note that "(Its) decisions lay a great stress on this feature of the law."

H.R. 1057 would deny to this single underprivileged overburdened class of debtors—the wage earners—their right to one fundamental purpose of the act.

H.R. 1057 says to the wage earner, "If you can pay your debts from your future earnings you shall not be discharged in bankruptcy." To so preclude the worker from his right, while preserving it inviolate to the fictitious corporation, the proprietor, the partner, the farmer, the professional man, would cast our bankruptcy law almost back to its origin—the debtors prison.

Mr. Chairman, we believe that men have a moral obligation to pay their debts. But our law recognizes that this obligation cannot always be met because of other considerations and that in due time the legal obligation may diminish. That is why, Mr. Chairman, our law does not require dire insolvency as a condition of bankruptcy. The petition needs only to allege that the debtor has debts he cannot pay.

Of course, there are abuses. There have no doubt been cases brought before the committee of persons with irresponsible debts and a clear and unfettered ability to pay them from future earnings. But it is repugnant to the AFL-CIO and our system of law itself that the abuse of a right by some should result in the denial of the right to all.

The coercive feature of the proposed legislation raises a serious issue of an individual's right to privacy, not present so long as a chapter XIII plan is purely voluntarily. The court not only protects the wage earner against harassment but equally important it assumes complete management of the wage earner's personal financial affairs.

The debtor and his family, in effect, become a ward of the court. If such an arrangement is coercive rather than voluntary, the debtor is reduced to the status of a minor or mental incompetent without adjudication as such. We suggest that this raises serious questions of personal liberties and rights.

I have already touched upon the discriminatory aspect of H.R. 1057. Briefly, the bill applies only to wage earners. They are denied straight bankruptcy on failure of a burden to show inability to comply with a chapter XIII arrangement.

But the fictitious corporate and non-wage-earner debtors may avail themselves of straight bankruptcy without obligation to the appropriate chapter and arrangement. Were not the responsible officers of the corporation or the nonwage earner just as liable for the detriment of the creditors?

I hasten to assure the committee that we do not challenge their rights under the system. We simply want to preserve the status for the wage earner.

This gross discrimination becomes more stark when the situation is looked at in another light. Under a chapter XI or chapter XIII arrangement a debtor may abandon the whole deal and revert back to straight bankruptcy on any fraudless motive, as he should be able to. But we wonder, Doesn't H.R. 1057 forbid this since it virtually precludes straight bankruptcy in the first place? We think it does.

I want to emphasize that our opposition to H.R. 1057 should not be construed as opposition to chapter XIII itself. The whole thrust of chapter XIII is to give the able and conscientious debtor the voluntary means to pay his just debts.

Indeed, our 28,000 debtors opted chapter XIII in fiscal 1966 and based on present unofficial estimates some 32,000 will do so in fiscal 1967.

We insist, however, that chapter XIII be kept purely optional lest it become, as is proposed, perverted from a protective and rehabilitative mechanism to relieve debtors into a coercive collection method to relieve creditors.

Finally, we suggest that H.R. 1057 takes a narrow and inhumane approach, primarily in behalf of creditors rather than debtors, to the whole problem of excessive use of credit and ensuing wage earner bankruptcies. The AFL-CIO has long been concerned with abuses in credit and wage garnishment legislation of which rising bankruptcy filings are symptomatic.

We have asked that the Congress enact a truth-in-lending bill to compel the full disclosure of actual costs of consumer credit in terms of dollars and cents and in terms of the often shocking rates of true annual interest. We have called attention to abusive wage garnishment statutes and other credit abuses. In 1959, for example, the convention resolution on consumer protection included the following statement:

We recommend to state legislatures that they extend and improve laws regulating operations of small loan companies and the terms of retail installment sales. We urge the further establishment and improvement of laws protecting workers against onerous terms of wage garnishment in payment of debts and that effective means be found to curb the operations of unscrupulous merchants seeking to possess themselves of workers' paychecks by deceptive extension of credit.

Garnishment laws and wage assignment laws in particular are an invitation to the irresponsible extension of credit. The creditor who knows he can collect through wage attachment proceedings cares little whether the debtor is a good credit risk or not.

Where garnishment laws are hush, a worker may be driven directly into bankruptcy to escape garnishment, and more especially where the worker is threatened frequently, with the loss of his job on account of a garnishment. Or he may desperately attempt to stave off bankruptcy by contracting further debts from loan companies or debt poolers, thus compounding his financial distress.

In a November 1966 pamphlet entitled, "Garnishment and Debt Pooling in Relation to Consumer Indebtedness," the U.S. Department of Labor, Bureau of Labor Standards called attention to the high ratio of wage earner bankruptcies in those States which have harsh garnishment laws.

For example, in 1965, in California where garnishment is obtained easily there were 25,580 personal bankruptcies while in Pennsylvania, with no garnishment there were only 512.

I have attached a more detailed excerpt from this study as appendix A.

The obvious conclusion is that easy credit exists where protected and encouraged by garnishment statutes and garnishment drives wage earners to bankruptcy.

Most writers and even some proponents for this bill will agree that garnishment is a key factor in personal bankruptcy.

Workers who become overextended on credit under the threat of having all or nearly all of their wages garnished, and, in some cases

are threatened with their jobs, will naturally choose the out that the law from time immemorial provides: the bankruptcy route.

We suggest that H.R. 1057, far from ameliorating the problem of overextension of credit, will contribute to further abuses by giving creditors a more certain guarantee of repayment of debt through coercive use of chapter XIII debt repayment plans.

The bill is not a cure, but only a liniment for the serious situation underlying the tremendous rise in wage-earner bankruptcies in recent years. Far more fundamental reform is needed in the array of creditors' weapons against borrowers in the form of harsh garnishment laws, cognovit notes, deficiency judgments, and the like.

In February 1967, the executive council of the AFL-CIO called upon the Congress to "undertake or authorize a comprehensive study of consumer credit laws and practices."

One such study, directed toward wage garnishment laws, is already underway, by order of President Johnson. The President, in his message to the Congress on urban and rural poverty, made the following announcement.

Hundreds of workers among the poor lose their jobs or most of their wages each year as a result of garnishment proceedings. In many cases, wages are garnished by unscrupulous merchants and lenders whose practices trap the unwitting workers.

I am directing the Attorney General, in consultation with the Secretary of Labor and the Director of the Office of Economic Opportunity, to make a comprehensive study of the problems of wage garnishment and to recommend the steps that should be taken to protect the hard-earned wages and the jobs of these who need the income most.

We respectfully urge the committee withhold its approval of H.R. 1057.

Thank you, Mr. Chairman.

Mr. JACOBS. Thank you very much, Mr. Doherty.

Without objection the appendix of your statement will be included in the record.

(The document referred to follows:)

APPENDIX A

WAGE GARNISHMENT

Wage garnishment is a collection method used by creditors to force payments on an employee's debts by requiring the employer to deduct payments from the employee's earnings before he receives his paycheck. Garnishment is a dangerous prospect for the wage earner because it reduces his available income for other day-to-day expenses, and because of the possibility he may lose his job, due to the employer's unwillingness to become involved in the garnishment process. (New York this year became the first State to prohibit discharging an employee solely because his pay is garnished.)

Garnishment laws include some protection for the debtor by exempting a portion of his earnings from the garnishment proceedings, to enable him to continue to support himself and his family. The portion of wages that may be garnished is limited to some extent in 48 States, the District of Columbia, and Puerto Rico; in a few of these States it is very strictly limited. Wages are not subject to garnishment in Texas and Pennsylvania.

The exemptions, and the circumstances under which they may be claimed, vary greatly from State to State. Some jurisdictions exempt a percentage of the worker's earnings, while others exempt a specified amount. Sometimes the exemption is allowed only to a head of a family or only to residents of the particular State. Under some laws, it is still possible to garnish a worker's wages for two or

more debts at the same time. Thus some States give more protection to a debtor than others. For instance, the California law exempts 50 percent of the worker's wages in all cases, and up to 100 percent if necessary for the use of the debtor's family, except for debts for necessities. In actual fact, however, a very small minority of those garnished obtain an exemption of over 50 percent due to the complexities of the law. In Maine the exemption is \$30 for the preceding month. On the other hand, Hawaii exempts from garnishment 95 percent of the first \$100 per month, 90 percent of the next \$100, and 80 percent of the balance.

Sometimes the debtor must specifically claim the exemption himself or must prove to the court that the family needs his earnings. The person living in poverty and ignorance is not likely to be aware of his rights, and in some cases his entire paycheck may be garnished.

There seems to be a direct connection between the number of garnishments and the number of personal bankruptcies. Studies have shown that States which have harsh garnishment laws and poor credit regulation have the highest number of personal bankruptcies proportionate to their population. States with less harsh laws, such as New York which exempts 90 percent of the debtor's pay, have a much lower rate of personal bankruptcies than do States with inadequate exemption provisions.

In 1965 the number of personal bankruptcies filed in Federal courts increased for the 13th straight year. Over 180,000 bankruptcies were filed, of which 163,400 (over 90 percent) were personal or "consumer" bankruptcies. A survey of referees in bankruptcy, conducted early in 1965 by the Administrative Office of the United States Courts, stated "The harsh garnishment laws of California, Minnesota, Ohio, Tennessee, Virginia, and Michigan were given as a major cause of insolvency. Loose credit was frequently blamed. Grasping practices, harsh collection laws, inadequate exemptions, unregulated finance charges on retail credit sales and unrealistic deficiency claim judgments were blamed along with reckless buying and cognovit notes."¹ The report indicated that when a collection agency goes after a debtor's wages, facing his employer's policy of nongarnishment, he files bankruptcy in order to save his job. Other States also cited as "bankruptcy capitals" are Alabama, Colorado, and Oregon.

In the States mentioned above, the following number of voluntary bankruptcies were filed by employees in 1965:

Alabama-----	9, 522	Ohio-----	14, 850
California-----	25, 580	Oregon-----	3, 080
Colorado-----	3, 203	Tennessee-----	8, 602
Michigan-----	5, 877	Virginia-----	4, 049
Minnesota-----	2, 567		

These figures can be compared with the number of employee voluntary bankruptcies in States that prohibit or strictly limit garnishment of wages:

South Carolina-----	76	Alaska-----	140
South Dakota-----	507	Florida-----	144
Texas-----	512	Pennsylvania-----	329

A law allowing only limited garnishment would be a deterrent to easy credit, because the businessman would be less inclined to use the courts as his collection agency, as is often the case now.

Mr. JACOBS. Mr. Poff?

Mr. POFF. Thank you, Mr. Chairman. It might be impossible for the witness to speak for Mr. Biemiller. If so, he will simply say so, and I will not press the question.

My concern is to know how he would feel about the amendment which has been discussed in the hearings concerning the broadening of the concept of the wage earner to include all those entitled to benefits under the Bankruptcy Act, except commercial corporations.

Can you respond to that, sir?

¹ A cognovit note, or confession of judgment, is a prior written admission of liability for a debt given by a debtor as security for the debt. Its effect is to simplify later legal procedures for the creditor to collect on the debt and, conversely, to make more difficult the debtors's efforts to contest it.

Mr. DOHERTY. Yes; we discussed that, and first of all, we haven't seen the amendment. Secondly, for it to become effective would involve revision of the whole bankruptcy code, because there are exemptions for the different types of nonwage earners.

Thirdly, we think the discrimination in favor of a corporation and its right to a free and untrammelled discharge of its debts will still exist, and this is where we object to your bill.

Mr. POFF. Would you object if the corporations would be included?

Mr. DOHERTY. If the corporations were included, we would certainly discuss it.

Mr. POFF. It is a hypothetical question, because we do not yet have firm language, and I realize that the specific language would not be an obstacle to your position on the concept.

Mr. Chairman, we have other witnesses today. I am not going to pursue the questioning further. Thank you.

Mr. JACOBS. Mr. Wiggins?

Mr. WIGGINS. I want to say that I do agree with you and the position of the AFL-CIO that one of the great reasons for these bankruptcies is the current status of our laws with respect to garnishment of wages, and I wish you some success in the State legislatures in getting this problem corrected, sir.

I only want to make an observation, and that is that throughout your statement you referred to irresponsible lenders and sellers—referring to them rather harshly. I think you would agree that the responsibility here, at least in part, falls upon the purchaser as well. While I understand that your interest is in representing them, and you have done a good job in doing so, I do want to comment that we have a good many irresponsible buyers in the United States, many of whom doubtless belong to your union. They have their fair share of responsibility.

Thank you.

Mr. DOHERTY. If I may make one comment, Mr. Chairman.

Perhaps we are harsh in our comments on supereasy credit. We are not against credit. We would like to see some sort of caveat emptor provided to the creditor, too. This is our objection to this bill.

Mr. WIGGINS. Thank you.

Mr. McCLORY. I concur with you that your actions would relate to any unconscionable conduct of any lenders of money, but I am wondering whether your attack and your campaign against unfair practices on their part should be carried on through the bankruptcy laws.

Don't you think that should be a direct campaign?

Mr. DOHERTY. Well, we view this bill, this proposal of Congressman Poff's, as an impediment to our attack, and that is the reason we are here today.

Mr. McCLORY. Insofar as enjoining garnishment, or forestalling garnishment is concerned, it can be accomplished under a chapter XIII proceeding just as well as it can under a straight bankruptcy proceeding; can it not?

Mr. DOHERTY. Yes, sir; it can. But we object to the compulsory nature of it as it would be if this bill became law.

Mr. McCLORY. One of the problems of straight bankruptcy is that these unwise borrowers or purchasers of property on installment

terms are forestalled from discharge from bankruptcy for a period of 6 years after they have utilized it once, so that they are completely defenseless then, aren't they, under the bankruptcy law?

Mr. DOHERTY. They are completely defenseless in that they are at the mercy of their creditors?

Mr. McCLORY. Yes. They can't utilize the bankruptcy law again for 6 years if they get a discharge from bankruptcy.

Mr. DOHERTY. This is true. I understand they can file a petition for a chapter XIII arrangement, and secondly, as far as the unwise and irresponsible purchaser is concerned, then it suffers the detriment—

Mr. McCLORY. If instead of utilizing chapter XIII, which this bill, H.R. 1057, would encourage, we continue the present practice of utilizing straight bankruptcy in most of the cases, because I understand there are only 28,000 chapter XIII cases out of 192,000 employee cases, that except for those 28,000 persons, employees have denied themselves the right to a discharge from bankruptcy for a period of 6 years.

Mr. DOHERTY. First of all, Congressman, we don't think it encourages the use of chapter XIII so much as it compels it.

Secondly, there is a right involved here, and this is the right of a debtor to be relieved of his debt. We give these rights to the bad businessman or irresponsible businessman. Why shouldn't the wage earner have it? This is what Congress did when it enacted the Chandler Act.

Mr. McCLORY. As I understand it, at the hearing which the referee would have, there would be a determination made as to whether or not the person would be able to pay his debts from his income, and there wouldn't be any requirement that he pay obligations that he wasn't able to pay.

Mr. DOHERTY. You are saying to the debtor, "You have a burden of showing us that you cannot pay your debts out of future earnings. We feel that in our judgment—not your judgment—in our judgment, if you can pay, we are going to force you into chapter XIII, or leave you at the mercy of your creditors."

This is what we object to. Wage earner debtors have a right to discharge as well as any other class of debtors.

Mr. McCLORY. Of course, we subscribe to a court system, and we support the principle of having our case submitted to a court for adjudication, wherein a person has the opportunity for a hearing.

It seems to me that it is a very fair and constitutional arrangement.

Mr. DOHERTY. I wonder whether or not it is. I talked to a referee on the phone from New York the other day and I was asking him about this bill. And he said he had been talking to several judges on the court of appeals in New York and he does have some constitutional reservations about this.

Secondly, by using these legalistic arguments, I think you are getting away from what is the Bankruptcy Act. The Bankruptcy Act is a social institution. It is supposed to have social utility.

One purpose is to give the debtor, even if he can pay debts out of future earnings—

Mr. McCLORY. It doesn't give an absolute right to discharge, because for a 6-year period after that, there is no right to a subsequent discharge under the Bankruptcy Act at all.

That is an unconstitutional position we have placed the debtor in, because he has not been given an opportunity by the court to determine

whether or not he wanted to, or whether he could, pay his debts under his future income.

Mr. DOHERTY. He has a right to an absolute discharge once every 6 years as much as anybody else. If this is what Congress intended in enacting the bankruptcy laws, we don't quarrel with that, and he still has the right to file a petition, as I understand it from the previous testimony, to go into chapter XIII during that 6-year period, isn't that right?

Mr. McCLODY. During the 6-year period he could file a chapter XIII proceeding?

Mr. DOHERTY. This is my understanding.

Mr. McCLODY. He wouldn't have any alternative during that 6-year period.

Mr. DOHERTY. No, but every 6 years he gets this break that Congress has given him, and to every other debtor.

Mr. McCLODY. Even though you wouldn't support the language of the bill the way it is, wouldn't you support some provisions which would encourage greater utilization of chapter XIII?

The reason I ask that is this: Earlier testimony indicated that in most cases the debtor was not advised of the opportunity under chapter XIII to discharge his lawfully assumed debts, and that in general debtors do want to pay their debts. They want to be responsible citizens, but they are really not given a full opportunity under the law as it is now for the practices which have developed, the tendency of counsel to avoid the more complicated chapter XIII proceeding. Therefore, do you feel, sir, that there should be this philosophy of encouraging the utilization of chapter XIII?

Mr. DOHERTY. So long as it does not involve compulsion. It is something like the Truth-in-Packaging Act, where Congress said to the Commerce Department, "You bring industry and consumer representatives together and try to set these standards," but there is no compulsion.

That is fine, we would have no objection to it as long as it is not compulsory.

Mr. McCLODY. Thank you.

Mr. JACOBS. Would it be a fair inference from your testimony that you draw a distinction between the so-called unwise buyer and borrower and the uninformed buyer and borrower?

Perhaps one of the wisest men in the world might shake out a couple of aspirins in a bottle and find they were strychnine unless there was some protection for him, not just because he was stupid, but because in this kind of civilization, this kind of society, the general public has come to depend upon certain kinds of protection for its benefit so that it is not required to make an elaborate investigation on each occasion when one enters into a consumer contract.

Mr. DOHERTY. That is correct. We agree with the distinction between an unwise consumer and a knowledgeable one.

The whole thrust of the truth-in-lending bill, it is not a regulatory statute, it is a disclosure statute. It simply says information should be available.

Mr. JACOBS. I have detected from time to time on the part of many people a tendency toward condescension in speaking of citizens with limited education, and their so-called irresponsibility as they deal in

the marketplace. But I think that while all citizens must have individual responsibilities, that it is not unreasonable to rely upon certain regulations for protection against ignorance, which I think are necessary in this kind of complex society.

Mr. DOHERTY. Ignorance is inevitable, but I think Congress is going to have to devote itself to this overpricing that the Federal Trade Commission is now looking into.

Some of these cases are just horrible.

Now how you do this without getting into price regulation, which we are opposed to, I don't know, but somebody is going to have to look at it, because these people are just being preyed upon.

Mr. JACOBS. Thank you very much for your testimony, Mr. Doherty. And thank you for bringing the ladies with you.

Our next witness is George S. Bullen, legislative director, National Federation of Independent Business.

**STATEMENT OF GEORGE S. BULLEN, LEGISLATIVE DIRECTOR,
NATIONAL FEDERATION OF INDEPENDENT BUSINESS, ACCOMPANIED BY JEROME GULAN**

Mr. BULLEN. Mr. Chairman, I have with me my assistant, Mr. Jerome Gulan.

Mr. JACOBS. Will you proceed in your own manner?

Mr. BULLEN. In behalf of our members, I wish to thank you, Mr. Chairman, for this opportunity to testify before your subcommittee in support of H.R. 1057 and H.R. 5771, identical bills, to amend the Bankruptcy Act with respect to the use of chapter XIII.

The National Federation of Independent Business was founded 24 years ago as a nonprofit, nonpartisan organization, and has grown steadily so that today we represent small businesses in every State and have a current membership of more than 234,000. From the standpoint of individual, directly supporting members it is the largest business organization in the United States.

More than one of every 20 small businesses make up our membership, which is a representative cross section of the Nation's entire independent business community at the retail, wholesale, manufacturing, servicing, and professional occupational levels.

The legislative policies of the federation are determined by the direct vote of the membership, with each member having only one vote regardless of the size of his business enterprise. The majority position of the federation's membership, distributed through all the States, and representative by type or trade of all the Nation's 4.7 million small businesses should, we believe, quite accurately reflect the opinion of all independents.

While the federation has not polled its members on either H.R. 1057 or H.R. 5771, we did present to them in September 1966, an identical bill, H.R. 292, introduced by Representative Celler in the 89th Congress. By a very large majority the members voted in favor of Mr. Celler's bill. This position naturally carries forward to the two bills being considered by this subcommittee. We polled our members in the following manner:

H.R. 292. A bill to amend the Bankruptcy Act to require that a person pay off his indebtedness out of future earnings over a period of years. (Cong. Celler, N.Y.)

The following are brief arguments "for" and "against" which our members were asked to read before voting.

Proponents of this bill including the American Bar Association, say that the purpose is to screen out the unnecessary bankruptcy cases in which the debtor has sufficient earnings to handle his debts. Now, even though a debtor may be fully capable of paying his debts out of future earnings, the judge or bankruptcy referee has no power to require the repayment. Studies have shown that 25% to 50% of the wage earner bankrupts could pay their debts out of future earnings, if the amendment to Chapter XIII is passed.

The arguments against were as follows:

The opponents of this amendment, including National Bankruptcy Conference and the National Legal Aid and Defender Association, contend that the proposal would substantially increase the work load of bankruptcy referees. Also they say that every person should have an unrestricted right to obtain a bankruptcy ruling and that the proposed amendment would discriminate against wage earners. This amendment would also leave quite a bit to guesswork, because it would allow some debtors to use straight bankruptcy.

The results of the voting were as follows: 79 percent for, 16 percent against, and 5 percent had no opinion.

From the strong vote in favor of the bill it appears that many small business proprietors may have been hurt by personal bankruptcy cases, and inasmuch as the stigma one associated with bankruptcy seems to be waning, they may fear that they will suffer even more unless steps are taken to halt personal bankruptcy as an easy out of paying one's just debts.

Representative Poff, in remarks made on the House floor in support of his bill, H.R. 1057, pointed out that during the past 25 years consumer credit has risen from an aggregate of \$9.2 billion to about \$93 billion, and that continued growth of sound and constructive consumer credit is being jeopardized by the rapidly increasing rate of consumer bankruptcies filed in the country each year. Nonbusiness filings have increased from 74.79 percent of total bankruptcy filings in 1940 to 91.5 percent of the total in 1966.

Some people have recommended that debtor-creditor relations be changed with the objective of reducing the ever increasing number of personal bankruptcies. It is likely that the number could be reduced by prohibiting the garnishment of wages and judgments of all kinds, by tightening consumer credit, and by restricting collection procedures. We do not feel that such action is desirable, however, either socially or economically.

We believe that lenders and sellers would become more selective and credit would become less plentiful. It has been estimated that in 1965, nearly half of the families in the Nation owed installment debt alone, and that many more owed some type of consumer debt.

Many of our citizens who presently enjoy consumer credit would be denied credit and could not maintain the standard of living they now enjoy. This would result in reduction in the consumption of durable goods, and would slow the economy.

Passage of this legislation would be most beneficial for many of the Nation's citizens, who find themselves in an overextended installment credit dilemma caused by overzealous persuasion on the part of sellers.

Many of these, in desperation because of creditor harassment have sought relief through bankruptcy. A great many with too many installments to meet, we feel would be willing to pay there just debts if

they could do so without fear of job safety as a result of creditor harassment.

Also, as you are aware, many so-called debt consolidators have sprung up throughout the country to prey on these unfortunate citizens who are unable to meet all their obligations on time.

Debt consolidators try to persuade debtors to refrain from making direct payments to their creditors and instead, make payments to them. They, in turn, pay the creditors, but only after taking a sizable premium from the debtor's payments, thus adding another creditor to the debtor's long list.

Senator Tydings has introduced a bill—S. 1739—to prohibit these commercial debt adjusters in the District of Columbia, and 21 States have already enacted legislation to control the practice. Passage of the legislation which your subcommittee is considering would be an effective deterrent to the operation of such outfits.

The federation believes that the most feasible tool with which to control the number of personal bankruptcies is to make changes in the bankruptcy laws that are consistent with the basic tenet of bankruptcy legislation; that is, those who can pay their legitimate obligations, or a portion thereof, should be required to do so, and those who cannot, without causing undue harm to themselves and society, should not be required to do so.

In other words, the wage earner plan should be the major avenue of a distressed debtor and straight bankruptcy would be permitted only after it had been determined that the debtor could not hope to pay his debts. According to our understanding, the bills being considered would provide that a referee in bankruptcy would have the authority to deny straight bankruptcy if he found the debtor in a position to pay a portion or all of his obligations.

This would screen out those petitioners who are in a position to pay a part or all of their debts. Passage of either of these bills would be a great improvement over the present arrangement.

That concludes my statement, Mr. Chairman.

Mr. JACOBS. Thank you, Mr. Bullen, for your testimony.

Mr. Poff?

Mr. POFF. Thank you, and I join in expressing our appreciation.

I hope you don't think our failure to interrogate you more shows a lack of interest.

However, we hope that we can conclude this phase of the hearings this afternoon.

With my thanks, I will defer to my colleague.

Mr. BULLEN. Mr. Poff, I am happy you are not asking me too many questions after following a Harvard professor.

Mr. WIGGINS. I have no questions. Thank you.

Mr. MCCLORY. I have no questions, thank you.

Mr. JACOBS. Thank you very much, sir.

Our next witness is Mr. Richard J. Schwarzstein, a member of the bankruptcy committee, association of the bar of the city of New York.

STATEMENT OF RICHARD J. SCHWARZSTEIN, COMMITTEE MEMBER
OF THE BANKRUPTCY SUBCOMMITTEE OF THE ASSOCIATION OF
THE BAR OF THE CITY OF NEW YORK

Mr. SCHWARZSTEIN. Our committee appreciates your having given me the opportunity to express to you its views as to H.R. 1057 and H.R. 5771.

It has been a long day for your committee and I don't want to take up any of your time unnecessarily.

Our committee has prepared and has filed with your committee a report indicating our objection to these two bills.

In the interest of time, I would suggest that our report be incorporated into the record of these hearings, and I use this opportunity simply to summarize the recommendations which we have set forth in that report.

Mr. JACOBS. Without objection, that matter will be included into the record at this point.

(The document referred to follows:)

COMMITTEE REPORT: DENIAL OF BANKRUPTCY RELIEF TO WAGE EARNERS ABLE TO
RESORT TO PLANS UNDER CHAPTER XIII OF THE BANKRUPTCY ACT

INTRODUCTION

H.R. 1057 and H.R. 5771 (90th Cong., 1st Sess.) would amend Section 55b of the Bankruptcy Act to provide that, at the first meeting of creditors, a bankrupt who is a "wage earner", as defined under the Act, must make a showing before the referee or judge that adequate relief cannot be obtained under Chapter XIII. In the event that showing is not made, the bankruptcy proceedings would be dismissed.

These bills, which are identical, are designed to preclude a wage-earner from resorting to straight bankruptcy and obtaining a discharge from his debts if the bankruptcy court concludes that the wage-earner, on the basis of his future earnings, could formulate a Chapter XIII plan providing for the composition or extension of his debts, and thereby meet his obligations to his creditors.

Our Committee believes that Chapter XIII offers many wage-earners a desirable alternative to straight bankruptcy. Later in this report there are recommendations as to steps that can be taken to popularize the use of Chapter XIII by debtors. Our Committee is opposed, however, to any change in the Bankruptcy Act that would prevent a wage-earner, who was aware of and could utilize Chapter XIII, but who preferred to receive a total discharge from his debts, from going through straight bankruptcy.

COMMENTS

Between 1867 and 1938, there was but limited statutory relief available for financially distressed wage-earners. Compositions under Section 1 of the Bankruptcy Act were generally unsatisfactory in view of the fact that those proceedings lacked flexibility and were expensive. On the other hand, a straight bankruptcy was a harsh remedy for anyone who wished to pay his debts in full, but lacked assets and the ability to hold off creditors until sufficient moneys were earned. Therefore, Congress decided, by passage of the Chapter XIII provisions of the Chandler Act, to give wage-earners, who so desired, a way to pay their debts in full out of future earnings.

With this revision of the Bankruptcy Act giving wage-earners, for the first time, meaningful alternative forms of relief, the Act reached an important milestone. For Congress now to eliminate straight bankruptcy as an alternative form of relief for wage-earners would constitute regressive legislation. Our Committee believes that, from a moral standpoint, wage-earners should have the same right to be discharged from debts and to start life anew as non-wage-earners do. Non-wage-earning individuals and corporations, of course, can file straight bankruptcy petitions and are not required to formulate plans under

Chapter X or Chapter XI. Moreover, it has been suggested by members of our Committee that to discriminate against wage-earners alone as proposed by these bills, by denying them the right to file straight bankruptcy petitions, would be unconstitutional.

The argument usually made for limiting the rights of wage-earners is that there have been a growing number of consumer bankruptcies with attendant losses in our economy, and that in resorting to bankruptcy a wage-earner consumer has not faced up to his financial and moral responsibility. Therefore, it is argued, he should be required to utilize Chapter XIII and pay off his obligations in full out of his future earnings.

It does not appear, however, that the increased number of consumer bankruptcies has been due to excesses on the part of wage-earners alone. These bankruptcies have also been made possible through the failure of lending or retailing institutions to make complete credit checks on consumers before extending credit, and through the encouragement of consumer installment credit purchases without frank disclosure to the consumer of the interest and other charges connected with the purchases. Therefore, since these creditors have not been blameless in these situations, Congress should not amend the Bankruptcy Act with respect to Chapter XIII just to satisfy them.

In addition, there is no justification for a statutory amendment to the Bankruptcy Act on the ground that Chapter XIII has not been sufficiently utilized by debtors over the years. According to the Administrative Office of the United States Courts, 20% of all bankruptcy proceedings filed in the past 20 years have been under Chapter XIII. It may be assumed that this percentage would have been even higher if (a) Chapter XIII had been available to all wage-earners during that period¹ and (b) the lower federal courts had not held that Chapter XIII could not be utilized where a Chapter XIII petition was filed within six years of the granting of a discharge in bankruptcy.² Although utilization of Chapter XIII has not been uniform through the country,³ this disparity does not mean that any drastic statutory remedy, such as the deprivation of straight bankruptcy for a wage-earner, is warranted. It merely means that, where Chapter XIII has not been utilized, steps should be taken to popularize Chapter XIII and to make its use more feasible.

RECOMMENDATIONS

Our Committee proposes that a number of things be done (a) to educate debtors as to the availability of Chapter XIII as an alternative to straight bankruptcy and (b) to make Chapter XIII more attractive to debtors. It is our belief that the steps set forth below will encourage the use of Chapter XIII, without denying any debtors relief through straight bankruptcy.

1. Official Form No. 2 (Statement of Affairs) should be amended by the Supreme Court to require that a bankrupt affirmatively state that he has been apprised of Chapter XIII, that he has considered utilization thereof as an alternative to straight bankruptcy, and that he has concluded that Chapter XIII would not be feasible.

2. In order to be certain that the bankrupt is aware of Chapter XIII, the Administrative Office, or the Supreme Court through its General Orders, should direct referees to have the bankrupt answer questions at the first meeting of creditors about his failure to utilize Chapter XIII. However, these questions would only be for educational purposes and no debtor would thereby be denied from utilizing the straight bankruptcy provisions of the Act.

3. Bar associations, trade associations, credit associations, consumer groups, counselling services, employer associations, and legal aid societies should attempt to make employees and practicing attorneys as aware of Chapter XIII as they are of straight bankruptcy. Our Committee proposes to take steps to meet our responsibility under this paragraph with respect to members of our Association.

¹ Until 1950, Chapter XIII was not available to wage-earners earning more than \$3,600 per year. From 1950 until 1959, it was not available to wage-earners earning more than \$5,000 a year. It is now available to any individual "whose principal income is derived from wages, salaries, or commissions."

² The Supreme Court recently reversed the lower courts in *Perry v. Commerce Loan Company*, 383 U.S. 392 (1966), and held that a Chapter XIII petition can be filed within six years of the granting of a discharge in bankruptcy. In its opinion, the Court noted that Chapter XIII filings had declined by virtue of the previous decisions of the lower courts.

³ According to the Administrative Office of the United States Courts, in fiscal year 1966, almost 80% of the filings in some districts were under Chapter XIII, while less than 1% of the filings in other districts were under Chapter XIII.

4. The cost of administering a wage-earner plan under Chapter XIII could be reduced by equipping a select group of court-appointed trustees with electronic bookkeeping machines. Such an innovation, which has been used in some districts, would make Chapter XIII more attractive to wage-earners since a reduction in cost would make more earnings available for obligations and would shorten the duration of the plan.

5. Chapter XIII could be made more popular with attorneys representing wage-earners if the extensive clerical and paper work involved in such a proceeding could be eliminated or made the responsibility of a court-appointed trustee who would work in close cooperation with the attorney for the wage-earner.

CONCLUSION

For the reasons stated above, H.R. 1057 and H.R. 5771 are disapproved (Albert W. Driver, Jr., dissenting). At the same time, however, our Committee strongly recommends that the steps suggested in this Report to encourage the use of Chapter XIII be considered by all advocates of the aforesaid bills and by all those who are charged with administering the Bankruptcy Act, including the Administrative Office of the United States Courts, referees in bankruptcy, and the Judges of the Supreme Court and the District Courts.

Respectfully submitted.

COMMITTEE ON BANKRUPTCY AND CORPORATE REORGANIZATION,
WILLIAM W. GOLUB, *Chairman*.

April 15, 1967.

Samuel R. Ballin*
Edgar H. Booth
Otto Crouse
Ambrose Doskow
Albert W. Driver, Jr.**
Malcolm Fooshee
Frank H. Heiss
Sydney Krause
George R. Lenz
Sidney R. Nussenfeld

Donald J. Robinson
Leonard M. Rosen
Michael E. Schoeman
Richard J. Schwarzstein*
Charles Seligson
Joseph P. Sullivan
John Trubin
Charles H. Vejvoda
Leonard Zalkin
George Zolotar

*Dissenting with respect to the Committee's disapproval of the wage-earner bills.

**Members of Subcommittee on Chapter XIII.

Mr. SCHWARZSTEIN. We feel that chapter XIII provides a meaningful alternative to straight bankruptcy, and that debtors and creditors will benefit from a greater utilization of it. However, we do not believe that the proposed legislation is necessary to bring about a greater utilization of chapter XIII in those judicial districts where it has not been popular.

Instead, we urge that certain steps be taken to encourage wider use of chapter XIII.

However, if the problem is basically the failure of some districts to utilize chapter XIII, we believe the solution must be based upon encouraging the voluntary use of chapter XIII in those districts, rather than the passage of a bill or amended bill, which would extend the compulsory features of these bills to other types of debtors and other types of bankruptcy proceedings where there have been no problems.

Our recommendations are as follows: 1. Official Form No. 2, which is the statement of affairs filed in a bankruptcy proceeding should be amended by the Supreme Court to require that a bankrupt affirmatively state that he has been apprised of chapter XIII, that he has considered utilization thereof as an alternative to straight bankruptcy, and that he has concluded that chapter XIII would not be feasible.

2. In order to be certain that the bankrupt is aware of chapter XIII,

the administrative office, or the Supreme Court through its general orders, should direct referees to have the bankrupt answer questions at the first meeting of creditors about his failure to utilize chapter XIII. However, these questions would only be for educational purposes and no debtor would thereby be denied from utilizing the straight bankruptcy provisions of the act.

3. Bar associations, trade associations, credit associations, consumer groups, counseling services, employer associations, and legal aid societies should attempt to make employees and practicing attorneys as aware of chapter XIII as they are of straight bankruptcy. Our committee proposes to take steps to meet our responsibility under this paragraph with respect to members of our association.

4. The costs of administering a wage earner plan under chapter XIII could be reduced by equipping a select group of court appointed trustees with electronic bookkeeping machines. Such an innovation, which has been used in some districts, would make chapter XIII more attractive to wage earners since a reduction in cost would make more earnings available for obligations and would shorten the duration of the plan.

5. Chapter XIII could be made more popular with attorneys representing wage earners if the extensive clerical and paperwork involved in such a proceeding could be eliminated or made the responsibility of a court appointed trustee who would work in close cooperation with the attorney for the wage earner.

6. Finally, I would like to point out that even the calling of these hearings by this committee, and the dissemination of information about these hearings to creditors, debtors, the judiciary, and the bar, even without a recommendation for new legislation, may very well give chapter XIII the impetus it needs.

Thank you.

Mr. JACOBS. Thank you for your testimony.

Mr. Poff?

Mr. POFF. I am sure you agree that the decision in the *Perry* case will also increase the use of chapter XIII.

Mr. SCHWARZSTEIN. I did see statistics that there had been a decline for a period, and there has been a revitalization.

Perhaps the statistics which have shown that chapter XIII did not grow as might have been expected were in part due to the uncertainty that was clarified by the *Perry* decision.

Mr. POFF. Do you speak for the full subcommittee of which you are a member?

Mr. SCHWARZSTEIN. Yes; the full committee of the bar association has voted on this, and out of our 20 members, 19 voted against the proposed legislation, and all 20 have—very strongly support methods to encourage the use of chapter XIII throughout the country.

Mr. POFF. Does the association have a subcommittee on chapter XIII?

Mr. SCHWARZSTEIN. Yes. That is a subcommittee of which I am a member, and we explored this problem when we first encountered it and discussed it with the full committee and they analyzed it over several sessions.

Mr. POFF. The subcommittee consists of how many members?

Mr. SCHWARZSTEIN. Three members.

Mr. POFF. Did the three concur in the statement you have made?

Mr. SCHWARZSTEIN. One member who declined to support the opposition to these bills was a member of the subcommittee and his position was that he supported chapter XIII, but did not oppose the bills.

I should add the reason for it. It is very simple. The member of our subcommittee was also very active with an American Bar Association committee which has over the years wanted chapter XIII to be used to a greater extent, and he takes the same view that the American Bar Association took, that it will require some legislation to establish uniformity in the districts with respect to chapter XIII.

Mr. POFF. Forgetting those for whom you appear in a representative capacity, but rather giving your personal viewpoint only, let me ask what impact would it have upon your view of the bill if the bill were broadened to include all natural persons other than commercial corporations?

Mr. SCHWARZSTEIN. I did make a reference to this earlier. Since the reason that the bills have been advocated is because of a general problem as to the lack of uniformity in the utilization of chapter XIII throughout the country, it would appear to me that this is what you must work on and not try to solve the problem through the other sections of the act, where there have been no problems. Also, as we have indicated in our full committee report, just as wage earners and other debtors have reached a status after many years of gradual steps by Congress in improving chapter XIII and creating alternative forms of relief, there just doesn't seem to be a sufficient reason at this time for going back to an earlier generation and denying a debtor alternative forms of relief.

We regard that as a type of regressive legislation. Today, if a debtor is informed, which is one of the things that we feel is most important, and he can make a choice, we feel he will see the benefits of chapter XIII, and will choose it. But he has alternatives which will be lost if the bill is passed as proposed or modified.

Similarly, a corporation may see the benefits in a chapter XI or a chapter X, or in a straight bankruptcy but I think our society does best where everybody who is informed has alternatives, and is not limited to one form of relief.

Mr. POFF. If the committee and the Congress see fit to enact a law, would you prefer that it apply only to wage earners, or to a broader group, and, if so, to what broader group?

Mr. SCHWARZSTEIN. I am not trying to beg the question. It is complicated by the interrelations of the sections of the Bankruptcy Act. Chapter XI has worked very well when used by corporations. However, corporations have at times decided not to use that chapter. Therefore, it becomes very difficult to envision what advantage there would be in a compulsory system. However, we did oppose this bill on at least one ground, which was that it had a discriminatory element.

Certainly, a broader bill would eliminate that.

On the other hand, it does appear that a broader bill may produce more problems in the other areas than it will solve just by trying to eliminate the discriminatory aspect. We would certainly have to review how it would apply in other areas where we feel there is a good method of dealing with creditor-debtor relations.

Mr. POFF. May I say in conclusion that I admire the five proposals you have made? Whatever the fate of this legislation, I hope that something appropriate in that area will be done.

Thank you.

Mr. JACOBS. Mr. Wiggins?

Mr. WIGGINS. Yes; I refer particularly to the last comment of Congressman Poff, that many of your suggestions are worthy of implementation regardless of what happens to the legislation before the committee.

Do you have some idea of what the typical fee charged is in the preparation of schedules in first meetings of attorneys with the debtor?

Mr. SCHWARZSTEIN. I am embarrassed to say that chapter XIII has been utilized so seldom in New York that we do not have very good guidelines on this.

It has very obviously been a well-worked-out system in Maine and some of the districts of Ohio and California where they have had experience and they come to an adjustment of what perhaps is a fair fee for the amount of work involved.

But it has not been utilized enough in New York to even test what would be a fair fee or what has been a uniform fee.

Mr. WIGGINS. The answer is then, I suppose, that you don't know?

Mr. SCHWARZSTEIN. I don't think it has been uniform. You are trying to find out whether it is as high as other straight bankruptcy fees, it obviously is not.

Mr. WIGGINS. It obviously is not?

Mr. SCHWARZSTEIN. No, it is not.

Mr. WIGGINS. The fee charged for a chapter XIII proceeding would be somewhat in line——

Mr. SCHWARZSTEIN. It would be lower because the philosophy of trying to keep costs down would prevail to a greater extent than in a straight bankruptcy.

Mr. WIGGINS. I would like your observation on something.

We had two witnesses here testify, among other things, on the purposes of the Bankruptcy Act. One says that the essential purpose of the whole Bankruptcy Act is the liberation of worthy debtors from the burden of unpaid debts, even though they may have the ability to pay out of future earnings.

In other words, this procedure is accorded the debtor as a matter of right.

Others say that one of the basic tenets of the bankruptcy legislation is that those who can pay legitimate debts or a portion of the debt should be required to do so, and that those who cannot without undue harm to themselves and society should not be required to do so.

I personally believe those two statements are somewhat at odds with each other, and I would like your guidance as to which one you believe is the correct one.

Mr. SCHWARZSTEIN. I think they are at odds, but I think the different sections of the Bankruptcy Act are at odds.

Chapters I through VII is straight bankruptcy, and I believe it deals with permitting a man to start afresh as long as he has not been involved in crimes or other unworthy acts.

Other sections, such as chapters XI and X, are an attempt to permit corporations or individual businesses, to work with their creditors and try to pay off debts in a way that will make everyone happy.

I think the congressional intent must have been that it becomes easier to work with creditors in or out of court, if there is no compulsion and the feeling is that while each section may be inconsistent, it works somehow, when all is said and done because the fellow who has a choice will make a choice that in most cases will make sense, assuming he is informed.

But in some cases it will be an intent not to pay off his debts. In other cases it will be an intent to work out with his creditors a suitable arrangement.

Mr. WIGGINS. Well, all right. In passing I will say you probably answered that about the way I would answer it. [Laughter.]

Mr. JACOBS. Mr. McClory.

Mr. MCCLORY. Thank you, sir, very much.

Our next witness is Mr. Linn K. Twinem, chairman of the Consumer Group Bankruptcy Committee of the American Bar Association.

STATEMENT OF LINN K. TWINEM, CHAIRMAN OF THE CONSUMER BANKRUPTCY COMMITTEE OF THE AMERICAN BAR ASSOCIATION

Mr. TWINEM. Thank you very much, Mr. Chairman.

My name is Linn K. Twinem, from New York City, and I am chairman of the Consumer Bankruptcy Committee of the American Bar Association.

I testified briefly yesterday.

I will try to be brief. It has been a long day and a lot has been said already about H.R. 1057 and H.R. 5771.

This proposal for a change in the Bankruptcy Act originated with the Consumer Bankruptcy Committee, and to begin, I would like to give you a few of the considerations that underlie this proposal.

First, the committee was naturally very much concerned about the rising tide in consumer bankruptcy filings. Over the years there have been progressively more and as you have heard, this year we can anticipate over 200,000 bankruptcy petitions, and 91 percent will be in the nonbusiness category.

The committee was already concerned because chapter XIII filings had seemed to reach a leveling off. If you will examine the appendix or supplement to Judge Brown's statement, you will find that in 1965 there were 28,000—28,027 chapter XIII filings.

The following year there were only 28,261, a very slight increase.

We have heard talk that we can anticipate as many as 32,000 this year, but of course a good deal of it, of the additional filings, under chapter XIII this year will probably be as a result of the *Perry* case which permits chapter XIII filings within a 6-year period.

But more alarming than this great increase in the number of filings and the fact that this year there probably will be \$1.5 billion or nearly that amount, washed down the bankruptcy drain in "no asset" cases. More alarming than that jolt to the economy is the fact

that the studies which have been conducted in the various universities, to which Professor Countryman referred, have indicated that many of these people could pay their debts without undue burden out of future earnings if they were so advised and so disposed.

It has been found in one of the better studies, the one conducted by Robert Dolphin, Jr., then at the University of Michigan State, conducted under the direction of Bob Johnson, who was one of the economic advisers to the Special Committee of the Commissioners on Uniform State Laws now working on the credit code, and under the guidance and assistance of the referee in bankruptcy in Flint, Mich., this study disclosed that given an adequate standard of living, 49 percent of all those who filed petitions in bankruptcy in that area could have paid their debts out of future earnings.

Given a comfortable standard of living, at least 28 percent could have paid their debts out of future earnings.

In addition to that study, we have the study by Grant L. Misbach, at the University of Utah. We had a study by a sociologist at the University of Arizona, and just recently we had the study by Prof. Edward W. Reed, at Oregon University, and as in many other cases they concluded that a good percentage of these people could have paid their debts out of future earnings. And then in Reed's study, which is the most recent of all, published in January 1967, he says:

The most desirable step that could be taken is to make changes in the bankruptcy laws that are consistent with the basic tenets of bankruptcy legislation.

Those who can pay their legitimate obligations or a portion thereof should be required to do so, and those who cannot without causing undue harm to the individual and society should not be required to do so.

Now, that, as I say, was one of the basic underlying considerations by the Consumer Bankruptcy Committee.

The committee also had in mind that the present act, which was really enacted in 1898, before we had any concept of consumer credit, and even at the time of the Chandler amendment or enactment in 1938, we still did not know much about consumer credit. The act at that time couldn't have contemplated the problems that have been arising today, and because of the new problems and the new needs, the committee took the position that fundamentally we want to amend the basic act.

This has nothing to do with chapter XIII. This is the basic act which up to the present time has had no standard at all as a requirement for going into bankruptcy.

It doesn't make any difference whether you are solvent or insolvent. It doesn't make any difference how great your ability to pay your debts out of future earnings. You can still have them quickly discharged by filing a petition in bankruptcy.

And we believe that that is fundamentally not sound from a social or an economic point, and that a person who incurs their obligations from a creditor who grants the credit in good faith should have some responsibility in discharging those obligations if they are so able.

Now, therefore, the bill now in the form of 1057 was designed not to require the use of chapter XIII—in no wise to represent compulsory XIII—but, was merely to screen out the unnecessary straight bankruptcy proceedings, and to encourage the people to pay their debts if they have the ability.

Now from my point of view, to my mind, this bill has no direct relationship to chapter XIII, and could in no wise be construed as

compulsory XIII. There are only two reasons for any reference to chapter XIII in this bill.

First, it was necessary to find some standard to apply in determining whether a person could pay their debts out of future earnings, and a very convenient standard, it seemed to the committee, was the standard that already existed under XIII. So, instead of providing a new test, or a new guide as to when a person can pay their debts out of future earnings, they said:

Well here is one we have had on the books since 1938. Let's take the test of chapter XIII and use that as a standard in determining whether a person can pay their debts out of future earnings, and if they can meet that test, if that test applies in that particular case, then we have the test to apply and no further standards or requirements need to be established.

And so that was one reason for referring to chapter XIII in 1057, and the other reason, and the only other reason for referring to chapter XIII was that they wanted to, the committee wanted to allow an easy conversion from the straight bankruptcy proceedings to chapter XIII so that there would be no additional fee required, and so that there would be no gap between the proceedings.

If they had not done that, the referee's only recourse in meeting that standard would be to dismiss the straight bankruptcy proceedings where he found the debtor could pay his debts out of future earnings.

That would leave a gap before he could come back with his attorney and file a chapter XIII proceeding and even the overnight gap might be disastrous from the standpoint of the debtor to eliminate any gap and to make it clear no additional fee was required; the second reference to chapter XIII was inserted in the bill.

So as I like to say again, I don't see how this can possibly be construed as a compulsory chapter XIII proceeding.

Now, the only other serious objection that has been raised and raised repeatedly is that this bill would discriminate against employees, or wage earners. I think that could be corrected, if there is a serious objection. In the first place, if there is any discrimination or classification, that was created in the enactment of the classification, that was created in the enactment of the Chandler provision in 1938. That is why the committee first seized on that distinction, because there was a readymade standard in the act and they wanted to have something to refer to, so they just followed it all the way through, and said, "This will also apply to wage earners."

But it doesn't have to apply to wage earners. The same principle should apply to anybody. If you can pay out of future earnings, why shouldn't you be required to pay, and I don't care where or who you are—whether you are a doctor, a dentist or a lawyer, or a hired hand, or whatever you are.

I think the same general rules of conduct should apply, and so I certainly would have no reason for not wanting to apply it in the case of all persons.

There are other objections, usually not expressed openly, orally or in writing, for opposing this bill, and it led to an organized group opposing the enactment of such legislation. One group, and one reason has been raised by the referees, because it would impose a substantial additional burden on them.

There is no doubt about it. Referee Poulos tells you how much time he spends on chapter XIII, and other referees that make it work spend some time, too, and there is no doubt that if this bill is enacted there would be some increase in chapter XIII filings, and so that would mean that the referees now sitting would have an additional burden and they would probably have to appoint more referees.

But my frank opinion on the effect of this bill, if enacted, would be that it wouldn't create a sudden great additional number of chapter XIII proceedings, because in the first place, in my opinion, it wouldn't apply to about more than 20 percent of the people who are filing bankruptcy petitions.

The other people would have need for, and probably would be readily entitled to relief in straight bankruptcy.

So it would apply to a very small number, relatively, although it might run up to 50,000 in total numbers, in total filings, but percentagewise it wouldn't represent a very great additional total, and so the net result, however, would be that the attorneys who frequently represent debtors in bankruptcy matters would soon learn that their clients would not be entitled to relief, certain of their clients would be entitled to their relief in straight bankruptcy, and they would decide then whether they wanted to put the man under chapter XIII or seek other relief.

We haven't talked very much about other relief, and there is—there are a number of other avenues of relief here.

Five States have State court trusteeships or receiverships. In addition, there are now 61 community debt counsel services in existence, and at least a hundred more are in the discussion stage and many of them will be open shortly.

Here is a place for a person to go to get free, competent, qualified advice in the management of his financial affairs, and in debt adjusting and in debt pooling, if necessary.

Many millions of dollars are being distributed now through these community credit counseling services, and it is without cost, generally—in most cases entirely free to the debtor, and that is one other alternative course.

And if the attorney feels his client wouldn't be qualified for relief in straight bankruptcy, he might want to make other choices available to him. He may undertake to deal with these creditors directly.

After all, we are dealing with the client that can pay. That means he has more than the usual, more than the minimum, income—he is not so overburdened with debts that it is a dismal impossible task to work him out through some kind of an arrangement.

Certainly we wouldn't want to make it compulsory because chapter XIII wouldn't work on a compulsory basis.

You can't compel a man to put himself under such a strict diet in his financial affairs over a long period of time unless he really wants that relief, and if he has ability to pay, more than the usual ability to pay, and he still wants the protection of the bankruptcy court, the choice is still there for him, and he still gets it, and if he is a repeater after straight bankruptcy, or if he wants to use chapter XIII more than once in 6 years, it is still there for him. But, the idea is that it is an involuntary or compulsory chapter XIII would not

work. This is not that type of legislation, it wasn't intended to create it, and it doesn't create it.

Now one question that has been raised: Is this an impossible thing that you are proposing? What kind of a showing would the debtor have to make. Actually, it would finally resolve itself into a very simple little test.

All he would have to do is come in and show his income, what his debts are, and how much it costs him to live. A very simple standard.

The same general test—the referee would be more sophisticated in applying them than that—in using the standards he probably now uses, I suppose, but actually it would be a very simple thing.

Another consideration is that you wouldn't want anybody under chapter XIII unless they obviously had the ability to carry out a XIII plan.

Nobody would want to suffer with him under XIII. His own attorney wouldn't want to, the referee wouldn't want to, and so the referee would be very generous in determining whether a man had ability to pay out of future earnings, and so it wouldn't be an impossible or even a very difficult matter to administer.

Certainly there is no uniformity now and there would be a greater chance of having uniformity in the future if we had a law of this type. But I must get back again and again to my fundamental premise that this is for the first time to establish a standard under which you would be entitled to relief in bankruptcy.

Now, other standards have been proposed. The committee considered a number of them.

Somebody said, "Well, unless the man owes \$5,000 he shouldn't be allowed to go into bankruptcy."

That is kind of an arbitrary standard. In the first place, \$5,000 in one section of the country means something quite different than \$5,000 in another, and other considerations were presented and considered.

One State legislature, Montana, for example, they came up with a proposal by which your right to proceed—your right to bankruptcy could be tested, and there, their test was that at least—that is debts must total at least one-half of average annual income for the preceding 2 years, less 5 percent for each dependent of the bankrupt.

I am citing this to show you that this is another standard like the standard we have raised here, a standard to screen out the unnecessary cases.

You can think of hundreds of standards that might be applied. The committee, as I say, considered and pondered a number of them, and thought this was the best, the safest, the fairest test of all, and so rather than prolong this statement, this introductory comment, further, I will be glad to entertain the questions that might concern the committee most.

Mr. JACOBS. Thank you, Mr. Twinem.

One point I don't fully understand in your testimony concerns the study that was made of individual bankrupts who could have paid all their debts and continued certain standards of living.

I believe the "adequate standard group" constitute 49 percent of those who were discharged?

Mr. TWINEM. Given an adequate standard of living, 49 percent could have paid 100 percent; given a comfortable living, 28 percent could have paid 100 percent of their debts.

Mr. JACOBS. You have also testified that under this legislation you would anticipate that only 20 percent, I believe, of those now being discharged from straight bankruptcy, would be availing themselves of chapter XIII proceedings?

Mr. TWINEM. That would be my guess.

Mr. JACOBS. Does that mean in your opinion that 29 percent of those under the adequate standard, or in that category, would be able to proceed without any assistance from the court or the referee?

Mr. TWINEM. I was going—I was taking into consideration a comfortable standard of living.

Mr. JACOBS. But under the adequate standard of living category, there are 49 percent, according to this study, who would not take straight bankruptcy, but who would be able to meet their obligations out of future wages.

Now, if only 20 percent of those who are taking straight bankruptcy today in your opinion will take advantage of chapter XIII provisions as a result of this legislation then that leaves 29 percent who are just getting along adequately, meeting their obligations, and can do so without assistance from the court.

Is that your judgment?

Mr. TWINEM. No. In the first place, I am not talking about the 28,000 that have filed under chapter XIII now. I am talking about an additional 20 percent of those who are now getting a discharge in straight bankruptcy.

Mr. JACOBS. I understand that, but 49 percent of those now getting a discharge in straight bankruptcy, according to the study you cited, would be able to provide an adequate standard of living.

Therefore, if only 20 percent of those switch over to chapter XIII, it seems to me that leaves 29 percent in that category in your study, who would be getting along without any assistance from the referee.

Is that your judgment?

Mr. TWINEM. That 29 percent would continue to receive relief in straight bankruptcy.

I mean, if you applied the adequate test to its fullest extent——

Mr. JACOBS. I wonder if we are communicating here properly.

The study shows that 49 percent of those people now taking straight bankruptcy and receiving discharges don't need to really, if they want to continue on an adequate standard of living. You think that with passage of this legislation 29 percent of the people—it couldn't be 29 percent of the people in that category, but of that 49 percent of all bankruptcy discharges, 29 percent would continue on straight bankruptcy in your judgment?

Mr. TWINEM. Yes.

In other words, it was my guess that the referee, if you enacted this legislation, would be extremely liberal and would not be concerned with an adequate standard of living if they couldn't be afforded a comfortable standard of living he wouldn't dismiss their proceedings.

Mr. JACOBS. I think, Mr. Twinem, that this judiciary committee, which often considers technical matters must, in matters of bank-

ruptcy, also consider the social implications of this legislation. Therefore, I would ask you if you can enlighten this committee concerning just what the definition of "adequate standard of living" was in terms of this study?

That is to say, did they take the average George Stone, American, or somebody like that, or did they take the man with so many children, where they might be going to school—how did they distill all the factors and come up with this "adequate standard" for a given bankrupt?

Mr. TWINEM. Each economist and each sociologist would apply a little different philosophy and a little different test, and so it is hard to know how they screened them.

They give you the details in the report, and it is quite a complicated process.

Mr. JACOBS. I am sure of that, but I just wondered if you could enlighten the committee as to what broad standards might have been used.

Is this a man with three children, no children, children in high school, out of high school?

Mr. TWINEM. First, he is giving you a picture of what a typical bankrupt is. He has told you that a typical bankrupt is a person who is married, that he is in the age bracket of 21 to 35, that he has four children; that he is employed and that he has an income of \$5,000 to \$6,000 a year.

Mr. JACOBS. All right.

Mr. TWINEM. This is the typical bankrupt.

Mr. JACOBS. What part of the country was that survey taken from?

Mr. TWINEM. This was in Flint, Mich.

The other test came out about the same way in different areas of the country.

Mr. JACOBS. You have other surveys that have been made?

Mr. TWINEM. Yes, I have four of them here, and Professor Countryman says that he refers to 11 in his own paper. I don't know though what they are. I haven't examined his paper, but there are a number of other studies.

Mr. JACOBS. Is there any general definition offered in brief form of what is meant by an "adequate standard of living" according to this?

I don't think it would be out of order, if you have no objection, to calling upon Professor Countryman.

Mr. COUNTRYMAN. On page 2 of my statement, you will find Mr. Dolphin's idea of a comfortable and adequate standard of living.

Mr. JACOBS. Thank you.

I have just one other question to ask, and that is on this question of compulsion.

I think that possibly some Members of the Congress and possibly even members of the Judiciary Committee have yet to make a determination in their own minds about whether there should be compulsory use of chapter XIII. There has been testimony, really, both ways, but to characterize this legislation as noncompulsory legislation seems to me to engage in somewhat of an exaggeration.

For example, a man who is under a garnishee order and who needs some sort of relief, is a little bit like the fellow who is terribly thirsty,

and is shown two cans of water, one with mud in it and the other clear, and told that he can do whatever he wants about his problem, but he cannot drink from the can of clear water.

Do you think that analogy is fair?

MR. TWINEM. Yes, I do. We tried to consider a distinction between compulsory and voluntary chapter XIII.

Senator Gore introduced what I considered to be tantamount to compulsory chapter XIII.

Under the bill, his bill, the referee had the authority to convert to a chapter XIII proceeding.

Under this bill, the referee, has no such authority. But if this man is faced with a garnishment proceeding, and yet he has the adequate ability to pay his debts out of future earnings, then we are still going to give him relief from that garnishment if the creditor won't relax it, but we are not going to give him a discharge in bankruptcy from all of his obligations.

MR. JACOBS. Excuse me. How would we give him relief from the garnishment unless he took the proceeding that you are saying is not compulsory?

MR. TWINEM. If he wants the relief in the bankruptcy court he would have to take that relief; that's right.

MR. JACOBS. I wish you would discuss the analogy of the thirsty man, and the garnishment.

I see that rather clearly.

MR. TWINEM. Suppose we didn't have any XIII in the act, like before 1938? We still could have provided a standard that the man has to meet to be entitled to relief in straight bankruptcy, and that is what we have done here.

We don't care about whether he seeks relief under chapter XIII or not, but we are going to say for him, and I think Congress should have done this a long time ago, "There must be a standard to apply to XIII."

There are standards in other countries, why not here? Why do we let anybody, no matter how much ability they have to pay their debts, why do we let them readily come in and totally disregard and ignore their creditor just because they have no feeling for their obligations?

MR. JACOBS. The Chair might observe as an individual member of this subcommittee that he has not reached a conclusion about that particular question in his own mind. The Chair is directing inquiry to the characterization of either compulsory or optional, or noncompulsory, as designation to describe this legislation.

Now, I am not asking whether it should or should not be compulsory. I just want it to be characterized as it is in fact. It strikes me that this is just a little bit like a marine sergeant once said to me when I was in the boot camp, "I can't make you do it, but I can make you wish you had," I merely pursue this line of questioning so that we fly under the right colors whatever legislation we are proposing. I say again in all candor as an individual member that I haven't really completely reached the conclusion in my own mind that whether at some point under some circumstances some compulsion might not be warranted.

That I have reserved; but to say that the man under a garnishment proceeding who was about to lose his job can go out and get a cake

or something like that, seems to me is an unfortunate characterization of this provision.

Mr. TWINEM. We don't want it to be a matter of semantics.

Candidly, our committee believes this is not compulsory, the people who drafted this proposal thought it was—believe that it was not compulsory, and they were searching—

Mr. JACOBS. What does the fellow do under garnishment? It is not compulsory—

Mr. TWINEM. It would depend where he lives. If he lives in Michigan, he could go under State court receivership.

Mr. JACOBS. We are talking about Federal legislation.

Mr. TWINEM. You are asking me what to do. If I were an attorney advising a client like this, and I had no longer the right to petition in State bankruptcy, I would tell him what he could do: "First, if you want to protect yourself against this garnishment, you may make the chapter XIII petition and pay your debts out of future earnings. There is no longer any relief in the bankruptcy court for you because you can pay your debts out of future earnings."

But here he is faced with garnishment. He has neglected this debtor for a long period of time, and it is probably a willful neglect in his case, because once again you are dealing with the man who can pay out of future earnings and he probably is able to handle that debt.

We are not talking about this great majority of the wage earners that may be in the \$4,000 and \$5,000 category, who are really up against it and really need some kind of bankruptcy relief.

It is still there and available for them. We are only talking about this higher element in the structure that has an income that—an income that out of which, without sacrifice, they could pay their debts from future earnings.

Mr. JACOBS. Would you agree that as between the denial of straight bankruptcy relief and the availability of chapter XIII and the consequent prohibition of a garnishment order, a man's choice would be limited as to the best way to proceed as regards the good of himself and his family.

Mr. TWINEM. No, I wouldn't think that. It was my estimate that 80 percent of those proceeding in bankruptcy, straight bankruptcy, could still proceed in straight bankruptcy. First you have to disregard 80 percent of those that you are now considering, and so what do you have left to deal with? You have left maybe 20 percent, maybe 25—I don't know exactly where it is going to break. It is going to break on the test that is applied as to ability to pay, so you are only dealing with a very small proportion of the overall number of people who are proceeding in bankruptcy, and generally they don't need this extreme and harsh remedy—and straight bankruptcy is harsh—straight bankruptcy is a very extreme form of remedy. There are too many of them, and this is one way to screen them out.

Mr. JACOBS. Within that 20 percent—I have been handed some figures regarding a study made by Dolphin, is that the one you spoke of?

Mr. TWINEM. Yes.

Mr. JACOBS. And an adequate income for a family of five according to Professor Countryman's testimony, that is three children and a mother and father, I presume, is a little over \$3,000 a year.

Mr. TWINEM. Yes.

Mr. JACOBS. Would that be your personal definition of an "adequate income" or an "adequate standard of living"?

Mr. TWINEM. Mr. Chairman, in the first place, I don't—I didn't agree on the adequate standard of living as a satisfactory test, but I agreed that—and the test that I would apply would be a comfortable standard of living.

I would pick out only those who can pay with very little effort.

Mr. JACOBS. That "comfortable standard," according to this description, is about a thousand dollars more per family, and it is only a very few hundred dollars a year more per person.

Mr. TWINEM. Yes.

Mr. JACOBS. I know the hour is late, and I don't want to belabor the point.

I did want to receive your comments on what was meant by the term, used in your statement "adequate standard of living." And I think we have pretty well explored that in terms of the health and education of children in the prototype family of five. The other question concerned compulsion, and something I remember way back in law school about what you can do by direction and what you can do by indirection—and it strikes me this bill might very well represent a clear and maybe classic example of indirect compulsion, especially for a debtor with a garnishment order against him.

Mr. TWINEM. I am sorry it appeals to you that way, that you get that appraisal of it, because it was not intended to be that way at all.

It was intended to screen out the straight, unnecessary bankruptcy petitions and was not designed at all to force anybody under chapter XIII, because as I say, it wouldn't work as an involuntary proceeding, it has to be voluntary. And if you have the garnishment, then the question is whether you wish to pay that price.

Mr. JACOBS. Thank you for your patience and I pass to Mr. Poff.

Mr. POFF. Thank you, Mr. Chairman.

Other witnesses have suggested that it might be fair if the creditor were required by the court in such a proceeding to abide by a plan that had been submitted by the debtor and confirmed by the court. Did the American Bar Association consider this possibility?

Mr. TWINEM. The committee is presently considering this proposal by the National Bankruptcy Conference. It hasn't taken a final position on it as yet, but my offhand opinion is that you first have got a constitutional question under the 14th amendment, and then going on from there the question is whether, if it is handled properly, the court hasn't enough authority now to deal with it effectively.

Some bankruptcy courts apply one form of practice and some another, and out in Colorado, for example, they seem to have been pretty effective, and so have gone quite far in enforcing a security creditor to come under the plan.

It has gotten so that the creditors are very upset about the way it is applied there, but you can effectively give a lot of protection to the debtor and to the plan if you apply the right rules.

Mr. POFF. When you speak of a constitutional question, do you have reference to the property right—in the lien?

Mr. TWINEM. Yes, sir.

Mr. POFF. You indicated that you might be sympathetic with an expansion of the coverage beyond that of wage earner.

Mr. TWINEM. Yes.

Mr. POFF. If the word "debtor" in chapter XIII were expanded to include those entitled to the benefits of section 4(a) of the Bankruptcy Act that would have the effect of covering all natural persons and commercial corporations and others, other than those specifically named in section 4(a).

Is that correct?

Mr. TWINEM. I believe it is, if I understand you. In other words, to expand this, you would change the words "wage earner," where it appears in chapter XIII to "debtor," and at the same time you would amend section 606(3) to define debtor as any natural person within the meaning of section 4(a) of the act.

Mr. POFF. Well, section 4(a) now identifies those who may become bankrupts and it says any person except municipal, railroad, insurance, or banking corporation, or a savings and loan association, shall be entitled to benefits of this type.

That would include a commercial corporation.

Mr. TWINEM. Yes.

Mr. POFF. And if the word "debtor" were redefined in chapter XIII to mean all those people included in subsection (a) of section 4, then it would embrace, not only natural persons, but also commercial corporations.

Mr. TWINEM. Yes, sir; and if you wanted to strip out the "commercial corporation," you could.

You could do it by amending section 606(3) to provide that a debtor shall mean any natural person within the meaning of section 4a, and that would strip out the corporation.

But if you wanted to expand it to include corporations, you would be silent and say a debtor would mean any person within the meaning of section 4(a) of the act.

Mr. POFF. The act contains two definitions of the words "wage earner," one in section 606(8) and the other in the first section.

The definitions are somewhat different. In your judgment, would it be necessary to amend the words "wage earner" as they appear in sections of the act other than chapter XIII?

Mr. TWINEM. Well, no; I don't believe so. Of course, there is another provision in the act. You couldn't petition a wage earner in involuntary bankruptcy. I contend that you are not doing that anyway.

Mr. POFF. No.

Mr. TWINEM. In my opinion, it wouldn't be necessary to change that.

Mr. POFF. Section 4(b) explicitly excludes the wage earner and the farmer.

I believe that is all, Mr. Chairman.

Mr. JACOBS. Mr. McClory?

Mr. McCLORY. Thank you, Mr. Chairman.

I was concerned with regard to some earlier testimony which related this legislation to imprisonment for debt, and I wondered where that notion comes from? Does this act operate in such a way where courts will imprison these debtors in case they select chapter XIII?

Mr. TWINEM. Not in my opinion, sir.

Mr. McCLODY. Are they in contempt of court if they don't comply with the plan, or something of that nature?

Mr. TWINEM. No, sir; in my opinion they are not.

As of today, if they amend their proceedings to a chapter XIII plan, it is still a voluntary thing, and they still can drop out of the plan. The referee can dismiss it if they drop out or fail to carry out the plan.

If they do it willfully, he can dismiss it without a discharge. If they stumble and have difficulty, he can reconsider and give them additional time or give them some changes in the plan, but it in no way, no wise, imposes any form of compulsion to carry out the plan.

I don't think that is any feasible way to do that.

Mr. McCLODY. I don't see the analogy there. That is the thing that concerns me. I want to accept legitimate criticism of their legislation, and also, of course, any number of suggestions that have been made to improve the legislation, but I am a little sensitive about something that I thought had real merit. I am sure you would feel that way, too.

Let me ask this further question: As I see it, under straight bankruptcy, the person is not encouraged to adopt a chapter XIII proceeding. The person who holds a chattel mortgage, or the person who is selling under a contract and can repossess, gets an unconscionable advantage, and the creditor who lends money on the basis of good faith and depends upon the earning capacity of the debtor to repay is left out on the limb, and there is tremendous discrimination, in my opinion, against that sort of creditor.

Is that right?

Mr. TWINEM. Yes, I think that's right, and that is one of the reasons why chapter XIII should be encouraged. The debtor gets a good deal of protection under chapter XIII that he doesn't get under straight bankruptcy.

I wouldn't want to make chapter XIII compulsory, but I think the debtor is better off under it than in straight bankruptcy. He is protected against suits, garnishment, he is given various other types of protection that he doesn't get in straight bankruptcy, and he is protected against unconscionable contracts, and the court can almost go to the extent of rewriting these contracts if they are unreasonable.

He is certainly protected against usurious contracts. If the creditor repossesses in straight bankruptcy, he is still going to show the full amount of debt and interest.

If there is any surplus, it would go to the bankruptcy court, but the creditor is going to go as far as he can in many cases in taking what he can, and the debtor—if the creditor is unconscionable in his conduct—the debtor has no protection that he would have under XIII.

Mr. JACOBS. Mr. Wiggins?

Mr. WIGGINS. At the present time, if a debtor is in financial straits and wishes to avail himself of the benefits of the Bankruptcy Act, he has the option of filing a petition for a straight discharge in bankruptcy, or voluntarily making the election to file a petition under chapter XIII.

Now, if that debtor makes the election to file under chapter XIII, he has no problem and this legislation wouldn't affect him at all. Is that true, sir?

Mr. TWINEM. Yes, sir.

Mr. WIGGINS. We are only dealing with the debtors, then, who make the initial determination to file for straight discharge.

Under the proposed legislation, as I understand it, the referee would have the right to interrogate the debtor as to whether or not he might qualify for chapter XIII.

If the debtor agrees with the referee and voluntarily dismisses his original petition or refiles, or amends, whatever has to be done, and files under chapter XIII, I agree with you, there certainly is no compulsion involved, but under the proposed legislation, as I understand it, doesn't the referee have a right to impose his will upon the debtor after a proper showing and compel an action under chapter XIII?

Mr. TWINEM. No. If the debtor's attorney said, "We don't want any part of chapter XIII proceedings," then the only thing the referee can do is dismiss the straight bankruptcy proceeding. He can in no event and in no case compel the debtor to refile or convert—

Mr. WIGGINS. We are at the point that bothered Mr. Jacobs, whether that involved compulsion.

He has the alternative of accepting the decision of the referee and availing himself of chapter XIII, or returning to face the wolves.

Mr. TWINEM. Yes, but we are dealing with a relatively small portion of these cases and we are saying to these people, "In the past you have been able to get a discharge no matter how many assets you had, no matter that you had \$10,000 in the bank," and so forth.

But now we are saying to him for the first time, "We are going to apply a test to determine whether you are entitled to this relief, and the test is, can you pay comfortably out of future earnings or not, and if you can't" and that will be a good percentage of the cases, then he will continue to proceed as he does today.

Mr. WIGGINS. I think that point of view has considerable merit, but I think we ought to call a spade a spade and say in fact it has some compulsion attached to it, and maybe that is desirable.

Mr. TWINEM. In my opinion, it doesn't really have the compulsion that seems to bother some people, and that is it has only the compulsion that if you want this type of relief, this is how you get it, if you want the protection of the court, and under your circumstances, this is the avenue, this is your form of redress to meet your particular situation.

Mr. WIGGINS. Thank you very much for your help.

Mr. JACOBS. Are there any questions? Counsel has some questions.

Mr. ZELENKO. One question, Mr. Chairman.

I understand the motivation behind this proposal is not only to help creditors but to provide amelioration to debtors. Is that correct?

Mr. TWINEM. Yes. It was thought this would eliminate some filings and at the same time encourage additional filings under chapter XIII where they are better off in many cases than they would be in straight bankruptcy.

Mr. ZELENKO. So it is to benefit debtors that you propose this?

Mr. TWINEM. Yes, of course.

Mr. ZELENKO. Do you believe the present system under chapter XIII benefits debtors?

Mr. TWINEM. I do, where it is used.

Mr. ZELENKO. And it is a voluntary procedure, wherein the debtor chooses that route.

Mr. TWINEM. Yes. Under this bill, it will encourage him to choose that.

Mr. ZELENKO. To the extent that this bill forecloses any other avenue for discharging debts in the Federal court is it compulsory?

Mr. TWINEM. If he wants the bankruptcy court as an avenue, he has to meet the standards imposed.

Mr. ZELENKO. Thank you.

Mr. JACOBS. The committee expresses its gratitude to Mr. Twinem for his appearance. Several labor unions have joined together to make a statement in opposition to bills H.R. 1057 and H.R. 5771, and have asked that it be included in the record, and without objection it will be included in the record.

(The statement referred to follows:)

STATEMENT IN OPPOSITION TO BILLS H.R. 1057 AND H.R. 5771

This statement is submitted on behalf of the following labor unions:

New York Hotel & Motel Trades Council, AFL-CIO, and its several affiliates

Bakery and Confectionery Workers International Union of America, Local No. 3

Truck Drivers Local Union No. 807, I.B. of T.

Chefs, Cooks, Pastry Cooks and Assistants Union of New York, Local 89, AFL-CIO

Pocketbook and Novelty Workers' Union, New York, Local No. 1, AFL-CIO

Sheet Metal Workers International Association Local Union No. 28 of New York City

Association of Theatrical Press Agents and Managers, AFL-CIO

Local Union No. 277, I.B. of T.

Local 325, Cooks, Countermen, Soda Dispensers, Food Checkers, Cashiers and Assistants Union

Local Joint Executive Board of New York City, AFL-CIO
with a membership of tens of thousands of wage earners.

On behalf of these labor unions, and the wage earners they represent, we wish to record opposition to the compulsory Chapter XIII proceeding proposed by Bills H.R. 1057 and H.R. 5771, on the grounds that it is unfair and discriminatory.

The Chapter XIII proceeding *presently* permits an insolvent wage earner to voluntarily enter into a Court approved plan whereby his debts are paid out of future earnings or wages.

H.R. 1057, introduced by Mr. Poff on January 10, 1967 in the House of Representatives, and H.R. 5771, an identical Bill, introduced by Mr. McClory on February 20, 1967 in the House of Representatives, provide as follows:

H.R. 1057 AND H.R. 5771

A BILL To amend the Bankruptcy Act with respect to the use of Chapter XIII

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 55(b) of the Bankruptcy Act (11 U.S.C. 91(b)) is amended to read as follows:

"b. At the first meeting of creditors, the judge or referee shall preside and, before proceeding with other business, shall, if the bankrupt is a wage earner within the meaning of subsection (8) of section 607 of this Act, determine whether the bankrupt has shown that adequate relief cannot be obtained under Chapter XIII of this Act. In the event that the judge or referee shall determine that the bankrupt has failed to make such a showing, he shall enter an order vacating the order of adjudication and dismissing the bankruptcy proceedings with notice to all of the bankrupt's creditors, unless, within such time as the judge or referee shall fix, the petition be amended to comply with the requirements of chapter XIII for

the filing of a debtor's petition. In the event that the bankrupt is not a wage earner or shall make such a showing as aforesaid, the judge or referee may then allow or disallow the claim of creditors there presented, and shall publicly examine the bankrupt or cause him to be examined, and may permit creditors to examine him."

These Bills, which seek to amend the present Section 55(b) of the Bankruptcy Act (11 U.S.C. 91(b)) :

"(b) At the first meeting of creditors, the judge or referee shall preside and, before proceeding with other business, may allow or disallow the claims of creditors there presented, and shall publicly examine the bankrupt or cause him to be examined, and may permit creditors to examine him", compel a wage earner to submit to a proceeding against his will in which his future earnings are pledged and divided amongst his creditors. No other insolvent is subjected to such treatment.

The relief of "discharge in bankruptcy" available to all other debtors in Bankruptcy Court, is, under these Bills, now to be denied to wage earners. There can be no justification for such discrimination against wage earners, who, more than others, need the protection of a fair and humane Bankruptcy Act.

In Chapter X proceedings involving corporations, partnerships or individual businessmen, there is no compulsory proceeding making the debtors liable to pay creditors out of future earnings. The very purpose of the Bankruptcy Act is to rehabilitate the debtor and to give him a new lease on life. Only such non-dischargeable debts as taxes, priority wage claims and those listed in Section 17(a) of the Bankruptcy Act, must be paid by the debtor.

Chapter XI, like Chapter XIII of the Bankruptcy Act, provides for voluntary proceedings whereby debtors who so choose may pay their creditors pursuant to a court approved plan. There is no provision for an involuntary Chapter XI plan, nor should one be imposed upon wage earners under Chapter XIII.

Wage earners have a fixed income which is subject to the ever-spiralling cost of living and entirely contingent upon a healthy economy. Even in the midst of prosperity, employers are closing their doors and throwing vulnerable wage earners out of work. These Bills would create additional and onerous pressures on wage earners whose financial difficulties are already so overwhelming as to bring them before the Bankruptcy Court. To deny such a debtor this relief would certainly not help the wage earner nor the public. The Bankruptcy Court should give him the same, if not greater, protection it affords all other debtors.

In most cases, wage earners fall into debt and become insolvent as a consequence of having over-extended themselves in installment purchases. Frequently, this results from their inability to resist the high pressure tactics of salesmen, whose concern is not with the customers' ability to pay, but rather with the commissions he will earn from the consummation of a sale. Conditional sales purchasers are already harassed under State Laws which permit income executions, and they should not be further exposed to the pressures these Bills will create.

If the creditors seeking these Bills need protection against losses from installment sales, they would be well advised to investigate their prospective purchasers more carefully before selling their products rather than seeking this severe and discriminatory legislation.

In conclusion, we wish to state that a wage earner should be permitted to choose the proceeding which best suits him: either filing a petition in bankruptcy, or voluntarily proceeding under Chapter XIII as it exists today.

For all of the foregoing reasons, on behalf of the labor unions which we represent, we wish to register strong opposition to these measures and recommend that they be defeated.

COHN AND GLICKSTEIN, *Attorneys.*

Mr. JACOBS. The committee will stand adjourned subject to call of the Chair.

(Whereupon, at 4:53 p.m., the subcommittee adjourned, to reconvene at the call of the Chair.)

STATEMENT OF THE CHAMBER OF COMMERCE OF THE UNITED STATES ON H.R. 1057
BY F. TURNER HOGAN *

The Chamber of Commerce of the United States supports H.R. 1057, and urges its prompt enactment in the best interests of both business and consumers.

Personal bankruptcies have risen to an alarmingly high level. As a result :

Many of our citizens are being enveloped needlessly in the stigma of bankruptcy; and

Other consumers are paying at least part of these losses, through prices that must necessarily be set higher to compensate for bad debts.

The Chamber believes that a major reason for this alarming trend is the failure to utilize fully Chapter XIII of the Federal Bankruptcy Act; therefore, we applaud the intent of H.R. 1057 to assure better use of Chapter XIII.

We also believe prompt enactment is called for, inasmuch as there is current agitation for mass bankruptcy filings—a movement which, if carried out, would affect adversely not only the individuals directly involved, but also the economy generally.

Chapter XIII of the Bankruptcy Act provides an opportunity for the petitioner in a personal bankruptcy proceeding to plan to pay his debts out of future earnings over an extended period of time, rather than declare bankruptcy. Unfortunately, there is evidence that this plan for delayed payment is too often ignored. Under present law, both the judge and petitioner may ignore Chapter XIII if they choose. And the petitioner may succeed with a straight bankruptcy petition, even though his income may be sufficient to pay his debts over an extended period.

H.R. 1057 would amend Chapter XIII so that the judge would have to determine if the petitioner is financially able to pay his debts in this manner. If petitioner is able, the judge would be required to dismiss the proceedings, unless the petition is amended to comply with Chapter XIII.

It is reasonable to assume Congress intended Chapter XIII be used whenever feasible. It has become evident that either the petitioner or the presiding officer of the court, or possibly both, need inducements to use Chapter XIII, when the petitioner is financially able.

* * * * *

In 1940, more than 39,000 nonbusiness bankruptcies were filed. In 1966, the figure increased to 176,000. This is a more than quadruple increase in just 26 years.

Nonbusiness filings in 1940 amounted to 74.79 per cent of total bankruptcy filings. In 1966, nonbusiness filings were 91.5 per cent of the total.

On a dollar basis, in the fiscal year ending January 3, 1960, \$469,865,567 was discharged by wage earners through bankruptcy. By 1965, in the space of only five years, this total had leaped to approximately \$1,352,413,394.

For the fiscal year ending June 30, 1967, it was estimated that more than 200,000 bankruptcy petitions would be filed and that nearly \$1,500,000,000 would be washed down the bankruptcy drain. This is a highly alarming increase and, in the interest of the national economy, a constructive solution to this type of debt problem is needed.

* * * * *

Education and credit counseling will help bring about a solution to debt problems. And these programs are on the increase across the country. But many citizens, regardless of education and counseling, find themselves personally in debt to such an extent that some form of relief is necessary. There must be a procedure that will allow these people to meet their obligations over a period of time and avoid the stigma of bankruptcy. That procedure exists now in Chapter XIII of the Federal Bankruptcy Act. It should be used in all possible cases.

If the present avoidance of Chapter XIII continues, it most certainly will have detrimental effects on the economy and on all consumers. The financial integrity and security of both individuals and businesses must be protected and maintained.

The tremendous volume of personal bankruptcies is inevitably reflected in prices. When a debtor declares straight bankruptcy and is released from paying his bills, the businesses that are his creditors lose money. This loss becomes a cost of doing business and a possible cause of business failure and must be re-

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flected in the prices paid by all consumers. The one and a half billion dollars in debts estimated to be released in the fiscal year ended June 30, 1967, through straight bankruptcy petitions, is an astounding amount that must be made-up ultimately by other consumers.

Already, at least one ethnic group leader is threatening to urge "tens of thousands of poor people" to declare bankruptcy en masse across the country—assumedly under the protection of the courts' avoidance of Chapter XIII. Not only would this be an injustice to creditors, but it would soil the credit record of the petitioners and possibly drive them into the hands of loan sharks and unethical merchants. Any such movement would be a dangerous abuse of the purpose and spirit of the Federal Bankruptcy Act—an abuse that could and should be avoided by proper use of Chapter XIII.

* * * * *

The National Chamber recognizes the need for a personal bankruptcy law to protect those who find themselves in a personal financial crisis. It also recognizes the need for a respectable and equitable way out of such a crisis, short of bankruptcy. We believe the use of Chapter XIII would answer both needs.

If Chapter XIII is worth having as part of the Federal Bankruptcy Act, it is worth using—and its use should be mandatory whenever feasible.

SUPREME COURT OF THE UNITED STATES

No. 694.—OCTOBER TERM, 1965.

Warren W. Perry, Petitioner,	}	On Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit.
v.		
Commerce Loan Company.		

[March 7, 1966.]

MR. JUSTICE CLARK delivered the opinion of the Court.

Perry, a furnace operator employed by Moore Lead Company, filed a petition in the District Court under Chapter XIII of the Bankruptcy Act, 52 Stat. 930 (1938), as amended, 11 U. S. C. §§ 1001–1086,¹ requesting confirmation of his plan for an extension of time within which to pay his debts out of his future wages. In his plan he proposed to pay his debts of \$1,412 in 28 equal monthly installments of \$60 from his wages of \$265 a month. On the hearing for confirmation of the plan, however, it appeared that Perry had previously filed a petition in straight bankruptcy and obtained a discharge therein in 1959, within six years of the filing of this proceeding. On motion of the respondent Commerce Loan Company, the referee dismissed the plan on the ground that the previous bankruptcy was a bar thereto under the provisions of § 14 (c) (5) of the Act.² On review the District Court upheld the dismissal. The Court of Appeals affirmed. 340 F. 2d 588. We granted certiorari,

¹ All United States Code citations herein refer to the 1964 edition.

² 52 Stat. 850 (1938), as amended, 11 U. S. C. § 32 (c) (5):

“(c) The court shall grant the discharge [in bankruptcy] unless satisfied that the bankrupt has . . . (5) in a proceeding under this title commenced within six years prior to the date of the filing of the petition in bankruptcy had been granted a discharge, or had a composition or an arrangement by way of composition or a wage earner’s plan by way of composition confirmed under this title . . .”
11 U. S. C. § 32 (c) (5).

382 U. S. 889, in view of a conflict on the point among the courts of appeals.³ We conclude that confirmations of wage-earner plans by way of extensions are not affected by § 14 (c)(5), and, therefore, reverse the judgment below.

I.

Background of Chapter XIII.

Although statutory relief for the financially distressed wage earner had been available to some extent as early as the Bankruptcy Act of 1867, 14 Stat. 517, Congress found in its study prior to the 1938 revision of the bankruptcy laws that there were no effective provisions for the complete repayment of the wage earner's debts suited to his problems. H. R. Rep. No. 1409, 75th Cong., 1st Sess., 53 (1937). For example, compositions under § 12 of the 1898 Act, 30 Stat. 549, were available to the wage earner, but the relief afforded was unsatisfactory. Section 12 proceedings, which were primarily adaptable for use by business entities, were disproportionately expensive in view of the small sums ordinarily involved in wage earner cases; they lacked flexibility; and they did not provide for jurisdiction of the court subsequent to confirmation. Other provisions of the Act had similar disadvantages. Faced with inadequate relief under the federal bankruptcy laws and often with little protection from creditors under state law, the only course usually open to the wage-earning debtor was straight bankruptcy. In such proceedings, everyone lost—the creditors by receiving a mere fraction of their claims, the debtor by bearing thereafter the stigma of having been adjudged a bankrupt. In designing a remedy for the di-

³ Compare *In re Schlageter*, 319 F. 2d 821 (C. A. 3d Cir. 1963), and *Perry v. Commerce Loan Co.*, *supra*, with *Edins v. Helzberg's Diamond Shops, Inc.*, 315 F. 2d 223 (C. A. 10th Cir. 1963), and *In re Mahaley*, 187 F. Supp. 229 (D. C. S. D. Cal. 1960). See also *In re Mayorga*, — F. 2d — (C. A. 9th Cir. 1966).

lemma facing a debtor seeking to repay, rather than avoid, his obligations, the Congress settled upon the wage-earner extension-of-time procedures of Chapter XIII. The chapter gave—and was intended to give—to the wage earner a reasonable opportunity to arrange installment payments to be made out of his future earnings. Congress clearly intended to encourage wage earners to pay their debts in full, rather than to go into straight bankruptcy or composition, by offering two inducements: (1) avoidance of an adjudication of bankruptcy with its attendant stigma; and, at the same time, (2) temporary freedom during the extension from garnishments, attachments and other harassment by creditors. H. R. Rep. No. 1409, 75th Cong., 1st Sess., at 52-55.

History demonstrates that extension plans under Chapter XIII are fulfilling the purposes intended. The records of the Administrative Office of the United States Courts show that over the past 20 years more than 20% of all proceedings filed under the Bankruptcy Act by wage earners have been for plans under Chapter XIII, the overwhelming majority of these being for extension plans.⁴ Since many wage earners who go into bankruptcy do not proceed under Chapter XIII because they are unemployed (and consequently have no earnings to use for extension arrangements), have an inextricably large indebtedness, or are simply unaware of the existence of an alternative to straight bankruptcy, the 20% figure is even more significant. Moreover, large sums of

⁴ Chapter XIII also provides for wage-earner plans by way of composition. Compositions under that chapter, however, are almost insignificant in the operation of wage-earner plans because most creditors will not give the necessary approval. The latest published statistics show that 95% of the funds paid to creditors under Chapter XIII proceedings derive from extensions rather than compositions. Administrative Office of the United States Court, Tables of Bankruptcy Statistics, Table F 11 (1964) (by computation).

money are annually returned to creditors under extension plans, the current rate being well over \$26,000,000. As wage earners ordinarily have little or no assets available for distribution in straight bankruptcy, these sums represent settlements which the debtors would otherwise be unable to effect and the creditors unable to obtain. See Note, *The Wage Earner Plan—A Superior Alternative to Straight Bankruptcy*, 9 *Utah L. Rev.* 730 (1965); Allgood, *Operation of the Wage Earners' Plan in the Northern District of Alabama*, 14 *Rutgers L. Rev.* 578 (1960).

In light of the proven advantages of extension plans, the Congress has re-expressed its legislative purpose in amendments to Chapter XIII adopted since the original enactment. A report to the House of Representatives expresses it in these words:

"[C]hapter XIII provides a highly desirable method for dealing with the financial difficulties of individuals. It creates an equitable and feasible way for the honest and conscientious debtor to pay off his debts rather than having them discharged in bankruptcy. The power of the court to change the amount and maturity of installment payments without affecting the aggregate amount of such payments makes Chapter XIII particularly applicable to the present-day financial problems generated by heavy installment buying." H. R. Rep. No. 193, 86th Cong., 1st Sess., 2 (1959).

And similarly, the Senate report states:

"We think there can be no doubt . . . that a procedure by which a debtor who is financially involved and unable to meet his debts as they mature, over a period of time, works out of his involvement and pays his debts in full is good for his creditors and

good for him." S. Rep. No. 179, 86th Cong., 1st Sess., 2 (1959).

It is with this underlying policy in mind that we turn to a consideration of the problem posed here; *i. e.*, whether confirmation of an extension plan is barred by a discharge in bankruptcy obtained within the previous six years.

II.

Chapter XIII requires the confirmation of a wage-earner extension plan if "the debtor has not been guilty of any of the acts or failed to perform any of the duties which would be a bar to the discharge of the bankrupt" § 656 (a)(3). And Chapter III commands that a discharge of a bankrupt shall be granted unless the court is satisfied that the bankrupt has "within six years prior to bankruptcy been granted a discharge, or had a composition or an arrangement by way of composition or a wage earner's plan by way of composition confirmed under this Act" § 14 (c)(5). The "discharge" of a debtor under a wage-earners plan shall issue after compliance with the provisions of the confirmed plan, § 660, c. XIII, 11 U. S. C. § 1060. If at the expiration of three years from the date of confirmation of the plan the debtor has not completed his payments in accordance with his plan the court may, after notice and hearing, discharge the debts and liabilities dischargeable under the plan, *provided* the court is satisfied that the debtor's failure to make all of his payments "was due to circumstances for which he could not be justly held accountable." § 661, c. XIII, 11 U. S. C. § 1061. And finally, § 602, of Chapter XIII⁵ declares that the provisions of

⁵ 11 U. S. C. § 1002: "The provisions of chapters 1-7, inclusive, of this title shall, insofar as they are not inconsistent or in conflict with the provisions of this chapter, apply in proceedings under this chapter"

Chapters I through VII of the Bankruptcy Act, insofar as they are not inconsistent or in conflict with the provisions of Chapter XIII, apply in proceedings thereunder.

We should note at the outset that in his present application for relief Perry did not file a straight, voluntary bankruptcy action in the District Court, nor "a composition or an arrangement by way of composition or a wage earners plan by way of composition." He proposed to pay all his debts, secured and unsecured, and sought only an extension of time—28 months—in which to pay them in equal installments from his future wages. Ordinarily, a wage earner seeking to obtain the benefits of extension proceedings under Chapter XIII need only file a plan that meets the approval of the majority of his creditors, § 652, 11 U. S. C. § 1052, and is confirmed by the court; whereupon the plan becomes binding, § 657, 11 U. S. C. § 1057, and the appointed trustee commences collecting and disbursing to the creditors the periodic payments provided under the plan. Extension plans, therefore, differ materially from straight bankruptcy, arrangements under Chapters XI and XII, and wage-earner plans by way of composition, all of which contemplate only a partial payment of the wage earner's debts. Indeed, under an extension plan, the wage earner who makes the required payments will have paid his debts in full and will not need a discharge, even though the Act provides for a formal one. § 660.

In view of these considerations and the purposes of Chapter XIII as outlined above, we do not believe that the Congress intended to apply the six-year bar of § 14 (c) (5) to the confirmation of wage-earner extension plans. The six-year bar was enacted 35 years prior to the adoption of Chapter XIII, 32 Stat. 797 (1903), at a time when no relief corresponding to extension plans existed under the Bankruptcy Act. The unmistakable

purpose of the six-year provision was to prevent the creation of a class of habitual bankrupts—debtors who might repeatedly escape their obligations as frequently as they chose by going through repeated bankruptcy. See H. R. Rep. No. 1698, 57th Cong., 1st Sess., 2 (1902); *In re Thompson*, 51 F. Supp. 12, 13 (1943). But an extension plan has no escape hatch for debtors, it is “a method by which, without resorting to bankruptcy proceedings in the usual sense, a wage earner may meet the claims of creditors.” S. Rep. No. 179, 86th Cong., 1st Sess., 2 (1959). To apply the six-year bar at the time of confirmation of an extension plan would be both illogical and in head-on collision with the congressional purpose as announced in the adoption and design of extension plans under Chapter XIII.⁶ Even if a literal reading of these provisions suggested the application of § 14 (c)(5) to extensions plans, we would have little hesitation in construing the Act to give effect to the clear policy underlying Chapter XIII. As was said in *United States v. American Trucking Ass'ns*, 310 U. S. 534, 543 (1940):

“There is, of course, no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes. Often these words are sufficient in and of themselves to determine the purpose of the legislation. In such cases we have followed their plain meaning. When that meaning has led to absurd or

⁶ Such a collision undoubtedly affects the functioning of the Act. The Administrative Office of the United States Courts reports that a “pronounced drop in Chapter XIII filings” has been noted in the districts in the Sixth Circuit as a result of the holding in *Perry*. Administrative Office of the United States Courts, Memorandum for the Committee on Bankruptcy Administration of the Judicial Conference of the United States, Report on the Use of Chapter XIII, p. 2 (June 22, 1965).

futile results, however, this Court has looked beyond the words to the purpose of the act. Frequently, however, even when the plain meaning did not produce absurd results but merely an unreasonable one 'plainly at variance with the policy of the legislation as a whole' this Court has followed that purpose, rather than the literal words."

But such a literal reading is not apparent in this case. Section 656 (a)(3) does not, on its face, state that a court may confirm an extension plan only if the debtor is eligible for a discharge in bankruptcy. Rather, the language of the section speaks, ambiguously, of "guilty" acts and unfulfilled duties. There is, of course, no unfulfilled duty involved in § 14 (c)(5). Moreover, a prior bankruptcy is hardly a "guilty" act within the usual meaning of that word, and its use as a reference to § 14 (c)(5) is strained indeed. In fact, the legislative history of § 14 (c) lends some support to a view that a prior discharge is not a "guilty" act. In 1903, when the forerunners of subdivisions (3) through (6) were originally added to § 14 (c) the House report stated:

"This amendment also provides four additional grounds for refusing a discharge in bankruptcy: (1) Obtaining property on credit on materially false statements; (2) making a fraudulent transfer of property; (3) having been granted or denied a discharge in bankruptcy within six years, and (4) having refused to obey the lawful orders of the court or having refused to answer material questions approved by the court. *No person who has been guilty of any of these fraudulent acts should be discharged, and a person who has refused to obey the order of the court ought not to be discharged, and it is quite clear that no person should have the benefit of the act as a voluntary bankrupt oftener than*

once in six years." H. R. Rep. No. 1698, 57th Cong., 1st Sess., 2 (1902). (*Italics added.*)

This language might be construed to set apart acts which are criminal or reprehensible in nature and to consider a prior bankruptcy to be something other than a "guilty" act. But we need not, and do not, go so far as to place this interpretation on the words "guilty acts." It suffices that we find in them sufficient ambiguity to impell recourse to the legislative purposes, outlined above, underlying § 14 (c)(5). And while the identical language of § 656 (a)(3) has been a part of the Bankruptcy Act since 1898, as a restriction to confirmation of compositions under what is now § 366 (3), 52 Stat. 911, as amended, 11 U. S. C. § 766 (3) and § 472 (3), 52 Stat. 923, as amended, 11 U. S. C. § 872 (3), there is no indication that its enactment in Chapter XIII was intended to bar confirmation of wage-earner extensions. Indeed, it would seem that the absence of any legislative history bearing on the adoption of this provision in Chapter XIII indicates that its inclusion was a legislative oversight,⁷ at least insofar as it bears on wage-earners' extension plans.

This oversight is, of course, cured by the provisions of § 602, which further buttress our conclusion. That section directs that the provisions of Chapters I through VII, which include § 14 (c)(5), are incorporated into Chapter XIII only "insofar as they are not inconsistent or in conflict with the provisions of this chapter." The rationale of § 14 (c)(5)—the prevention of recurrent

⁷ This is not the only example of drafting oversights in the Act. Although § 14 (c)(5) was amended in 1938 to include a reference to wage-earner compositions, the provision in that section relating to confirmation of a composition was not deleted even though § 12 of the 1898 Act, 30 Stat. 549, under which such a composition might have been confirmed, was repealed in the same enactment.

avoidance of debts—is so inconsistent with the aims of extension plans as to fall squarely within the exception of § 602.

It is claimed, however, that § 686 (5) of Chapter XIII, 11 U. S. C. § 1086 (5), indicates a contrary result. We think not. This provision, in setting the effective date of the chapter, provides that confirmations thereunder “shall not be refused because of a discharge granted or a composition confirmed prior to the effective date of this amendatory Act.” It must be remembered that extension plan relief of Chapter XIII was novel to the law of bankruptcy. However, both compositions and straight bankruptcies were old on the books. The Congress, we believe, was only making certain, insofar as extensions are concerned, that the old procedures would not affect the new. This would be consistent with the purpose of the Congress not to make § 14 (c)(5) applicable to confirmations in extension plan cases. Rather than an illogical exemption from the six-year bar, given in cases where a discharge had been received before—but not after—the new Act, § 686 (5) merely gave expansive effect to the congressional purpose by making it clear that the remedy afforded be available retroactively as well as prospectively.

We emphasize that our construction of the Act does not preclude application of § 14 (c)(5) to confirmations of general arrangements under Chapter XI or to real property arrangements under Chapter XII. It is true that restrictions identical in phrasing to § 656 (a)(3) appear both in Chapter XI, § 366 (3), and in Chapter XII, § 472 (3). The relief afforded in those chapters, however, represents a wholly different statutory scheme from wage-earners’ extensions, and the restrictive provisions are not, therefore, in *pari materia*. Sections 366 (3) and 472 (3) neither impart to nor receive from § 656 (a)(3) a meaningful effect. Nor does our construction

imply an immunity from the six-year bar to those seeking confirmation of wage-earner compositions. A composition under Chapter XIII, unlike extensions, is closely akin to straight bankruptcy and to proceedings under Chapters XI and XII, for under such a plan the debtor is discharged from his debts and claims of the creditors are only partially paid. *In re Jenson*, 200 F. 2d 58 (1952), cert. denied, 345 U. S. 926 (1953), but see *In re Goldberg*, 53 F. 2d 454 (1931). It is both logical and consistent with the underlying purposes of § 14 (c)(5) that confirmation of wage-earner compositions be barred by prior bankruptcy, since repeated use of such plans would, in effect, provide an opportunity for abuse of the Act.

It has been argued that extension plans do not completely avoid the possibility of adjusting the wage earner's debts. It is true that § 660 provides for discharge after compliance with the provisions of a Chapter XIII plan. While this section applies to wage-earner compositions as well as to extensions, a "discharge" thereunder has a wholly different impact where an extension is involved. In the latter case a discharge is little more than a mere formality. It is also claimed that § 661 presents a somewhat more troublesome objection. That section as we have noted may allow a wage earner to obtain a release from all dischargeable debts if, after notice and hearing, the court is satisfied that the failure of the debtor to comply with the plan was due to circumstances for which he could not be held justly accountable. However, we see no serious problems in this section. First, experience has shown that almost all plans approved under the Act envision repayment within three years. The problem, therefore, is not likely to arise. Second, there are adequate provisions for notice and hearing prior to a discharge under § 661. Objecting creditors may raise § 14 (c)(5) as a bar to relief if and when the debtor seeks such relief. A request for relief

under § 661 would, in effect, constitute an attempt to transpose an extension plan into a composition, and a grant of relief thereunder would, at that time, be tantamount to a confirmation of a composition. The six-year bar would, therefore, be operative in such a situation. In view of this, as well as the power of the court to make certain that the provisions of the chapter are not abused, we see no reason to allow this section alone to destroy the beneficial purposes of enactment.⁸

For the foregoing reasons, we conclude that petitioner's plan should have been confirmed.

Reversed and remanded.

⁸ We note that the National Bankruptcy Conference has proposed amendments to the Act which are intended to clarify the interrelationship of §§ 14 (c) (5), 656 (a) (3), and 661. The proposed clarification is in accord with our construction of the Act. See H. R. 20, 89th Cong., 1st Sess. (1965). The Judicial Conference, upon request of the Congress, has submitted its views approving the bill. Letter from the Director of the Administrative Office of the United States Courts to the Chairman of the Committee on the Judiciary, House of Representatives (September 29, 1965). See also Report of the Proceedings of the Judicial Conference of the United States, at 68 (September 22-23, 1965).

SUPREME COURT OF THE UNITED STATES

No. 694.—OCTOBER TERM, 1965.

Warren W. Perry, Petitioner,	} On Writ of Certiorari to	
v.		the United States Court
Commerce Loan Company.		of Appeals for the Sixth Circuit.

[March 7, 1966.]

MR. JUSTICE HARLAN, dissenting.

The result reached by the Court may well be desirable, but in my opinion it is one that cannot be attained under the present statute within the proper limits of the judicial function.

Chapter XIII of the Bankruptcy Act establishes procedures for the relief of wage earners who are unable to meet their debts as they mature. Two types of procedures are made available: extension plans under which the wage earner's debts are intended to be paid off in full over a period of time, and composition plans under which only a percentage of debts are recoverable. Referring to both types of plans, § 656 of the Bankruptcy Act, 11 U. S. C. § 1056 (1964 ed.), provides that "a plan" shall not be confirmed if the debtor has "been guilty of any of the acts or failed to perform any of the duties which would be a bar to the discharge of the bankrupt" To ascertain what would be a bar to the discharge of a bankrupt one must turn to § 14 (c), 11 U. S. C. § 32 (c) (1964 ed.), which provides, among other things, that no discharge may be granted if the bankrupt has been granted a previous discharge within six years. § 14 (c)(5). It is undisputed that petitioner here was so discharged, and there is no question but that he would have been refused another discharge in bankruptcy at the time he applied for this extension plan. The statu-

tory scheme thus plainly seems to bar him from obtaining Chapter XIII relief as well.

The process by which the Court has undertaken to release the debtor from the impact of these straightforward statutory provisions seems to me wholly unavailing. The Court's major argument is built upon its reading of the word "guilty" in § 656 (a)(3). As already noted that section denies confirmation to an extension plan if the debtor has been "guilty" of any act that would bar a discharge in bankruptcy. The argument is that since receiving a prior discharge is neither unlawful nor morally reprehensible one cannot be "guilty" of it, and hence that the six-year "discharge" provision cannot be a bar to a Chapter XIII extension plan.

This argument presupposes that the word "guilty" was intentionally used in § 656 in a discriminating sense, that is, to distinguish among those acts catalogued in § 14 (c) which under § 656 would bar confirmation of an extension plan. The fact of the matter is, however, that when Congress in 1938 enacted Chapter XIII, 52 Stat. 930-938, it took as its model the form and language of the prior bankruptcy act, more specifically § 12d, 30 Stat. 550, dealing with compositions.¹ The "guilty" phrase was appropriate in that 1898 statute because at that time the only bars to a discharge in the predecessor of § 14 (c) were offenses punishable by imprisonment or fraudulent concealment. Section 14b, 30 Stat. 550. In 1903, Congress amended § 14b to include the six-year bar, 32 Stat. 797, and over the years other grounds for refusing confirmation have been added to that section. But the word "guilty" was never changed, and has obviously remained in several chapters of the

¹ "The judge shall confirm a composition if satisfied that (1) it is for the best interests of the creditors; (2) the bankrupt has not been guilty of any of the acts or failed to perform any of the duties which would be a bar to his discharge;" § 12d, 30 Stat. 550.

act merely as a shorthand way of referring back to those items that preclude the granting of a discharge. Thus, Chapter XI of the Bankruptcy Act, which deals with arrangements, has almost an exact duplicate of § 656 (a)(3) containing the same "guilty" phraseology. § 366 (3), 11 U. S. C. § 766 (3) (1964 ed.). Chapter XII, which deals with real property arrangements, contains a similar provision. § 472 (3), 11 U. S. C. § 872 (3) (1964 ed.). And of course Chapter XIII, dealing with *both* compositions and extensions for wage earners, uses this language. These parallel provisions all derive from the same section framed in 1898.

This history and this parallelism indubitably demonstrate two things: first, that the Congress did not devise the "guilty" terminology in 1938 as a means of making a subtle distinction between the morally reprehensible bars to bankruptcy contained in § 14 (c) and the other bars there enumerated; and second, that the word "guilty" means the same thing when applied to general arrangements in § 366, to real property arrangements in § 472, and to compositions and extensions in § 656. If the word "guilty" excludes the six-year bar for extension plans, it is impossible to see what sort of statutory interpretative sleight of hand would save it for general arrangements, real property arrangements, and wage-earner composition plans. Moreover, it seems already accepted that as applied to Chapter XI arrangements, the "guilty" provision does refer back to the six-year bar. See *In re Jensen*, 200 F. 2d 58; 9 Collier, Bankruptcy ¶ 9.19, at 310-311 (14th ed. 1964); Kennedy, Hospitality for Repeaters Under the Bankruptcy Act, 68 Commercial Law J. 117, 119-120 (1963). The same would appear to be true of the meaning of "guilty" in Chapter XII. See 9 Collier, *supra*, ¶ 9.07, at 1146. And the Court in its present opinion appears to concede that when applied to

compositions, § 656 is somehow transformed to include the six-year bar.

In short, construing "guilty" to refer only to "reprehensible" aspects of § 14 (c) has no basis in legislative history, and requires a strained attempt to distinguish other applications of the identical section and of parallel sections which concededly are applied more generally. Because of its ramifications, this construction may do serious harm to the administration of Chapter XIII compositions, Chapter XII real property arrangements, and Chapter XI arrangements.

The Court also advances another argument in support of its conclusion that confirmation of this extension plan was not barred by virtue of §§ 656 and 14 (c). This argument rests essentially on § 602 of the Bankruptcy Act, 11 U. S. C. § 1002 (1964 ed.). Section 602 provides that the provisions of Chapters I through VII shall apply to Chapter XIII "insofar as they are not inconsistent or in conflict with the provisions of this chapter" It seems to be said that the six-year bar is inconsistent with the provisions of Chapter XIII because the extension plan is designed to give wage earners relief, and the six-year bar would preclude some such people from receiving that relief without good reason.

This argument likewise does not withstand analysis. To be sure the six-year bar makes it impossible for certain wage earners to get relief by way of extension plans, but so do all the other restrictions on this form of relief. Nobody would suggest that it is "inconsistent" with Chapter XIII to withhold extension-plan relief from those who engage in fraud on the ground that such a restriction cuts down the number of people who can take advantage of Chapter XIII. Section 656 clearly does establish restrictions on the class of people to whom relief is available; the question before us is whether the six-year bar is such a limitation; citation of § 602 is con-

clusory only, and makes no positive contribution to a meaningful analysis.

My conclusion that the statute should be read literally to preclude the confirmation of an extension plan if the applicant has been granted a discharge within the previous six years is reinforced by § 686 (5) of Chapter XIII, 11 U. S. C. § 1086 (5) (1964 ed.). Section 686 (5) in its entirety declares that "confirmation of a plan under this chapter shall not be refused because of a discharge granted or a composition confirmed prior to the effective date of this amendatory Act." The inclusion of this provision indicates quite clearly that Congress did believe that a prior discharge would be a bar to a Chapter XIII plan, and that it decided to remove that restriction only for discharges granted *before* September 22, 1938, the effective date of the statute in question. See 10 Collier, *supra*, ¶ 33.05, at 477. Such a provision is perfectly understandable. Before the enactment of the extension plan amendment, wage earners who sought a bankruptcy remedy could obtain only a discharge through straight bankruptcy or composition. There would be no reason to preclude wage earners who availed themselves of such relief prior to September 1938 from obtaining a more favorable extension plan subsequently. On the other hand, after enactment of Chapter XIII, wage earners would have the opportunity to apply for an extension plan. It is not difficult to understand why Congress should have refused to permit wage earners who chose a discharge in bankruptcy rather than an extension plan a second opportunity, within six years, to receive statutory relief. I am frank to say that I am unable to perceive the basis for the Court's contrary explanation of this provision.

The short of the matter is that the Court's arguments do not support the conclusion it reaches. The conclusion is of course supportable as a legislative judgment, even though arguments can be made for both sides. Thus,

it might be argued for the six-year bar in a Chapter XIII context somewhat as follows: the wage-earner extension plan is a new and very advantageous procedure for the debtor, but it is a burden on the courts. It is also a constraint on creditors who will be delayed in collecting, will be precluded from garnishing, and may not receive full repayment if the debtor obtains a discharge under § 661 of the Act, 11 U. S. C. § 1061 (1964 ed.). It is therefore reasonable to limit the availability of this kind of relief to those wage earners who have not had the advantage of a discharge in bankruptcy in the previous six years. Furthermore, it is certainly arguable that the six-year bar encourages wage earners to make use of the Chapter XIII procedure. With the prior-discharge bar eliminated, a debtor might eschew an extension plan and decide instead to go through straight bankruptcy first, waiting a few months until the going once again "gets tough" to take advantage of the extension plan.

I venture considerations such as these not as overcoming the countervailing ones relied on by the Court, and heretofore espoused by others,² but simply to point up the fact that this is not one of those cases where seemingly straightforward statutory language must yield its literal meaning to a contrary congressional intent. What we have here are but two contrasting legislative policies, wherein the Court's duty is to take the statute as it is presently plainly written.

I would affirm the judgment of the Court of Appeals.

² See the proposed amendment of the Bankruptcy Act by the National Bankruptcy Conference, note 9, *ante*, p. 12; Kennedy, Hospitality for Repeaters Under the Bankruptcy Act, 68 Commercial Law J. 117 (1963).

