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Jean Braucher's article usefully describes the many complexities of the pending consumer bankruptcy legislation,[1] and performs a valuable service by tracing out its implications for the consumer bankruptcy system.[2] I agree that the legislation has problems[3] and is far from ideal, but I like some aspects of it, and was unsure of the basis of Professor Braucher's critique. In particular, I did not understand her praise for the current system,[4] or the source of her conviction that the pending bankruptcy legislation could only make things worse.[5]

Our disagreement might stem from the unfortunate use of highly moralistic terms in the current policy debate, terms that Professor Braucher accepts uncritically. Academics and politicians alike provoke emotional responses by depicting the participants in

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1. *See* Bankruptcy Reform Act of 2001, S. 220, 107th Cong. (2001); H.R. 333, 107th Cong. (2001) [hereinafter Bankruptcy Reform Act of 2001].

2. *See generally* Jean Braucher, *Means Testing Consumer Bankruptcy: The Problem of Means*, 7 FORDHAM J. CORP. & FIN. L. 407 (2002).

3. *Id.* at 408 (stating that the Bankruptcy Reform act "would make access to bankruptcy more difficult, imposing new hurdles and costs for all and thus pricing the worst off out of the system"); *see also id.* at 433-43 (outlining the new provisions in the pending bankruptcy legislation and noting problems with the propositions, such as increased cost (including attorney fees), increased filing requirements, and increased duties for U.S. Trustees,); *id.* at 445 ("The bankruptcy bureaucracy would swell.").

4. *Id.* at 407 (stating that "the current system already effectively screens out most of those who do not belong in it"); *see also id.* at 408 ("Chapter 7 works reasonably well to give distressed debtors a fresh start."). *But see id.* at 412 ("Certainly, improvements in consumer bankruptcy law could be made."); *see also id.* at 447-54 (discussing other options to the pending bankruptcy legislation).

5. *See supra* note 3 and accompanying text.

the credit market and the bankruptcy system as composites of offensive (or attractive) characteristics. These composites serve the same purpose as roles in medieval morality plays: they embody vices we loathe or virtues that we respect. The common story is this:

Debtor

Moral Intuition	*Characters*
People should be responsible and pay their debts.	The spendthrift The rich person who parks assets in a Florida homestead
We should forgive people who suffer through of their own.	The divorced woman with no skills The parents of a sick child

Creditor

Moral Intuition	*Characters*
People should not make money off the misery of others.	Deceptive credit card companies

There is no morally positive story for the creditor, even though we would all be lost if credit were not available; the reason is just that creditors make money and do not try to hide that fact. The rhetorical battle thus focuses on the characterization of the debtor as parasite or victim.

This debate quickly becomes one about whether debtors file for bankruptcy in order to abuse the system (as parasites) or to escape hardships (as victims). The bankruptcy filing rate is taken as a sign of moral and social decay (if debtors are parasites) or of a well-functioning safety net (if debtors are victims). The debt level is also taken as a sign of aggregate irresponsibility (if debtors are parasites) or the evil practices of lenders (if debtors are victims). A sterile empirical debate ensues about whether the debt level and

bankruptcy rate are too "high," and whether trends are due to moral decay, bad behavior by creditors, or (as is most likely, and as Professor Braucher acknowledges) shifts in the technologies of credit and the legal regulation of the credit market.[6]

Much progress would be made in bankruptcy reform if this moral posturing were abandoned, and policymakers focused on the relevant consideration, namely, how much debtors should be forced to pay in the form of higher interest rates, or in the withdrawal of credit, for the right to escape repayment of their loans. The cost of any bankruptcy system takes the form of higher interest rates for all debtors. The benefit is the ex post prevention of hardship. I say "ex post" because by raising the cost of credit, bankruptcy also creates "ex ante" hardship for people who as a consequence cannot borrow money. It is not at all clear that the current balancing of these benefits and costs is correct, and I do not understand why Professor Braucher believes otherwise.

The pending legislation implicitly assumes a status quo in which people pay more for the bankruptcy safety net than they would want to, and addresses this problem by making bankruptcy less attractive. It makes bankruptcy less attractive in two ways: (1) by creating paperwork requirements,[7] exposing sloppy lawyers to sanctions,[8] and so forth; and (2) by creating a means test.[9] The first appears to be directed toward lower income debtors; the second toward higher income debtors. Professor Braucher focuses entirely on the ex post costs of these requirements,[10] and she is right to stress them, but that, of course, is their whole point. If the purpose

6. Braucher, *supra* note 3, at 422 (stating that it is plausible that interest rate deregulation prompted more lending, and more lending meant more over-burdened debtors finding their way to bankruptcy).

7. *See* Bankruptcy Reform Act of 2001, *supra* note 1, § 102 (requiring a debtor to submit a means test calculation); *see also id.* § 315(b) (discussing debtors filing requirements); *id.* § 315(e)(2) (requiring debtor to submit tax returns when filing for bankruptcy).

8. *Id.* § 102 (including sanctions such as payment for the costs of a dismissal action, attorneys' fees, and a civil penalty).

9. *Id.*

10. Braucher, *supra* note 2, at 412 (asserting that reducing access to bankruptcy would likely lead to the expansion of the high-risk, high-cost credit market, which would also increase the social problem of over-indebtedness).

of the law is to make bankruptcy more difficult, it does not make sense to criticize it for making bankruptcy more difficult.

To assess the pending legislation, we need to address two questions: (a) is the current bankruptcy system too generous, and (b) if so, are there better ways of making it less attractive.

Professor Braucher focuses on (a), claiming without any explanation that there is too much debt already, and so society would be better off with less.[11] If that is true, however, there are more direct ways of reducing the debt load: taxing the extension of credit would be sensible and equitable as well. What is true is that it is hard to know what the proper balance is. I would be more persuaded of the need for bankruptcy reform legislation if interest rates on credit cards had zoomed above their historic averages, or if credit card companies started withdrawing credit. But in any event this is a complex question about which I have nothing to say.

As for (b), this is a more interesting question for bankruptcy policy. Suppose we want to reduce the amount of nonpayment of debt.[12] Limiting exemptions turns out to be politically difficult, and in addition, there are some good reasons for deferring to the states. Limiting the discharge means requiring debtors to pay creditors out of a portion of their future income. The means-testing provision has just this effect: by restricting access to Chapter 7 it encourages debtors to file a plan under Chapter 13, a plan that distributes future disposable income to creditors.

The benefit of this system is that it makes human capital accessible to creditors. Creditors will lend more, and at a lower interest rate, if they can obtain some portion of the future income of defaulting debtors.[13] Debtors will not suffer too much hardship ex post as long as they retain enough future income to live on. By

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11. Braucher, *supra* note 2, at 424-29 (discussing the causes of over-indebtedness and how reducing access to bankruptcy will only increase debt levels).

12. This does not necessarily mean that we want to reduce the bankruptcy filing rate! That is not the economically relevant variable.

13. Barry Adler et al., *Regulating Consumer Bankruptcy: A Theoretical Inquiry*, 29 J. LEGAL STUD. 585, 591 (2000) ("When an insolvent borrower can trade future income for current assets, the creditor's expected insolvency state payoff increases, and this in a competitive credit market will reduce the interest rate.").

treating non-human and human capital more equally, the reformed bankruptcy system would discourage inefficient substitutions: the person who sells non-exempt revenue-generating assets in order to finance an education that will produce discharge-protected income.

This is not to say that the new system is ideal. By taxing all non-disposable income, Chapter 13 reduces the incentive of debtors to work during the pendency of the plan.[14] Many people have criticized Chapter 13 for this effect,[15] and it probably ought to be changed. But by bringing human capital into the bankruptcy system, the pending legislation moves in the right direction.

Another problem with limiting discharge is that for lower income individuals the amounts at stake are too small to be worth the cost of monitoring the Chapter 13 plan. This, I take it, is the reason for limiting the "abuse" test to higher income debtors, and using paperwork and other costly requirements in order to deter lower income debtors. The effect of these requirements is predictable: people whose earning power is low enough will not file for bankruptcy, nor will people whose debt burden is relatively low. These people are filtered out, leaving debtors whose debt burdens are more serious and pressing. Unfortunately, for the filtering to work, these hard-pressed debtors need to bear the increased filing costs.

After some experimenting with the system, we might conclude that the increased hardship is not worth the benefit – the predicted reduction in the cost of credit for poorer people. That might be the case, but it is an empirical question, not one that can be answered

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14. *Accord* Harry L. Deffebach, *Postconfirmation Modification of Chapter 13 Plans: A Sheep in Wolf's Clothing*, 9 BANKR. DEV. J. 153, 169 (1992) ("The Fourth Circuit recognized that some individuals might be discouraged from working harder if the court distributed the extra wages to their creditors.").

15. *See, e.g.*, Local Loan Co. v. Hunt, 292 U.S. 234, 245 (1934) (written by Judge Sutherland); Thomas H. Jackson, *The Fresh-State Policy in Bankruptcy Law*, 98 HARV. L. REV. 1393, 1434 (1985).

> Thus, to say that human capital is in existence at the time of bankruptcy does not mean that creditors are entitled to claim any of the debtor's measurable future income as an existing asset, for some of that income will depend on future efforts by the debtor – efforts over which the creditors will have no control and that society will never require.

Id. *But see* Deffebach, *supra* note 14, at 168-69 (stating that it is unfair to allow a debtor to improve his financial outlook without compensating past creditors).

in the abstract, and not one that benefits from moralistic posturing.