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# Do Debtors Have an Obvious Financial Rationale for Filing a Chapter 13 Bankruptcy Petition?

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### Abstract

The decision to file for bankruptcy, and more specifically to file for Chapter 13 bankruptcy protection, is a major financial decision that impacts the debtor's financial well-being for several years. Under financial economic theory, debtors should make informed choices, which include having clear rationale for making specific chapter filing choices. Based on those choices, expected outcomes accrue to the debtor. Moreover, rationales for the debtor's decisions should be revealed as debtors disclose their assets, liabilities, income and other salient characteristics in the filing process. The common rationales, as characterized by the outcomes accruing from making a choice to file under Chapter 13, are explored in this manuscript. Using a sample of nearly 300 Chapter 13 bankruptcy filings in the Eastern Washington Bankruptcy Court District, approximately 32 percent of all filers accrue no obvious financial benefit from filing under Chapter 13, and would be been better off financially by filing under Chapter 7. These filings are typically attributed to local norms and business practices that occur within a community, also known as "legal culture". This analysis suggests that legal culture plays a very significant role in Chapter 13 bankruptcy chapter filing choices.

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The decision to file for bankruptcy, and more specifically to file for Chapter 13 bankruptcy protection, is a major financial decision that impacts the debtor's financial well-being for several years. Under financial economic theory, debtors should make informed choices, which include having clear rationale for making specific chapter filing choices. Based on those choices, expected outcomes accrue to the debtor. Moreover, rationales for the debtor's decisions should be revealed as debtors disclose their assets, liabilities, income and other salient characteristics in the filing process. The common rationales, as characterized by the outcomes accruing from making a choice to file under Chapter 13, are explored in this manuscript. Using a sample of nearly 300 Chapter 13 bankruptcy filings in the Eastern Washington Bankruptcy Court District, approximately 32 percent of all filers accrue no obvious financial benefit from filing under Chapter 13, and would be better off financially by filing under Chapter 7. These filings are typically attributed to local norms and business practices that occur within a community, also known as "legal culture". This analysis suggests that legal culture plays a very significant role in Chapter 13 bankruptcy chapter filing choices.

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## 1. Introduction

When faced with decisions that have significant consequences, individuals typically use all available information to make choices. If a paucity of information exists, decision makers will acquire information to identify possible courses of action and their expected consequences. In doing so, individuals make decisions that more closely satisfy their objectives and reduce the adverse (expected) outcomes associated with those decisions (Hanna and Wozniak 2001; pp. 291-304). One such decision concerns households who become financially unstable and file for bankruptcy protection. Upon making the choice to file for bankruptcy (which generally, but not always, coincides with financial exigency), the debtor must choose a chapter of the U.S. Bankruptcy Code under which to file. In the vast majority of cases, debtors (with the help of an agent, or attorney) file under either Chapter 7 or Chapter 13 of the Code (Sullivan, Warren and Westbrook 1997, 2003; Zhu 2011). Under Chapter 7, assets (beyond those qualifying for exemptions) are liquidated and used to repay outstanding financial obligations. The liquidation of assets rarely occurs (less than 1% of Chapter 7 cases) because of generous state or federal exemption statutes available to the debtor to shield their property (Gropp, Scholz and White 1997). Most remaining debts are typically discharged. The bankruptcy code provides a list of non-dischargeable debts (11 U.S.C. §523), but these types of debts will not affect the majority of consumer debtors. Under Chapter 13, most assets are retained, and a repayment plan is established lasting from 36 to 60 months whereby the filer repays some portion of the financial obligations (Nelson 1999; 11 U.S.C. §362). In doing so, the debtor may retain possession of key assets such as a home or an automobile (Li, 2001).

Following Norberg (2006), Norberg and Velkey (2006) and Norberg and Compo (2007), this analysis focuses on decision makers who file for bankruptcy under Chapter 13. The decision to file for bankruptcy, and more specifically to file for Chapter 13 bankruptcy protection, is a major financial decision that impacts the debtor's financial well-being for several years (Nelson 1999). For example, the bankruptcy effect on credit rating scores will adversely affect the debtor's access to future credit, including home purchases (Gropp, Scholz and White 1997). Under financial economic theory, debtors should make informed choices, (including the selection of bankruptcy chapter), with the expected outcomes accruing to the debtor based on those choices (Li 2001; Athreya 2005). Moreover, rationales are revealed as debtors disclose their assets, liabilities, income and other salient characteristics in the filing process (Domowitz and Sartain 1999). This raises an interesting question: what are the common rationales, as characterized by the outcomes accruing from making a given choice, for filing under Chapter 13?

The remainder of the manuscript proceeds as follows. In the next section the legal framework for filing Chapter 13 bankruptcy, as well as the benefits of this chapter choice, are described. The third and fourth sections describe the empirical methodology and data collection process, respectively. A discussion of the empirical results follows. The manuscript concludes with a discussion of the implications of our findings, and some suggestions for future research in this area of study.

## 2. Legal Framework

Broadly speaking, individuals who file for bankruptcy under Chapter 13 generally do so for one of three reasons (Clements *et al.* 1999; Domowitz and Sartain 1999). The first reason is because the filer is prohibited from filing under a different chapter (usually Chapter 7) of the

U.S. Bankruptcy Code. This applies to individuals who have previously filed for bankruptcy within 8 years of the current bankruptcy petition (11 U.S.C. §727 (8); Administrative Office of the Courts 2011). The ineligibility criteria may also apply to filers who have relatively high household incomes. To ensure that filers with an ability to repay some or all outstanding debts actually fulfill their obligations, Congress passed (and the President signed into law) the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) of 2005, which took effect on October 17, 2005. A major component of BAPCPA was the establishment of a “means test” (Norberg 1999; Norberg and Compo 2007; Lefgren and McIntyre 2010; McIntyre, Sullivan and Summers 2010). Under this test, a filer whose household income (net of court approved expenses) was above the state median would be deemed “able to repay” some of their debts, and in some cases, excluded from filing under Chapter 7. Filers whose net household income falls below this threshold “pass” the means test and can file under either Chapter 7 or Chapter 13 (Wedoff 2005).

The second reason an individual files for Chapter 13 bankruptcy petition is to resolve a specific financial obligation that would not otherwise be resolved through a Chapter 7 filing or (in the absence of a bankruptcy filing) through traditional negotiation with creditors (Clements *et al.* 1999). Under 11 U.S.C. §362, a Chapter 13 bankruptcy filing automatically stays all collection efforts while the Bankruptcy Court prioritizes debts and establishes a repayment plan. This includes outstanding tax claims, unpaid traffic fines and domestic support obligations, in addition to other “priority unsecured”, but potentially non-dischargeable financial obligations (Loibl, Hira and Rupured 2006; Power 2007; Hackney, McPherson and Friesner 2010; Reilly 2012). As an example, if an individual owes taxes to the U.S. federal government, filing for bankruptcy under Chapter 13 would prevent the U.S. Internal Revenue Service (IRS) from seizing assets and/or garnishing wages to recoup outstanding taxes until such time as the bankruptcy process is resolved (Hackney *et al.* 2014). It also prevents family courts from levying additional wage garnishments for unpaid child support and/or alimony until the bankruptcy process is complete (Hackney, McPherson and Friesner 2010). Additionally, Chapter 13 provides a strategy for paying delinquent traffic fines, allowing the debtor to retain his/her driver’s license while paying fines in a 3-5 year plan (11 U.S.C. §362). For secured claims, the reorganization of debts and the establishment of a repayment plan allow Chapter 13 filers to retain ownership of their collateral or assets as long as they meet the requirements of the repayment plan (Administrative Office of the Courts 2011). Moreover, with some secured claims, the amount remunerated through the repayment plan may be less than the original value of the claim. This is common in filings where the debtor has an automobile loan, and the current value of the car is less than the loan balance. In such cases, any outstanding debt in excess of the amount allocated for repayment by the plan (which is tied to the current value of the asset) is discharged. In legal circles, this is known as “cramming down” a loan. The changes in BAPCPA, effective late 2005, made the “cram down” much less attractive to debtors, (11 U.S.C. §1325 (5) )<sup>1</sup>.

The third reason an individual files for Chapter 13 bankruptcy protection is to adhere to a moral or other social obligation to repay one’s debts. Often described in the literature as “legal culture”, these obligations may be based on religious beliefs, the formation of social stigmas (particularly with regard to money management) or the professional practices and/or advice of local bankruptcy attorneys (Sullivan, Warren and Westbrook 1988, 1997; Neustadter 1986;

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<sup>1</sup> Changes from BAPCPA largely eliminated the other few advantages of Chapter 13, leaving the remaining categories as are set out in the tables 11 U.S.C. §1322.

Braucher 1993; Clements *et al.* 1999; Athreya 2005; Lefgren and McIntyre 2010; Lefgren, McIntyre and Miller 2010; McIntyre, Sullivan and Summers 2010). One commonality across all types of “legal culture” is the fact that they are reflected in the community as a whole. That is, the existence of a specific legal culture leads to a consistent pattern of behaviors within the community; multiple individuals file for Chapter 13 bankruptcy protection based on similar socio-cultural rationale.

### 3. Empirical Methodology

Following the bankruptcy literature, the methodology employed in this paper uses both case study and hedonic methods (Clements *et al.* 1999; Himmelstein *et al.* 2009; Himmelstein, Thorne and Woolhandler 2011). More specifically, simple random sampling techniques are used to identify a statistically appropriate number of Chapter 13 bankruptcy filings. For each filing, the research team identified whether an individual met any of the following criteria, which reflect the possible rationales for a Chapter 13 filing: ineligibility to file under Chapter 7 of the U.S. Bankruptcy Code, outstanding traffic (and related) fines, outstanding tax obligations, outstanding domestic support obligations, arrear mortgage obligations, or negative automobile equity. If an individual Chapter 13 filing does not contain evidence of any of these criteria, the rationale for the filing falls under the default auspices of “legal culture”. Because legal culture is, by definition, a community-based concept, it can be characterized by examining trends in bankruptcy filings across various communities that exist within the population (Pollack 1997; Sullivan, Warren and Westbrook 1997). However, it is important to note that the definition of “community” may be based on any number of socio-cultural factors, including (but not limited to) area of residence, gender, religion and cultural/ethnic heritage. As an initial (albeit imperfect) measure of legal culture, this analysis employs the county (or a related group of counties) as the definition of “community”. More specifically, the Eastern District of Washington, the source of the data used in this study, covers 20 counties; Adams, Asotin, Benton, Chelan, Columbia, Douglas, Ferry, Franklin, Garfield, Grant, Kittitas, Klickitat, Lincoln, Okanogan, Pen Oreille, Spokane, Stevens, Walla Walla, Whitman, and Yakima. The filer’s home county was identified, and subsequently aggregated into one of four mutually exclusive and collectively exhaustive groups: Spokane County (the most populous county in the District), Benton and Franklin Counties (an upper-middle class community, and home to the Hanford Military Site and Pacific Northwest National Laboratories), Yakima County (a largely agricultural county with a very large Hispanic population accounting for 64.34% of the total county population), and all other counties comprised of the remaining 16 counties (mostly geographically large, rural counties that share similar cultures and demographics).<sup>2</sup> We leave an exploration of more specific community designations as they relate to the formation of legal culture as a suggestion for future research.

A sequential, exploratory method of data analysis is used to identify the benefits of filing for Chapter 13 bankruptcy, and by extension the underlying rationale for filing under this chapter

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<sup>2</sup> If the researchers are confident that they have defined their communities appropriately within the context of legal culture, it is possible to employ stratified random sampling (or other, related experimental designs) to ensure that each community is weighted appropriately in the random sampling process (Anderson, Sweeney and Williams 2002; p. 277). Because the use of the county (or groups of counties) may not be an accurate or precise definition of the communities that exist in the population, we employ a general (non-weighted) sampling design, and test for community specific differences under the null hypotheses of no difference. This is consistent with employing a very conservative sampling approach under the assumption of ignorance about the formation of legal culture in the population.

of the U.S. Bankruptcy Code. Each of these factors is examined individually under a null hypothesis of ignorance (or homogeneity) about whether or not that factor is a contributor to the filing. That is, under the null hypotheses, a randomly selected Chapter 13 bankruptcy filer is equally likely to have an outstanding obligation which is to be resolved in the filing, or to not have this type of outstanding obligation. With regard to the county of filing, an assumption of ignorance or homogeneity indicates that the likelihood that a filer lives in a particular county is equivalent to the county's population as a proportion of the District's population. So, for example, if a given county represented 25 percent of the District's population, the null hypothesis also says that there is a 25 percent chance that a randomly selected Chapter 13 filer lives in that county.

The second step in the methodology is to disaggregate each of the previously defined benefits by county. If filers in a particular county or group of counties are disproportionately likely to file for Chapter 13 bankruptcy and obtain a specific benefit from submitting a Chapter 13 filing, then there is likely some underlying social or economic force in that community that is responsible for generating these incentives. In other words, a specific legal culture exists in those communities. As in the first step, no prior knowledge exists to suggest that a specific community (or geographic region) has a particular type of legal culture, or that the county is the appropriate way to define legal culture. Hence, the analysis operates under the null hypothesis of no relationship (i.e. homogeneity) between the community in which a filer lives and the receipt of a particular benefit of filing under Chapter 13.

Lastly, individuals who file under Chapter 13 may accrue none, one, or more than one of the benefits described previously. Hence, for each filer, the number of benefits (as defined previously) that accrue when filing under Chapter 13 are identified and cross-tabulated against the filer's county of residence. This provides a simple test of both the rationale for Chapter 13 filings (as measured by the benefits accrued by filing) and local legal culture. As before, the analysis operates under a null hypothesis of no relationship between the number of benefits accruing under Chapter 13 and filer residence.

Because each of the null hypotheses identified above assumes ignorance (or homogeneity), and are empirically quantified using counts and cross-tabulations, a chi-square test of homogeneity (also known as a chi-square test of independence) is used to test each null hypothesis (Anderson, Sweeney and Williams 2002). Note that, since multiple benefits of filing under Chapter 13 exist, the null hypotheses in steps one and two must be tested several times, once for each of the variables identified in that step (i.e., once for each benefit of filing under Chapter 13). Step 3 requires two chi-square tests, since we test both the number of benefits received, as well as the count of benefits received from filing under Chapter 13, disaggregated by county. In each case, a 5 percent significance level is employed. All tests were conducted using Microsoft Excel (Microsoft Corporation, Renton, WA) and IBM SPSS Statistics Version 21 (IBM Corporation, Armonk, NY).

The decision to file for Chapter 13 bankruptcy is based on causal factors and expected outcomes that are both generalizable and non-generalizable to the U.S. population as a whole (Clements *et al.* 1999; Li 2001). The application of the means test, the prioritization of debts, and the imposition of factors beyond the means test, such as recent prior bankruptcy filings, that requires or encourages a Chapter 13 filing are common across all U.S. Bankruptcy Court districts. Hence, some studies have examined bankruptcy decisions using national data (Sullivan, Warren and Westbrook 1997; Norbery and Velkey 2006; Norberg and Compo 2007). Concomitantly, median state incomes, local legal cultures (which likely exist at county or

regional levels), and the distributions of outstanding debts are all likely to vary substantially both across and within U.S. Bankruptcy Court districts. Hence, defining the population at the national level may lead to aggregation bias, and a failure to adequately capture the effects of local legal culture (Braucher 1993; Bermant, Flynn and Bakewell 2002; Lefgren, McIntyre and Miller 2010; Hackney *et al.* 2014). Analysis at a more local level (usually within a single U.S. Bankruptcy Court district) may be generalizable to some larger geographic designations, but not others. This analysis adopts the conservative approach of defining a single U.S. Bankruptcy Court District (in this case, the Eastern Washington District) as the population of interest. This choice is conservative because a sufficiently small population of interest allows for a meaningful analysis of local legal culture without explicitly expecting that such cultures exist. As discussed in footnote 2, an analysis at a local level also alleviates the need to employ a complicated (possibly stratified) sampling design, which would be required in instances where the population encompasses multiple U.S. Bankruptcy Court districts. Eastern Washington, being a rural, agriculturally dependent region, may be generalizable to other districts which share similar demographics. Should the population of interest be national in scope, then the results of this analysis can be considered as a case study (or alternatively, as a pilot study), and used as a framework upon which to conduct a national analysis.

#### **4. Data**

To test the study's null hypotheses, interval random sampling techniques were used to identify a random sample of 300 Chapter 13 bankruptcy cases filed during 2005 and 2007 in the Eastern Washington Bankruptcy Court District (via the Public Access Electronic Court Records, or PACER, System). This time frame was chosen because it immediately precedes, and immediately follows, the implementation of BAPCPA. As stated earlier, one major goal of BAPCPA is to reduce Chapter 7 filings (where many outstanding debts are discharged) and move those individuals into Chapter 13 filings (where relatively more debts are repaid) (Wedoff 2005). The BAPCPA means test clearly represents a constraint on individual behavior. Since bankruptcy is a financial decision, how individuals respond to this constraint (if at all) is likely driven by the financial benefits of filing under Chapter 13 (relative to Chapter 7) and possibly by local legal culture (which may encourage a specific chapter filing). Hence, the implementation of BAPCPA essentially forces an individual to be more strategic (both in terms of capturing specific benefits as well as the timing of the bankruptcy filing) and more transparent about the underlying rationale for filing for Chapter 13 bankruptcy protection.

According to the Districts Reports

([http://www.waeb.uscourts.gov/sites/default/files/waeb/filing\\_statistics/10%20Year%20Review.pdf](http://www.waeb.uscourts.gov/sites/default/files/waeb/filing_statistics/10%20Year%20Review.pdf)), there were 2815 Chapter 13 filings in 2005 and 2007. The random sample of 300 Chapter 13 filings represents approximately 10.7 percent of the population during this time frame. According to Dillman (2000; p. 207), this sample size should (at least approximately) be sufficient to draw meaningful statistical inferences from the data. All filings are signed "under penalty of perjury", and therefore should provide accurate and precise information at the time of the filing. Of the 300 filings, 272 (or 9.6 percent of the population) contained a complete set of information relevant to the study. We used these records to identify the primary benefits from filing under Chapter 13, as discussed in the Empirical Methodology.

#### **5. Results**



Table 1 contains a series of panels that investigate the first set of hypotheses. Panel A examines whether the distribution of Chapter 13 filings in the District is consistent with the underlying population distribution as reported by the Washington State Office of Financial Management (<http://www.ofm.wa.gov/pop/april1/hseries/default.asp>). The chi-square test statistic is significant, indicating that the two distributions are different. More specifically, residents of Yakima represent 33.1 percent of total Chapter 13 filings, but only 16.6 percent of the population. Concomitantly, residents of all other rural counties represent 35.7 percent of the population, but only 20.2 percent of Chapter 13 filings. The percentage of filings in Spokane and Benton/Franklin counties are consistent with their share of the District's population.

Panels B through G describe the distribution of filers with specific types of debts that are more favorably resolved in a Chapter 13 filing. In each case, the chi-square tests indicate that the null hypothesis of homogeneity (that a filer is equally likely to have or not have this type of financial obligation) is rejected at a 5 percent significance level. Of the 272 debtors in the sample, 89 (33 percent) were filing under Chapter 13 because they were ineligible to file under Chapter 7, 53 (19 percent) have outstanding traffic (or other) fines, 85 debtors (31 percent) have outstanding tax claims, 25 filers (9 percent) have arrearaged domestic support obligations, 63 filers (23 percent) have arrearaged mortgage payments, and 32 (12 percent) have negative equity in their automobiles.<sup>3</sup>

Table 2 disaggregates each of these types of outstanding obligations by location of residence. At the 5 percent significance level, there is no statistical relationship between residence and whether a filer is eligible or ineligible to file under Chapter 7 (Panel A; prob. = 0.098). As noted in Panel B, there is a significant relationship between location of residence and whether or not a filer has outstanding traffic (and other, related) fines to be resolved in the Chapter 13 filing. Filers in Yakima County are much more likely (26 out of 90 filings, or 29 percent) to have such fines, compared to Benton and Franklin Counties (9 out of 39 filings, or 23 percent), Spokane County (14 out of 88 filings, or 16 percent), and all other counties (4 out of 55 filings, or 7 percent). Panel C examines the relationship between county of residence and the existence of outstanding tax obligations, which is also significant at the 5 percent level (prob. = 0.001). Individuals from Spokane County (41 out of 88 filings, or 47 percent) are more likely to incur such obligations compared to those from Benton and Franklin Counties (8 out of 39 filings, or 21 percent), Yakima County (19 out of 90 filings, or 21 percent), and all other counties (17 out of 55 filings, or 31 percent). The results in Panel D examine county-level differences across filings with arrearaged domestic support obligations. No significant county-level differences exist in the data (prob. = 0.388). Panel E disaggregates arrearaged mortgage obligations by county. Significant differences exist (prob. = 0.047), with Spokane County filers (29 out of 88 filings, or 33 percent) being more likely to incur such obligations compared to those from Benton and Franklin Counties (9 out of 39 filings, or 23 percent), Yakima County (17 out of 90 filings, or 19 percent), and all other counties (8 out of 55 filings, or 15 percent). Lastly, as indicated in Panel F, no significant relationship exists between the filer's county of residence and the existence of negative automobile equity (prob. = 0.776).

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<sup>3</sup> As an aside, chi-square tests were also conducted to determine whether significant differences existed in each of the Chapter 13 filing characteristics and county of residence over time (between 2005 and 2007). In all instances but one, the tests indicate that no significant differences exist across the two years of the panel. The exception is for Chapter 13 filers who experienced negative equity in an automobile (prob. = 0.022), where 26 of the 32 filers with negative automobile equity filed in 2005. Changes to BAPCPA, 11 U.S.C. §135(5), made the "cram down" much less attractive, affecting the 2007 filings.

Table 3 examines the cumulative number of different rationale for filing under Chapter 13 of the U.S. Bankruptcy Code. Panel A describes the distribution of rationale, which is significantly distinct from an even distribution (prob. < 0.001). Cumulatively, 1 individual (0.3 percent) met six of these criteria, 0 filers (0 percent) met five of the six criteria, 6 filers (2 percent) met four of the criteria, 26 (10 percent) fell into three categories, 62 (23 percent) fell into two of these categories, 115 (42 percent) met one of these criteria, and 62 (23 percent) met none of them. Panel B examines the relationship between the number of reasons to file Chapter 13 bankruptcy, disaggregated by county. The chi-square statistic's probability value is 0.213, indicating that filers in different communities are no more or less likely to file for Chapter 13 bankruptcy protection based on a higher or lower number of financially beneficial criteria.

## 6. Conclusions

For nearly two-thirds of Chapter 13 filers, there is a clear reason for filing under Chapter 13 of the U.S. Bankruptcy Code. A surprisingly large number of these filers (89 of 272) are ineligible to file under Chapter 7. But approximately 45 percent of our sample (the 189 filers that are not ineligible to file under Chapter 7, less those 32 files with no obvious reason to file under Chapter 13) receive one or more identifiable, expected financial benefits from filing under Chapter 13. This brings into question the effectiveness of the BAPCPA means test (Hackney, McPherson and Friesner 2011). According to the Districts Reports ([http://www.waeb.uscourts.gov/sites/default/files/waeb/filing\\_statistics/10%20Year%20Review.pdf](http://www.waeb.uscourts.gov/sites/default/files/waeb/filing_statistics/10%20Year%20Review.pdf)), in 2005 there were 1772 Chapter 13 filings (and 1967 in 2004). Yet between 2008 and 2013, the number of Chapter 13 filings has consistently fluctuated between 1027 filings (in 2013) and 1404 filings (in 2009). This indicates that BAPCPA does not consistently shift more debtors into Chapter 13 filings. This analysis posits a simple reason to explain these trends. While the means test shifts few debtors from Chapter 7 to Chapter 13, other incentives are present for Chapter 13 filers, or that filer's attorney, to induce a Chapter 13 filing.

The data show the emergence of important distinctive debtor characteristics, measured by county. Almost one third of Yakima County filers, Table 2, Panel B, utilize Chapter 13 to pay their traffic fines while maintaining their driver's license. This is much higher than the other county measurements. Does Yakima County have worse drivers? Is the County more likely to revoke a typical driver's privileges? Or have attorneys who practice in Yakima County simply devised a clever strategy for protecting bad drivers? The last possibility, while not demonstrated in this manuscript, is certainly the most interesting (and perhaps the most persuasive) explanation. Future research is necessary to empirically identify which of these rationales is the most appropriate.

Spokane County has a much higher ratio, 41 of 88, of debtors needing protection from the I.R.S. This phenomenon likely has two causes. The first plausible explanation is that Spokane County's higher resident incomes<sup>4</sup> generate more tax debt, which some debtors fail to pay. Alternatively, the Spokane bankruptcy lawyers may have developed unique Chapter 13 based strategies for dealing with these claims. Again, future research is necessary to identify which of these explanations is consistent with reality.

The higher ratio of Spokane arrear mortgage cases, 29 of 59, may reflect higher home ownership in Spokane County (or simply larger mortgages and higher home prices facilitated by

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<sup>4</sup> According to the Washington State Office of Financial Management's website (<http://www.ofm.wa.gov/economy/hhinc/>) median household incomes in the District were highest in urban counties, including Spokane County.

higher median household incomes), early response to the pre 2007-2008 financial mortgage crisis and/or the presence of Spokane lawyers advertising to meet this exigency. Even if home equity turns out to be illusory after the mortgage meltdown, the early debtors (2005-2007) may be tempted to try and save their homes, which can be accomplished with a Chapter 13 filing.

Perhaps more curious is that approximately 32 percent (62 out of 272) of all filers accrue no obvious financial benefit from filing under Chapter 13, and would be better off financially by filing under Chapter 7. There are two possible implications from this finding, neither of which is mutually exclusive. First, the individual files under Chapter 13 not to capture a financial gain or because they are prohibited from filing under Chapter 7, but because the debtor feels a moral obligation to repay some or all outstanding obligations while financially reestablishing themselves. Second, because Chapter 13 filers establish a repayment plan (a portion of which accrues to the filer's attorney on a regular basis), attorneys may achieve greater revenue from a Chapter 13 filing (both on total and in terms of a flow of income over time) than a Chapter 7 filing (Hackney *et al.* 2014). In either case, this analysis suggests that legal culture plays a very significant role in bankruptcy chapter filing choices. Further research is necessary to understand why legal culture plays such a prominent role in these decisions, and to examine the formation of legal culture using smaller or more specific definitions of a community than a county.

While this study presents some interesting findings, the results should be interpreted with caution. The analysis uses data from a single U.S. Bankruptcy District, which may or may not be generalizable to other districts. The formation of legal culture may be different across each of these districts. If different communities have different views on (and stigmas associated with) filing for bankruptcy, how people respond to bankruptcy-related incentives may be altered, and by extension affect the rates of Chapter 13 filings in that district. This, in turn, would require more complicated experimental designs than are used in this study in order to appropriately account for the formation of legal culture. Lastly, the analysis used in this study is descriptive rather than causal. Future studies that use more sophisticated methods of data analysis (i.e., regression) and employ a larger number of financial and cultural variables would undoubtedly extend the results contained herein.

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**Table 1: Reasons to File for Chapter 13 Bankruptcy****Panel A: County of Residency (Proxy for Local Legal Culture)**

<u>County</u>	<u>Population</u>	<u>Number of Filers</u>	<u>Proportion of Filers</u>	<u>Proportion of District Population in 2006</u>	<u>Expected Number of Filers per County</u>
Benton & Franklin	228,626	39	0.143	0.162	44
Spokane	446,751	88	0.324	0.316	86
Yakima	234,406	90	0.331	0.166	45
All Other Counties	504,129	55	0.202	0.357	97
Total	1,413,912	272	1.000	1.000	272
Chi-Square Test of Homogeneity Probability					<0.001

**Panel B: Ineligibility to File under Chapter 7 (Recent, Prior Bankruptcy)**

<u>Recent, Prior Chapter 13 Filing</u>	<u>Number of Filers</u>
Existence of a Recent, Prior Bankruptcy	89
No Recent, Prior Chapter 13 Filing	183
Total	272
Chi-Square Test of Homogeneity Probability	<0.001

**Panel C: Outstanding Traffic and Related Fines**

<u>Traffic Fines</u>	<u>Number of Filers</u>
Existing Traffic and Related Fines	53
No Such Fines	219
Total	272
Chi-Square Test of Homogeneity Probability	<0.001

**Panel D: Outstanding Tax Obligations**

<u>Tax Obligations</u>	<u>Number of Filers</u>
Existing Tax Obligations	85
No Tax Obligations	187
Total	272
Chi-Square Test of Homogeneity Probability	<0.001

**Panel E: Arreared Domestic Support Obligations**

<u>Domestic Support Obligations</u>	<u>Number of Filers</u>
Existing Domestic Support Obligations	25

No Domestic Support Obligations	247
Total	272
Chi-Square Test of Homogeneity Probability	<0.001

***Panel F: Arreared Mortgage Obligations***

<b><u>Arreared Mortgage Obligations</u></b>	<b><u>Number of Filers</u></b>
Existing Arreared Mortgage Obligations	63
No Arreared Mortgage Obligations	209
Total	272
Chi-Square Test of Homogeneity Probability	<0.001

***Panel G: Negative Automobile Equity***

<b><u>Automobile Equity</u></b>	<b><u>Number of Filers</u></b>
Negative Automobile Equity	32
Zero or Positive Automobile Equity	240
Total	272
Chi-Square Test of Homogeneity Probability	<0.001

Population Data Source:  
<http://www.ofm.wa.gov/pop/april1/hseries/default.asp>

**Table 2: Number of Reasons to Declare a Chapter 13 Bankruptcy*****Panel A: Ineligibility to File under Chapter 7 (Recent, Prior Bankruptcy)***

<u>County</u>	<u>Recent, Prior Bankruptcy</u>	<u>No Recent, Prior Bankruptcy</u>	<u>Total</u>
Benton & Franklin	6	33	39
Spokane	32	56	88
Yakima	31	59	90
All Other Counties	20	35	55
Total	89	183	272
Chi-Square Test of Homogeneity Probability			0.098

***Panel B: Outstanding Traffic and Related Fines***

<u>County</u>	<u>Traffic (and Related) Fines</u>	<u>No Such Fines</u>	<u>Total</u>
Benton & Franklin	9	30	39
Spokane	14	74	88
Yakima	26	64	90
All Other Counties	4	51	55
Total	53	219	272
Chi-Square Test of Homogeneity Probability			0.010

***Panel C: Outstanding Tax Obligations***

<u>County</u>	<u>Outstanding Taxes</u>	<u>No Such Taxes</u>	<u>Total</u>
Benton & Franklin	8	31	39
Spokane	41	47	88
Yakima	19	71	90
All Other Counties	17	38	55
Total	85	187	272
Chi-Square Test of Homogeneity Probability			0.001

***Panel D: Arreared Domestic Support Obligations***

<u>County</u>	<u>Arreared Domestic Support Obligations</u>	<u>No Such Domestic Support Obligations</u>	<u>Total</u>
Benton & Franklin	2	37	39
Spokane	7	81	88
Yakima	12	78	90
All Other Counties	4	51	55
Total	25	247	272
Chi-Square Test of Homogeneity Probability			0.388



***Panel E: Arreared Mortgage Obligations***

<b><u>County</u></b>	<b><u>Arreared Mortgage Obligations</u></b>	<b><u>No Such Mortgage Obligations</u></b>	<b><u>Total</u></b>
Benton & Franklin	9	30	39
Spokane	29	59	88
Yakima	17	73	90
All Other Counties	8	47	55
Total	63	209	272
Chi-Square Test of Homogeneity Probability			0.047

***Panel F: Negative Automobile Equity***

<b><u>County</u></b>	<b><u>Negative Automobile Equity</u></b>	<b><u>No Such Negative Equity</u></b>	<b><u>Total</u></b>
Benton & Franklin	5	34	39
Spokane	12	76	88
Yakima	8	82	90
All Other Counties	7	48	55
Total	32	240	272
Chi-Square Test of Homogeneity Probability			0.776

**Table 3: Number of Financially Beneficial Reasons to Declare a Chapter 13 Bankruptcy**

***Panel A Total Number of Reasons***

<b><i>Reasons</i></b>	<b><u>Count</u></b>
<b>No Reasons</b>	62
<b>One Reason</b>	115
<b>Two Reasons</b>	62
<b>Three Reasons</b>	26
<b>Four Reasons</b>	6
<b>Five or More Reasons</b>	1
<b>Total</b>	272
Chi-Square Test of Homogeneity Probability	< 0.001

***Panel B: Reasons Disaggregated by County***

<b><u>County</u></b>	<b><u>None</u></b>	<b><u>One</u></b>	<b><u>Two</u></b>	<b><u>Three</u></b>	<b><u>Four</u></b>	<b><u>Five or More</u></b>	<b><u>Total</u></b>
Benton & Franklin	11	19	7	2	0	0	39
Spokane	13	34	27	11	2	1	88
Yakima	22	37	20	8	3	0	90
All Other Counties	16	25	8	5	1	0	55
Total	62	115	62	26	6	1	272
Chi-Square Test of Homogeneity Probability							0.489
Chi-Square Test of Homogeneity Probability (Combining the Last Two Columns into a Single Column)							0.403
Chi-Square Test of Homogeneity Probability (Combining the Last Three Columns into a Single Column)							0.213

Note: The individual with five or more reasons had six reasons to declare bankruptcy.