

CRS Report for Congress

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Consumer Bankruptcy and Household Debt

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Summary

The 107th Congress is considering legislation (H.R. 333, S. 220) that would require some consumer bankruptcy petitioners to repay certain debts rather than have them discharged, or erased, by the bankruptcy court. The principal impetus behind bankruptcy reform is the high number of consumer bankruptcy filings, which in recent years have been running at nearly four times the levels of the early 1980s. It is not clear why bankruptcy filings have increased so dramatically during a period that has included two of the longest economic expansions in U.S. history. Since bankruptcy is almost by definition a condition of excessive debt, many would expect to observe a corresponding increase in the debt burden of U.S. households over the same period. However, while household debt has indeed grown, debt costs as a percentage of income have been fairly constant over the past two decades. What these aggregate debt statistics do not show is that there has been an increase in the percentage of families in financial distress (those spending more than 40% of their incomes on debt service). Financial distress is most common among lower-income families, but its incidence has grown in all income brackets. This trend suggests that explanations for the rise in consumer bankruptcy filings are more likely to be found in micro-analysis of individuals and groups of debtors than in macroeconomic indicators. This report presents statistics on bankruptcy filings, household debt, and households in financial distress, and will be updated as new statistics become available. For discussion of bankruptcy reform proposals, see CRS Report RL30865, *Bankruptcy Reform Legislation in the 107th Congress*.

The tables below present data on bankruptcy filings, household debt, and families in financial distress. Table 1 shows bankruptcy filings since 1980. Both business and non-business bankruptcies showed increases in the early 1980s, but business filings peaked in 1987 and have since declined, while the number of consumer filings continued to grow through the 1990s. Consumer bankruptcies exhibit a pattern of rapid annual growth for several years, a 2- or 3-year pause, and a resumption of growth. The most recent pause began in 1999 and continued through the end of 2000: there were 13% fewer filings in 2000 than in 1998. In the first three quarters of 2001, however, consumer bankruptcies were up 21% over the previous year. If filings continue at that level throughout the year, the annual total for 2001 will exceed 1998's record number.

Table 1. Bankruptcy Filings in the United States, 1980-2001

Year	Total	Business	Nonbusiness or Consumer Filings		
	Number	Number	Number	% Change from Previous Year	Rate per 1,000 Population
1980	331,264	43,694	287,570	46.0	1.26
1981	363,943	48,125	315,818	9.8	1.37
1982	380,251	69,300	310,951	-1.5	1.34
1983	348,880	62,436	286,444	-7.9	1.22
1984	348,521	64,004	284,517	-0.7	1.20
1985	412,510	71,277	341,233	19.9	1.43
1986	530,438	81,235	449,203	31.6	1.87
1987	577,999	82,446	495,553	10.3	2.04
1988	613,465	63,853	549,612	10.9	2.24
1989	679,461	63,235	616,226	12.1	2.49
1990	782,960	64,853	718,107	16.5	2.87
1991	943,987	71,549	872,438	21.5	3.45
1992	971,517	70,643	900,874	3.3	3.53
1993	875,202	62,304	812,898	-9.8	3.15
1994	832,829	52,374	780,455	-4.0	2.99
1995	926,601	51,959	874,642	12.1	3.33
1996	1,178,555	53,549	1,125,006	28.6	4.24
1997	1,404,145	54,027	1,350,118	20.0	5.02
1998	1,442,549	44,367	1,398,182	3.6	5.17
1999	1,319,465	37,844	1,281,581	-8.3	4.68
2000	1,253,444	35,472	1,217,972	-5.0	4.54
2001*	1,106,418	29,872	1,096,881	14.1	5.12

* 2001 filing numbers are for Jan.- Sept.; percentage change and rate per 1,000 population figures are based on the twelve months ending September 2001.

Source: Administrative Office of the U.S. Courts.

Table 2. Household Debt Levels and Debt Burden, 1990 – 2001

(At end of year, except as noted for 2001)

Year	Consumer Credit (\$ billions)			Home Mortgage Debt (\$ billions)		Debt Burden (% of Income Used for Debt Payments)		
	Revolving	Non- revolving	Total	Home Equity Loans	Total	Consumer Debt	Mortgage Debt	Total
1990	250.9	554.2	805.1	235.9	2,532.3	7.10	6.31	13.41
1991	277.1	517.4	794.5	256.4	2,708.7	6.51	6.26	12.77
1992	292.2	508.3	800.6	255.6	2,865.1	5.97	5.88	11.85
1993	325.0	534.0	859.0	248.2	3,001.4	6.09	5.67	11.76
1994	383.2	600.7	983.9	264.4	3,178.2	6.48	5.69	12.17
1995	464.1	658.7	1,122.8	289.3	3,367.6	7.04	5.85	12.89
1996	494.4	683.1	1,182.6	338.1	3,577.7	7.43	5.83	13.26
1997	531.2	703.3	1,234.5	416.2	3,818.1	7.44	5.90	13.35
1998	560.5	740.5	1,301.0	476.7	4,169.5	7.51	5.89	13.40
1999	595.6	798.0	1,393.7	532.8	4,558.9	7.56	6.09	13.65
2000	663.8	869.3	1,533.2	630.5	4,941.5	7.82	6.44	14.26
2001	683.8	961.3	1,645.1	689.7	5,305.9	7.69	6.12	13.81

Note: 2001 figures for consumer credit are end of year; mortgage debt and debt burden figures are end of 3rd quarter.

Source: Federal Reserve. Release G. 19 (consumer credit) and Flow of Funds Accounts, Table L. 218 (household mortgage debt).

Table 2 shows figures on household debt. The major categories of household debt are mortgage debt and consumer credit, which together comprise about 97% of all household indebtedness. Consumer credit consists of revolving credit, or credit card debt, and non-revolving debt, which is dominated by auto loans (though it includes loans for boats, mobile homes, vacations, and so on). Mortgage debt is borrowing secured by real estate. A rapidly growing category within mortgage debt, home equity loans, is broken out in the table because it may substitute for consumer debt in many cases.

Table 2 also includes estimates of the burden of debt service, that is, the percentage of household disposable income that goes to repay loans. It is noteworthy that consumer credit is more expensive in terms of debt costs than is mortgage debt, even though the principal outstanding on mortgage debt is three times as great. This reflects the higher interest rates charged and the shorter maturities in consumer lending, as well as the fact that mortgage and home equity debt receives favorable tax treatment.

The total debt burden figures in table 2 fluctuate within a fairly narrow range: from 11.8% to 14.3%. (During the 1980s, the range was similar: from 12.3% to 14.2 %.) These figures do not suggest any dramatic trend towards higher indebtedness on household balance sheets. In the aggregate, Americans have taken on more debt, but their incomes have kept pace. The relative stability of the debt burden would not lead one to expect the explosion in consumer bankruptcy filings that has in fact occurred.

It is likely that the aggregate numbers mask important differences among families: some have done very well in the long booms of the 1980s and 1990s, while others have taken on debt that they have difficulty repaying. Table 3 below, based on the Federal Reserve's Survey of Consumer Finances, shows the percentage of families at various income levels who devote more than 40% of their incomes to debt service, for selected years from 1989 through 1998 (more recent data is not yet available).

Table 3. Families in Financial Distress* by Income Level, 1989-1998
(Percent)

Income (In 1998 dollars)	1989	1992	1995	1998
All Families	10.1	10.9	10.5	12.7
Less than \$10,000	28.6	28.4	27.6	32.0
\$10,000 – \$24,999	15.0	15.5	17.3	19.9
\$25,000 – \$49,999	9.1	9.6	8.0	13.8
\$50,000 – \$99,999	4.9	4.4	4.2	5.7
Over \$100,000	1.8	2.2	1.7	2.1

* "Financial distress" means that debt service payments consume over 40% of the family's income.

Source: Federal Reserve. Survey of Consumer Finances. In: *Federal Reserve Bulletin*, January 2000.

Two striking facts emerge from the data in Table 3. First, financial distress has become more common over the last decade despite unusually favorable conditions in the general economy. The incidence of distress was higher in 1998 than in 1989 for families of all income levels. It may be that economic good times lead consumers to take on more debt, in confidence that they will be able to repay. Second is the extremely high rate of distress among lower-income families, who are the most likely to file for bankruptcy.¹

The question remains why so many families at or below the national median income take on high levels of debt and end up in bankruptcy court. Some explanations focus on particularly vulnerable populations: the sick and uninsured, the divorced, or residents of states without mandatory uninsured motorist coverage or with “pro-debtor” legal cultures. Supporters of bankruptcy reform maintain that the current bankruptcy code is too debtor-friendly and creates an incentive to borrow beyond the ability to repay, or in some cases without the intention of repaying. Opponents of reform claim that financial distress is often a by-product of the high-pressure marketing campaigns of credit card issuers and other consumer lenders. Lack of a consensus explanation for the rise in consumer bankruptcy filings ensures that reform efforts will be controversial.

¹ Several studies in the mid-to-late 1990s reported that the median income of bankruptcy petitioners was about \$22,000. See: U.S. General Accounting Office. *Personal Bankruptcy: Analysis of Four Studies on Chapter 7 Debtors' Ability to Pay*. GAO/GGD-99-103. June 1999. p. 23.