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The Past, Present, and Future of Bankruptcy Law in America

By Todd J. Zywicki

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Abstract

This essay reviews David A. Skeel, Jr., *Debt's Dominion: A History of Bankruptcy Law in America*. Although nominally a book about the history of bankruptcy law in America, Skeel's book is a comprehensive analysis of the past, present, and future of bankruptcy law in America. Skeel divides the history of bankruptcy law in America into three historical stages: the Nineteenth Century, the era of the 1898 Bankruptcy Act and the Great Depression, and the modern era of the 1978 Bankruptcy Code. As Skeel notes, the shape of bankruptcy law and practice throughout American history is at least as much a factor of political considerations and influence as economic considerations. To develop his point, Skeel draws on the fields of public choice and social choice, both of which apply the assumptions and tools of economics to the study of political science. Skeel uses these tools to shape his narrative, giving his argument an analytical edge that prior historical studies of American bankruptcy law have lacked. In particular, American bankruptcy law can be understood as resulting from the clash of three sets of interests: pro-debtor ideological interests (often spearheaded by law professors), creditors, and bankruptcy professionals (including bankruptcy judges). Although the outcome of this three-way struggle is unclear at any given moment, the dominant course of evolution of American bankruptcy law has been towards increasingly-generous bankruptcy laws that provide strong incentives for both individual and corporate debtors to file bankruptcy.

Building on Skeel's insights, I then offer my own impressions of the current debate over the bankruptcy reform act as well as the future of bankruptcy law in America. Although largely explained by the factors identified by Skeel, the current debate over the bankruptcy reform act has introduced a new element to the traditional debate—an ideology of personal responsibility ushered in by the Republican takeover of Congress in 1994 that has offset the traditional dominance of prodebtor ideology. At the same time, the bankruptcy system has become sufficiently unbalanced in a prodebtor direction that creditors have been able to overcome the collective action problems that have undermined prior reform efforts. These historical developments have made bankruptcy reform possible, unlike reform efforts in the past. With respect to the future of bankruptcy law, this essay argues that the likely result will be global convergence on efficient bankruptcy laws. Building on prior work demonstrating convergence on efficient corporate law rules in the American federal system, this essay argues that globalization will drive a similar convergence on efficient bankruptcy laws. This will encourage countries with excessively prodebtor laws, such as the United States, to adopt less-generous laws; it should also induce European countries to loosen their laws so as to encourage greater entrepreneurship and risk-taking.

Keywords: Bankruptcy, Consumer Bankruptcy, Bankruptcy Reorganization, Rent-Seeking, Political Economy

JEL Codes: D14, D72, G33, K22

THE PAST, PRESENT, AND FUTURE OF BANKRUPTCY LAW IN AMERICA
BY TODD J. ZYWICKI*

DEBT'S DOMINION: A HISTORY OF BANKRUPTCY LAW IN AMERICA. By *David A. Skeel, Jr.* Princeton: Princeton University Pres. 2001. pp. xi, 281. Cloth, $35.

As this review was being written, after failures in the past two Congresses, Congress was once again on the verge of passing a comprehensive bankruptcy reform bill. At the same time, WorldCom, Enron, Global Crossing, and their ignominious peers continue to set records for the size, expense, and public attention drawn to business bankruptcy. For the first time, consumer bankruptcies surpassed the 1.5 million per year mark, continuing an irresistible upward trend. Meanwhile, as law firms announce layoffs and salary freezes in most departments, bankruptcy professionals prosper amidst the despair, billing $20 million per month on the Enron case alone—even as creditors and shareholders sit by awaiting payment. Clearly we are witnessing a profound and unprecedented change in the political, social, and economic framework of bankruptcy.

How did we get here and where are we headed in the future? These are the questions brilliantly addressed by David A. Skeel, Jr., in his book, *Debt's Dominion: A History of Bankruptcy Law in America*. Told with a sound understanding of theory, law, and an eye for detail, Skeel's book is an instant classic—a comprehensive and intriguing history of bankruptcy law in America. But to characterize it as "history" is to slight the book's reach and importance. In a concise and readable 250 pages, Skeel brings to life not only the political and economic history of bankruptcy law, but also the fascinating history of the bankruptcy bar itself. Finally, Skeel deftly leads the reader through the fundamental theoretical debates that have shaped bankruptcy law during the past century, including the contentious intellectual debates between "Progressive" academic theorists and their rivals from the "Law and Economics School." Skeel has at once written a book that will serve as the definitive work on the history of bankruptcy law for bankruptcy experts while also crafting a book accessible to the interested generalist in law or business who seeks a comprehensive guide to how the modern American bankruptcy system developed.

This review will consider the past, present, and future of bankruptcy law through the lens of Skeel's analysis. Part I will provide an overview of Skeel's historical thesis, including the novel theoretical methods he uses to advance his analysis. Part II examines the current state of bankruptcy law, focusing particularly on the political and economic battles involving bankruptcy reform during the past several years. Part III considers Skeel's predictions as to the future evolution of bankruptcy law and practice in America and abroad.

I. The Past: The History of Bankruptcy Law in America

Skeel divides the history of bankruptcy law in America into three historical stages: the Nineteenth Century, the era of the 1898 Bankruptcy Act and the Great Depression, and the modern era of the 1978 Bankruptcy Code. As Skeel notes, the shape of bankruptcy law and

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practice throughout American history is at least as much a factor of political considerations and influence as economic considerations. To develop his point, Skeel draws on the fields of public choice and social choice, both of which apply the assumptions and tools of economics to the study of political science. Skeel uses these tools to shape his narrative, giving his argument an analytical edge that prior historical studies of American bankruptcy law have lacked.[1] In particular, American bankruptcy law can be understood as resulting from the clash of three sets of interests: pro-debtor ideological interests (often spearheaded by law professors), creditors, and bankruptcy professionals (including bankruptcy judges). Although the outcome of this three-way political wrestling match is unclear at any given moment, the dominant course of evolution of American bankruptcy law has been towards increasingly-generous bankruptcy laws that provide strong incentives for both individual and corporate debtors to file bankruptcy.

A. Bankruptcy Legislation in the Nineteenth Century

The first era of American bankruptcy legislation was rooted in the Constitution's enumeration of Congress's power to "establish uniform laws on the subject of Bankruptcies throughout the United States."[2] Like the other economic provisions of the Constitution, the primary purpose of the Bankruptcies Clause of the Constitution was to reign in the pro-debtor excesses of state legislatures under the Articles of Confederation.[3] Under the Articles of Confederation, creditors confronted numerous obstacles to their attempts to collect judgments, including judgment-jumping from one state to another and efforts by some states to discharge obligations owed by debtors, primarily at the expense of out-of-state creditors.[4] According to James Madison, regulation of bankruptcy was "intimately connected with the regulation of commerce, and [would] prevent so many frauds where the parties or their property may lie or be removed into different states that the expediency of it seems not likely to be drawn into question."[5] Subject to these powers designed to augment the power of creditors to recover judgments, most debtor-creditor relations was to remain governed by state law, an allocation of power which remains the case today.

During the Nineteenth Century, the federal government enacted three bankruptcy laws prior to the 1898 Act: the Bankruptcy Acts of 1800, 1841, and 1867 (p. 25). Each Act was spawned in the midst of financial crisis and was repealed soon thereafter. The 1800 Act lasted only three years, the 1841 Act lasted only two years, and the 1867 Act was repealed eleven years later. All together, therefore, these three acts lasted a total of sixteen years. In the intervening periods, debtor-creditor relations remained wholly the province of state law. Skeel demonstrates that this instability resulted from "legislative cycling," a phenomenon identified by economists and political scientists that can arise where lawmakers hold three or more positions which cannot be aligned on a simple linear spectrum of choices (p. 28). Skeel identifies three

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[1] The classic study has been CHARLES WARREN, BANKRUPTCY IN UNITED STATES HISTORY (1935).
[2] U.S. CONST. Art. 1, §8.
[3] *See* Todd J. Zywicki, *The Bankruptcy Clause*, *in* THE HERITAGE GUIDE TO THE CONSTITUTION (forthcoming 2002).
[4] Thus, although conventional wisdom has it that the Bankruptcy Clause of the Constitution was a protection for debtors, it was primarily the reverse. Indeed, many states maintained imprisonment for debt well into the Nineteenth Century. *Id.*
[5] *See* THE FEDERALIST NO. 42 (James Madison).

different positions with respect to bankruptcy, each identified with a particular region of the country, and each of which had approximately equal support. As a result of these tensions, bankruptcy legislation was enacted only in periods of crisis, receding soon afterwards. Even then, it was often necessary to engage in political logrolling in order to fashion a majority. Given the regional nature of the American economy for most of the Nineteenth Century, however, there was little need for national bankruptcy legislation in most circumstances, leaving debtor-creditor relations largely in the hands of state governments.

B. The Bankruptcy Act of 1898 and the Great Depression

The decades following the Civil War saw an increasing nationalization of the American economy, spurred by advances in communications and transportation technology, such as railroads, electricity, the air brake, the elevator, and the steam boiler.[6] Millions of Americans left rural farms for urban factories, accompanied by millions more new immigrants.[7] The number of factories nearly quadrupled from 140,000 in 1865 to 512,000 in 1900, and the size of factories grew even more rapidly.[8] Between 1870 and 1900 the nationwide rail network grew from 53,000 to 193,000 miles.[9] Accompanying the rise of the national economy was the rise of a host of new special-interest groups representing an interstate constituency.[10]

Skeel focuses on the large number of commercial organizations that were founded during this period, arguing that they provided the impetus that eventually led to the 1898 Bankruptcy Act (p. 35). In particular, the overlay of an emerging national economy onto a state-based system of debt collection created numerous problems. "Merchants who engaged in interstate commerce complained bitterly and repeatedly that debtors played favorites when they ran into financial trouble," he writes (p. 36), adding that, "The favorites were family members and local creditors, not the out-of-state merchants."

The primary impetus for the 1898 Act, therefore, was the efforts of creditors to develop more streamlined procedures for debt collection, especially on interstate debts. But Skeel notes two anomalies of the 1898 Act as finally enacted: first, the primary beneficiaries of the Act were bankruptcy lawyers rather than creditors, and second, that the 1898 Act turned out to much more debtor-friendly than originally anticipated (p. 43). As Skeel observes of the finished product, "These characteristics—the generally debtor-friendly approach to bankruptcy, and the primacy of lawyers rather than an administrator—distinguish U.S. bankruptcy law from every other insolvency law in the world." (p. 43).

The lawyer-friendly and debtor-friendly characteristics of the 1898 Act have distinguished American bankruptcy law ever since. Moreover, they served to end the century of legislative cycling that had undone previous bankruptcy laws. The debtor-friendly nature of the 1898 Act created reflected the rise of an American populist ideology that continues to

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[6] *See* ROBERT D. PUTNAM, BOWLING ALONE: THE COLLAPSE AND REVIVAL OF AMERICAN COMMUNITY 368 (2000).
[7] *Id*. at 370-71.
[8] *Id*. at 369.
[9] *Id*.
[10] *See* Todd J. Zywicki, *Beyond the Shell and Husk of History: The History of the Seventeenth Amendment and its Implications for Current Reform Proposals*, 45 CLEV. ST. L. REV. 165 (1997); Todd J. Zywicki, *Senators and Special Interests: A Public Choice Analysis of the Seventeenth Amendment*, 73 OR. L. REV.1007 (1994).

permeate the bankruptcy debates today. Although lawyers did not provide the impetus for the 1898 Act, they "came out of the woodwork to fill the need" created by the new law (p. 43). This created an entrenched and well-organized constituency who would benefit from the perpetuation of the law and therefore could be counted on to oppose any future repeal or major innovations, thereby ending legislative cycling in Congress.[11]

The 1898 Act remained in place until supplanted by the 1978 Code. During this period, however, bankruptcy law and practice was certainly not static. The invention of equity receiverships as a judicial procedure to reorganize the railroads at the turn of the century, the intervention of the Great Depression, and William O. Douglas's high-profile hearings while Chairman of the Securities and Exchange Commission are also among the pivotal incidents recounted by Skeel. From this economic and political process emerged the Chandler Act amendments to the Act, which increased governmental oversight of the bankruptcy process. Although space limits the ability to discuss these developments in detail here, the end result of these developments was to drive prestigious Wall Street law firms from bankruptcy practice. At the same time, ordinary bankruptcy lawyers remained unscathed, and in many ways richer and more influential than ever before.

C. The 1978 Bankruptcy Code

By the 1970s the creaky construct of the 1898 Act was ripe for overhaul. Again the impetus came from creditors who were frustrated with the rising number of personal bankruptcy filings during the 1960s. Filings tripled from 50,219 in 1950 to 178,202 in 1970. Although trivial by modern standards, at the time this rise sparked concern. Nonetheless, creditors once again lost control of the process they initiated, as the bar again seized the reins of the reform effort. By the time the process was over, both personal and business bankruptcy laws were made more lax rather than strict. Skeel documents a series of bankruptcy "scope expanding" reforms that resulted in increased bankruptcy filings (both personal and business), as well as a more expansive role generally for bankruptcy law in the American economy and society. In addition, the 1978 Code brought Wall Street lawyers and banks back into bankruptcy practice by increasing fees, increasing prestige, and further weakening public oversight of the process by elimination of the SEC's oversight role. The end result was to reinvigorate professional control of bankruptcy proceedings and professional influence in Congress. As Skeel notes, ideology was muted throughout the process that culminated in the 1978 Code, leading to a belief that bankruptcy was primarily a "technical" process best left to the "experts"—namely, bankruptcy professionals. Wrapped in the veneer of expertise, bankruptcy professionals further entrenched their influence over bankruptcy proceedings and legislation, fending off efforts to retrench the scope or expense of either personal or business bankruptcy. As Bruce Carruthers and Terence Halliday observe in their study of the 1978 Code, following its enactment "bankruptcy professionals experienced a meteoric rise in their professional identity, their market position, and the rewards accompanying both."[12] Similarly, Congressman Robert Drinan observed during the debates over the 1978 Code that it amounted to a "'full employment' bill for lawyers."[13]

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[11] Saul Levmore, *Voting Paradoxes and Interest Groups*, 28(2) J. LEG. STUD. 259 (1999).
[12] BRUCE G. CARRUTHERS AND TERENCE C. HALLIDAY, RESCUING BUSINESS: THE MAKING OF CORPORATE BANKRUPTCY LAW IN ENGLAND AND THE UNITED STATES 421 (1998).
[13] *Id*. at 302 (quoting Congressman Robert Drinan).

The 1978 Bankruptcy Code profoundly changed the bankruptcy system and its importance in society and the economy. By making bankruptcy more attractive to individuals, personal bankruptcies have risen from less than 200,000 in 1978 to almost 1.5 million annually. By making bankruptcy more attractive for corporations as well, it has routinized corporate bankruptcy as well, turning it into a business and strategic decision rather than a last resort. The wealth and prominence of bankruptcy professionals has risen as well, escaping the unsavory ghetto in which they toiled for decades after the New Deal reforms. Today, the largest and most prestigious law firms, investment banks, accounting firms, and consultants in America have thriving bankruptcy practices, representing all interests in the bankruptcy system, including debtors. And although piecemeal reforms enacted in 1984 reined in some of the excesses of the 1978 Code, they did little to stem the rising tide of consumer bankruptcy filings or to reduce the expense and delay associated with the chapter 11 process.

D. The Lessons of History

The 1898 Act thus set in place the three political interests that have shaped American bankruptcy law from 1898, through the 1978 Code, to the present: (1) creditor interests, (2) pro-debtor interests (usually ideological, rather than particular), and (3) the interests of bankruptcy professionals. As Skeel notes, however, of all these groups "bankruptcy professionals are the ones who have most strongly influenced the shape of U.S. bankruptcy law in the century since its enactment in 1898." (p. 81). This is because, compared to other interest groups, bankruptcy lawyers are relatively better-positioned than other interest groups to influence the legislative process. It is important to keep in mind that interest-group influence is a matter of *relative* influence, not *absolute* influence.[14] Thus, in general, even if interest-group A is less-organized than some other interest group B, A will still be favored in the political process relative to even more dispersed and unorganized groups, except for the rare situation where A's and B's positions are squarely opposed. In general, however, gains to trade are available among interest groups such that comparatively well-organized interest groups can form alliances to provide shared benefits to themselves and to impose the costs on the unorganized public.[15] Following Mancur Olson, Skeel observes that interest-group influence is primarily a function of how homogeneous, coherent, politically-savvy, and well-organized the group is.

Public choice analysis illuminates why bankruptcy lawyers have proven such a potent lobbying force. Bankruptcy lawyers have clear goals—to increase the number of bankruptcies filed and the expense of each. Regardless of a whether a particular lawyer represents debtors, creditors, or both, the fact remains that bankruptcy lawyers can make money only if individuals and corporations file bankruptcy. Thus, bankruptcy lawyers generally will seek to increase both the number of bankruptcy cases filed and the expense of bankruptcy proceedings. This also means that even though debtors and potential debtors are not directly represented in the bankruptcy process, their interests are usually well-represented by bankruptcy attorneys who will lobby for open access to bankruptcy for debtors. Moreover, the highly technical and complex nature of bankruptcy law and practice increases the leverage of lawyers in the

[14] *See* Todd J. Zywicki, *Environmental Externalities and Political Externalities: The Political Economy of Environmental Regulation and Reform*, 73 TULANE L. REV. 845 (1999).
[15] For examples drawn from the field of environmental regulation, see *id*.

legislative process both by making their expertise an essential part of the legislative process as well as making it more difficult for the public and lawmakers to monitor their special-interest influence on particular provisions that may seem unimportant but can have vast effect on a lawyers' wealth (p. 87). This technical expertise further heightens the influence of lawyers when lawmakers move from issues of broad principle to technical legislative drafting (p. 46).

Although creditors have clear interest in the content of bankruptcy laws, they suffer several problems in exercising political influence when compared to bankruptcy professionals.[16] First, many creditors, such as trade creditors, are simply too hard to organize into an effective lobbying group because of their large numbers and the small stake each has in changing the law. Second, unlike bankruptcy lawyers, the interests of creditors are not homogeneous, creating collective action problems. Because a debtor by definition is unable to pay his debts, secured creditors and unsecured creditors usually are locked in a zero-sum game regarding distribution of the debtor's estate. A bigger slice for secured creditors means less for unsecured creditors, and vice-versa. Third, to the extent that unsecured credit becomes more risky because of easy access to bankruptcy, this will raise the cost of unsecured credit and create a market substitution toward greater use of secured credit.[17] Thus, secured creditors will have little concern about the overall number of bankruptcy filings or the amounts distributed, although they will care about specific issues that affect them, such as cramdown and valuation issues.

The incentive for creditors to lobby for changes in the bankruptcy system will also be mitigated by the fact that any gains will be temporary. Tightening bankruptcy laws to reduce risk retroactively will create a one-time opportunity to earn economic profits, but competition and entry into the market will dissipate those profits, returning all lenders to a competitive equilibrium. Creditors are able to pass along some of their losses to borrowers who repay their debts—"repayers"—in the form of higher downpayments, higher interest rates, and reduced benefits (p. 82). Because this mitigates some of the creditors' losses, this further reduces the incentives of creditors to lobby for changes to tighten bankruptcy laws. Repayers face even more daunting obstacles to making their voices heard—given the small cost borne by each repayer as a result of excessive bankruptcies, each has minimal incentive to try to influence the legislative process. Moreover, repayers have no effective proxy representative for their interests, unlike bankruptcy filers who can count on bankruptcy lawyers to aggressive advance their interests in the political process.

The final influence on the bankruptcy process is the tradition of pro-debtor, populist and progressive ideology in American politics. These bankruptcy "progressives" view bankruptcy as an economic and social safety valve to redistribute wealth to the poor and to preserve struggling businesses. Skeel also notes the major involvement of bankruptcy law professors in the legislative process, such as Vern Countryman, usually articulating a pro-debtor ideological perspective. Finally, so-called "consumer advocates" such as Ralph Nader have also tended to favor expansion of access to the bankruptcy system on populist principle, even though easy bankruptcy access only benefits the small class of bankrupt consumers, not the larger class of

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[16] *See* Todd J. Zywicki, Book Review, 16 BANKR. DEV. J. 361, 387-88 (2000) (reviewing Bruce G. Carruthers and Terence C. Halliday, *Rescuing Business: The Making of Corporate Bankruptcy Law in England and the United States* (1998)).

[17] *See* Todd J. Zywicki, *The Economics of Credit Cards*, 3 CHAPMAN L. REV. 79 (2000).

consumers who repay their debts and thereby subsidize those who file bankruptcy. As Skeel notes, this progressive ideology has greatly influenced the shape of American bankruptcy legislation.

Thus, the history of American bankruptcy legislation is not surprising. Reform efforts are initiated in the rare instances when creditors are able to overcome their collective-action problems and progressive ideological opposition to push for reforms. Once the process is commenced, however, both the process and the technical drafting of legislation is soon captured by lawyers. In the end, lawyers usually manage to side-track the reforms that were originally sought and instead end up turning the legislation to their own advantage.

II. The Bankruptcy Reform Act of 2002

Skeel's analysis helps to unravel the politics surrounding the Bankruptcy Reform Act of 2002 (the "BRA"), which was finally ready to be passed in August 2002 after a long and arduous legislative process. The reform efforts were initiated in 1994, when Congress authorized a new commission to conduct a study of bankruptcy law and to recommend changes, the National Bankruptcy Review Commission ("NBRC") (p. 187). Modeled after the 1973 Commission, the NBRC was charged with a similar task of reviewing the Code and recommending changes and updates. The bankruptcy world had certainly changed dramatically in the intervening quarter-decade. In 1978, when the new Code was enacted, there were 172,423 nonbusiness bankruptcy filings. By the time the NBRC was chartered in 1994, the consumer bankruptcy filing rate had quadrupled to over 800,000 annually, and has almost doubled again since then. Moreover, the rise of LBOs, junk bonds, and mass tort litigation had all changed business bankruptcy substantially.

Unlike the 1973 Commission, however, the NBRC's deliberations and conclusions were highly divisive and controversial, especially regarding consumer bankruptcy issues. As Skeel writes, "In its consumer recommendations, the 1994 commission's report took a prodebtor case, firmly rejecting calls to tighten the bankruptcy laws and vigorously defending consumer debtors' right to an immediate discharge. Consumer creditors were less than enthusiastic with the process." (p. 187). NBRC Reporter Elizabeth Warren, the acknowledged leader of the modern bankruptcy progressives, excluded contrary views and orchestrated a set of recommendations that advanced the unique perspectives of its leaders (p. 201). Despite the "blue ribbon" composition of the NBRC, its idiosyncratic ideological orientation guaranteed that its recommendations would be dead on arrival when presented to Congress in 1996. Unsurprisingly, when Congress actually turned to the task of reforming the bankruptcy laws, it moved in the direction of tightening the laws, rather than loosening them, efforts which finally culminated in enactment of the BRA several years later.

Launched with fanfare, the NBRC had at its disposal ample financial, intellectual, and political resources. Nonetheless, the NBRC process quickly ran off the rails of moderation and compromise, producing a one-sided and politically stillborn product. Instead of following the Commission's prodebtor recommendations, Congress immediately proposed a bankruptcy reform bill that tightened the bankruptcy laws by weeding out fraud and abuse in consumer cases and enacting reforms designed to reduce the cost and delay of small-business bankruptcies. Skeel asks, "How did so much dysfunction come from a commission who innocuous-sounding charge was to look for ways to perfect a generally adequate framework?"

(p. 198). In addition, why were the political dynamics in this situation so strongly oriented toward reform that the BRA was able to overcome the traditional obstacles that had prevented comprehensive reform in the past?

In part, both the NBRC's dysfunction and the BRA's reforms occurred because of the different ideological orientations of the NBRC and Congress during the 1990s. In contrast to the leftward tilt of the NBRC and its leaders, the Republican takeover of Congress in 1994 made the Washington political environment turned much more ideologically conservative, leading to a political and intellectual environment that was decidedly unfriendly to the NBRCs prodebtor recommendations (p. 199). Skeel attributes this distinction to the academic debate between "progressive" scholars on one hand and "law and economics" scholars on the other. Although there is much truth to this analysis, I believe it is incomplete. Based on my personal experience as an advisor to Congress for the past several years on bankruptcy reform, I believe that Congress is animated by a new political ideology of "personal responsibility" that serves as an counterweight to the traditional prodebtor ideology.[18] Although it overlaps in many ways with law and economics ideas, there is much in the personal responsbility ideology that is not captured by the "law and economics" label, which connotes an overriding concern with economic efficiency. The personal responsibility ideology sees consumer bankruptcy as primarily a *moral* issue, rather than as an economic issue. To be sure, personal responsibility and law and economics arguments often reinforce one another, as much of the personal responsibility rhetoric stresses the injustice of forcing responsible consumers to subsidize the recklessness of profligate borrowers. But the distinction is deeper than just economics: soaring consumer bankruptcy filing rates is viewed as a crisis of the American soul, rather than a mere matter of economic policy. Put simply, there is no economic explanation for the upsurge in individual bankruptcy filings in the late-1990s, an era of unprecedented prosperity, low interest rates, low unemployment rates, and roaring levels of individual wealth. Given the anomaly of economic prosperity combined with soaring bankruptcy filings, many have concluded that the problem is social and spiritual, rather than economic.[19]

This focus on an ideology of personal responsibility is evident in the debates. Consider the comments of House Majority Leader Richard Armey, "Bankruptcy laws in America have put a lie to one of the most important lessons we teach our children. Bankruptcy laws in America have said to our children, you are a fool if you do not file. That is not right…. It is not about the money. Anybody who thinks this bill is about who gets the money is missing the point…. This bill is about the character of a Nation and will the Nation's laws have a character of the Nation's people."[20] House Judiciary Chairman James Sensenbrenner similarly remarks, "The purpose of the bill is to improve bankruptcy law and practice by restoring personal responsibility and integrity in the bankruptcy system, and to ensure that the system is fair to both debtors and creditors."[21] When the BRA was reported out of the Conference Committee in

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[18] This political emphasis on personal responsibility is evident in many other areas as well, including most notably, welfare reform. *See* Todd J. Zywicki, *Bankruptcy Law as Social Legislation*, 5 TEX. REV. L. & POL. 393, 430 (2001).
[19] *See id*. at 428-29.
[20] 147 CONG. REC. H518 (daily ed. Mar. 1, 2001) (statement of Mr. Armey).
[21] 147 CONG. REC. H517 (daily ed. Mar. 1, 2001) (statement of Mr. Sensenbrenner).

July 2002, Senator Orrin Hatch compared to recent corporate responsibility initiatives, stating, "In these hard economic times, while we're dealing with corporate responsibility, we should also address personal responsibility."[22] Many liberal leaders have embraced the moral argument in favor of bankruptcy reform, such as Democratic Congressman Barney Frank, who says, "I think that people should have to pay their bills. . . . I am for toughening bankruptcy laws. It's only a minority who ever go bankrupt, and those costs get passed on to the majority who pay their bills."[23] Although economic analysis is entwined in the values argument, much of Congress's interest in consumer bankruptcy reform is rooted in values-based concerns over personal and financial responsibility.[24] Personal bankruptcy is part of a larger set of concerns over the moral character of the nation, its leaders, and the negative impact of rampant breaking of one's financial promises on aspects of reliability, trust, and reciprocity in other aspects of life.[25]

Nesting bankruptcy into a larger social and ideological framework regarding personal responsibility and morality has altered the political balance regarding bankruptcy. According to Douglass North, the power of ideology in political decision-making is that it helps to overcome collective action and free rider problems and thus to motivate action in the face of concentrated interest-group pressures.[26] Non-progressives have traditionally viewed bankruptcy in technical, rather than ideological terms, leaving no articulate philosophical counterweight to the progressives. The development of a personal responsibility ideology in Congress has offset progressive's traditional advantage, creating a shift in the baseline presumptions for Congress as to the appropriate direction for reforms. Ideological voting by politicians also tends to be most pronounced on issues of low public salience, of which bankruptcy appears to be such an issue.[27] The effect of the conservative takeover of Congress in 1994, therefore, effected an ideological shift in Congress that created a momentum for stricter bankruptcy laws anchored in notions of personal responsibility, rather than for the prodebtor reforms favored by the NBRC. This counteroffensive must have surprised the NBRC leaders—whereas previous progressive initiatives had met with minimal ideological opposition, this time the NBRC's recommendations met with fierce ideological opposition from Congress.

The Republican takeover of Congress also dramatically affected the interest-group balance in Congress, weakening the traditional hammerlock exercised by bankruptcy lawyers. When the NBRC was constituted, it was generally believed that its influence would be similar to that of the lawyer-dominated National Bankruptcy Review Commission of the 1970s, which had exercised comprehensive control over the drafting of the 1978 Code. The Commission of the 1970s had effectively served as a "private legislature," exercising agenda control throughout

[22] "Tougher Bankruptcy Laws Likely," Associated Press, July 26, 2002 (Quoted in http://cbs.marketwatch.com (July 26, 2002)).
[23] Anne E. Kornblut, *Credit Card Issuers Seek to Curb Debtors' Bankruptcy Relief*, BOSTON GLOBE, Oct. 11, 1999, at A1.
[24] Todd J. Zywicki, *With Apologies to Screwtape: A Response to Professor Alexander*, 9 J. BANKR. L. & PRACTICE 613 (2000).
[25] Zywicki, *Bankruptcy Law as Social Legislation*, *supra* note.
[26] DOUGLASS C. NORTH, STRUCTURE AND CHANGE IN ECONOMIC HISTORY 51-58 (1981).
[27] *See* Joseph P. Kalt and Mark A. Zupan, *Capture and Ideology in the Economic Theory of Politics*, 74 AM. ECON. REV. 279 (1984).

the entire legislative process that culminated in the 1978 Code. It was generally believed that the NBRC of the 1990s would have a similar influence. As commentators have observed, these "private legislatures" exhibit many of the same interest-group and public choice influences as traditional legislatures. In fact, because of the undemocratic composition of these groups, their narrow scope, and their low public profile, these private law reform groups often exhibit even deeper pathologies than public legislatures.[28] As noted above, lawyers and progressive ideologues share a common interest in the expansion of the role of bankruptcy. Given the pro-debtor ideological orientation of the NBRC and the strong agenda control exercised by its leaders, the interests and influence of bankruptcy lawyers was highly magnified, much more so than in a public legislature.

Given the obvious stake of lawyers in the in the reform process, the polyannish attitude of the NBRC's leaders to the influence of lawyers is striking. Professor Warren, the NBRC reporter, has criticized the attempts of creditors to influence the NBRC's hearings, longing instead for the days when creditors and other interested parties left bankruptcy law up to "the experts": "Those who spent their professional lives in the field, advising Congress either through the National Bankruptcy Conference or later as part of the National Conference of Bankruptcy Judges. Those days have passed."[29] Elsewhere she observes of the NBRC, "The interests of the lobbyists and their collateral acquaintances came as a surprise, but it should not have. Long past were the days when Frank Kennedy could meet with Larry King, Joe Lee, Conrad Cyr, Vern Countryman, Gerry Smith and a handful of other people to work out the basic structure of the 1973 Commission recommendations on consumer bankruptcy."[30] Whereas creditors and other interested parties were dismissed as special interest pleaders, bankruptcy lawyers and judges were viewed as disinterested experts, notwithstanding the vital financial stake that they had in the outcome of the NBRC process. This dichotomy is absurd, but to the extent that key NBRC decision-makers actually embraced a "white hat" versus "black hat" characterization of rival interest groups, it may account for some of the dovetailing of lawyer and ideological interests in the NBRC process. In turn, various organizations of bankruptcy professionals have provided major financial support to progressive researchers that coincidentally tends to support the positions advocated by the bankruptcy bar.[31]

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[28] *See* Alan Schwartz and Robert E. Scott, *The Political Economy of Private Legislatures*, 143 U. PA. L. REV. 595 (1995). To be sure, there are some differences as well as similarities between the NBRC and other private legislatures. Unfortunately, space constraints prevent a more detailed comparison.

[29] Elizabeth Warren, *The Market for Data: The Changing Role of Social Sciences in Shaping the Law*, 2002 WISC. L. REV. 1, 5 (2002).

[30] Elizabeth Warren, *A Principled Approach to Consumer Bankruptcy*, 71 AM. BANK. L.J. 483, 488 (1977).

[31] *See* "The Endowment for Education of the National Conference of Bankruptcy Judges, *available in* <http://ww.ncbj.org/Endowment/Endowsanjaun.htm> (listing recipients of grants from the NCBJ Endowment for Education). A highly-publicized study critical of the impact of means-testing was funded by the American Bankruptcy Institute, another organization of bankruptcy professionals. *See* Marianne B. Culhane and Michaela W. White, *Taking the New Consumer Bankruptcy Model for a Test Drive: Means-Testing for Chapter 7 Debtors*, 7 AM. BANKR. INST. L. REV. 27 (1999). The negative conclusions of the study rest on an erroneous understanding of how the budget allowances for means-testing would be calculated. *See* Edith H. Jones and Todd J. Zywicki, *It's Time for Means-Testing*, 1999 B.Y.U. L. REV. 177, 187-88 (1999).

In the end, the NBRC recommendations eventually comprised a veritable "wish-list" of the positions favored by the bankruptcy bar. Although the NBRC's recommendations cover a vast scope, they almost uniformly increase the power, prestige, and wealth of bankruptcy lawyers and judges. This included such items as prohibitions of pre-bankruptcy waivers of bankruptcy rights in Chapter 11 cases (such as waiver of the right to file bankruptcy or waiver of the automatic stay), Article III status for bankruptcy judges, recommendations for greater use of bankruptcy to resolve mass tort issues, and numerous recommendations in the consumer area that increased the incentives to file bankruptcy.[32]

Bankruptcy professionals also lobbied intently against the BRA in Congress, and while successful at delaying reform, in the end they were unable to defeat it. In the end, opponents of reform were able to count on only 20%-25% of Congress to oppose reform. Moreover, even this meager figure includes the votes of those who voted against the BRA not from ideological or interest-group solidarity regarding its core provisions, but because of opposition on tangential issues such as proposed limits on the homestead exemption or the "Schumer Amendment" relating to nondischargeability of civil judgments imposed on abortion-clinic protestors. Many of these members, especially conservatives from Texas and Florida, clearly supported the core provisions of the BRA. In the end, therefore, the only substantive opposition to bankruptcy reform came from the extreme prodebtor fringe of the ideological spectrum and politicians who were especially beholden to financial contributions by lawyers.[33] Despite these intense lobbying efforts, bankruptcy professionals were unable to replicate their previous successes in turning the reform process to their advantage. Although a final reckoning of the reasons why will require further study in the future, my personal experience suggests two reasons why this was the case.

First, the Republican takeover of Congress not only changed the ideological orientation of Congress, it also dramatically changed the political balance. Lawyers are simply less-influential and less-friendly with Republicans than with Democrats, especially in the Judiciary Committee, which traditionally has been the private playground for lawyers. The overwhelming majority of lawyers' political contributions flow to Democratic politicians.[34] Moreover, on important issues such as tort reform and others, the Republican legislative agenda is fiercely opposed by a core Democratic constituency. Given this history, special-interest pleading by lawyers generally is less well-received by Republican congresses than by Democratic predecessors.

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[32] For instance, bankruptcy lawyers attempted to force through a recommendation to weaken the disinterestedness requirement, but the initial vote on the effort to do so was later reconsidered after it drew substantial opposition from other members of the Commission. The incident is described in Todd J. Zywicki, *Mend It, Don't End It: The Case for Retaining the Disinterestedness Requirement for Debtor in Possession's Professionals*, 18 MISS. COLL. L. REV. 291 (1998).

[33] Jerrold Nadler spearheaded opposition to the BRA in the House; Paul Wellstone and Edward Kennedy did so in the Senate. Each of the three have received thousands of dollars of campaign contributions from lawyers and lawyers are among the top two or three contributors to their campaigns. Kennedy alone received over one million dollars from lawyers and lobbyists in his last Senate election. *See* http://www.opensecrets.org. *See also* Zywicki, *Screwtape*, *supra* note, at 626 n. 68 (elaborating on financial contributions in the context of bankruptcy reform).

[34] *See* Zywicki, *Screwtape*, *supra* note, at 626 n.68.

Second, early on in the legislative process bankruptcy lawyers undermined their own credibility through a strategy of confrontation and confusion, rather than constructive participation in the reform process. Instead of offering constructive influence on the process, bankruptcy professionals instead launched a full-frontal assault against the BRA and its alleged political motivations. The purpose of the strategy apparently was to delay the BRA in the hopes of a Democratic takeover of Congress in the 1998 election cycle, which did not occur. Nonetheless, their aggressive rhetoric did stall reform, thereby emboldening the strategy. From that point on, bankruptcy professionals committed themselves to a slash-and-burn rhetorical and political strategy that quickly eroded support on Capitol Hill. False charges about the purported negative effect of the BRA on women, children, poor, and infirm successfully spawned confusion and delayed reform in the short-run, but in the long-run the strategy proved self-defeating. It soon became difficult to distinguish the bar's legitimate criticisms from posturing and obstructionism, and blatant factual errors coupled with a hard-edged rhetorical strategy eventually undermined the trustworthiness of bankruptcy professionals. In the end, this squandered the one traditional source of professional influence—their purported provision of nonpartisan technical advice to Congress.

Which raises the third group of interests in Skeel's trinity—creditors. Much has been said and written about the influence of creditors in lobbying for the BRA, and while most of it is overblown, there is in fact a kernal of truth in the fact that for the first time in recent memory creditors as a group have been able to overcome their collective action problems so as to prove an effective lobbying interest. In part this greater political organization reflects the greater incentives of creditors to do something in the face of millions of bankruptcy filings and the billions of dollars in discharged debts caused by them. As the benefits of action (or the costs to be averted) rise, parties will be willing to invest greater amounts to organize to capture those benefits. But more fundamentally, the greater ability of creditors to organize regarding the BRA reflects the fact that unlike previous reform efforts, the benefits of the BRA are spread across many different classes of creditors, thereby overcoming the intramural struggles that have crippled creditor efforts in the past. Unsecured creditors obtain such long-sought provisions such as means-testing eligibility of debtors for chapter 7 relief, creating a presumption for high-income debtors with substantial repayment capacity to file in chapter 13 instead of chapter 7, unless they can demonstrate significant hardship.[35] There are several new protections for secured creditors as well, such as rules limiting the cramdown of automobile loans and increased powers of mortgage creditors to respond to repeated bad-faith filings by debtors simply to stave off foreclosure. Even tax creditors were given new mechanisms for protecting their rights. Finally, marital support creditors receive several new protections that reduce the interference of bankruptcy with collection of alimony and child support obligations, as well as eliminating the incentives of debtors to file bankruptcy strategically to discharge certain marital obligations. Moreover, all creditors will benefit from reforms that increase debtor accountability by increasingly the honesty of debtors' schedules and limiting the ability of debtors to hide assets and understate income. As the fabric of the 1978 Code has become increasingly tattered and

[35] The rationale and mechanism of means-testing is described in detail in Edith H. Jones and Todd J. Zywicki, *It's Time for Means-Testing*, *supra* note, at 181-207.

debtors have become increasingly savvy about exploiting the loopholes in the Code, it has become possible for creditors to find common ground to lobby for reforms that benefit all classes of creditors. Traditionally political action by creditors has been frustrated by the zero-sum nature of bankruptcy—more money for secured creditors means less for unsecured creditors and vice-versa. Today, however, bankruptcy losses to all creditors are sufficiently large and widespread that all creditors have something to gain from reducing bankruptcy fraud and abuse, and as a result a coherent and stable coalition of creditors has been able to hold together for several years.

To be sure, creditors were actively involved in the legislative process of the BRA. But it is easy to overstate their influence. In a recent study, Stephen Nunez and Howard Rosenthal conclude that perhaps 15 of the 306 of the votes in the House in favor of the BRA in 2001 may have been swayed by campaign contributions from the consumer credit industry—about five percent of the House's 74% majority in favor of passage.[36] Indeed, although Nunez and Rosenthal examine only the number of votes influenced by creditor contributions, it is probably the case that these votes were at least to some extent canceled out by lobbying by bankruptcy professionals against reform. The modest effect of lobbying by creditors and lawyers suggests that positions on the BRA were driven largely by the ideological debate between "pro-debtor" and "personal responsibility" advocates, rather than political calculation. In this, the BRA can be distinguished from the reform process of the 1978 Code. In 1978, the debate focused primarily on reforms to the Chapter 11 process rather than on consumers. As a result, the debates were technocratic and interest-group driven, allowing bankruptcy professionals to claim an upper-hand in the process. By contrast, the core reforms in the BRA were driven by consumer bankruptcy issues, an area with heavy ideological overtones.

The three core influences that comprise the core of Skeel's analysis thus explain the success of the BRA, despite the efforts to derail it. First, an ideological shift in Congress following the 1994 elections created a new constituency for an ideology rooted in personal responsibility, which manifested itself in a concern over soaring personal bankruptcy filing rates during an era of unprecedented economic prosperity. This new ideological influence counterbalanced the traditional prodebtor ideology that historically had dominated ideological thinking about bankruptcy. Second, the interests of bankruptcy professionals was attenuated relative to prior eras. In part, this was because the new Republican majority was less responsive than Democrats were to the interests of lawyers. In addition, early on in the reform process bankruptcy professionals committed themselves to a crude and partisan rhetorical and political strategy that sacrificed the one source of influence that they were able to claim in the past, the provision of constructive technical advice. Third, creditors were able to overcome their traditional collective action problems and thereby patch together a set of reforms that would satisfy creditors from across the spectrum: secured, unsecured, marital support, and even government creditors. Thus a combination of factors congealed to create an environment rich for bankruptcy reform: a less debtor-oriented ideological environment, weakened influence by

[36] Stephen Nunez and Howard Rosenthal, "Bankruptcy 'Reform' in Congress: Creditors, Committees, Ideology, and Floor Voting in the Legislative Process" (working paper, Princeton University, January 18, 2002).

bankruptcy professionals, and strengthened influence by creditors. In this environment, therefore, the overwhelming and bipartisan support for bankruptcy reform in both houses of Congress was not surprising.

III. The Future of Bankruptcy Law

In the final chapters of the book Skeel turns to the future of bankruptcy, reviewing many of the current "hot topics" in bankruptcy law and policy, as well as offering predictions about the future of bankruptcy law, both domestically and internationally. Of particular interest is the impact of globalization on the future evolution of American bankruptcy law. Skeel concludes that globalization will have minimal impact on the structure of American bankruptcy law. "Although the new, world economy will have important effects," he writes, "the basic parameters of American bankruptcy law are unlikely to change. We will continue to see the same three forces—creditors, prodebtor ideology, and bankruptcy professionals—and the shape of the bankruptcy process will remain roughly the same." (p 241). In particular, Skeel observes, that despite the many criticisms of American bankruptcy law, under the pressures of globalization, bankruptcy law in much of the world is evolving to look *more* like the American bankruptcy system, rather than less. On both business bankruptcy and consumer bankruptcy, Skeel observes, the rest of the world is loosening its bankruptcy laws. Thus, even though they generally remain stricter than in the United States, the direction is clear—they are moving toward more generous bankruptcy laws. He writes, "The important point, however, is that all of the pressure unleashed by globalization is pushing in the this direction. All around the world, other nations are beginning to adopt some of the features of U.S. bankruptcy law. There is little evidence of a trend in any other direction, in the United States or elsewhere." (p. 243).

In general the world does seem to be moving toward more generous bankruptcy laws, but in the United States there is in fact clear evidence of a counter-trend as exemplified by the BRA. Not only does the BRA temper the prodebtor character of consumer bankruptcy, it also streamlines business bankruptcies to reduce the cost and delay of the Chapter 11 process. By contrast, there is no viable constituency for the adoption of the NBRC's prodebtor recommendations. In fact, as Chapter 11 has increasingly become a refuge for scandal-plagued companies, public opinion seems to be turning against Chapter 11. In addition, creditors are becoming increasingly ingenious in changing actual bankruptcy practice and devising non-legislative contractual and other "self-help" mechanisms for effectively opting-out of bankruptcy completely, or for devising mechanisms to minimize the expense, risk, and delay of being entangled in America's bankruptcy proceedings.[37] These legislative and practice attempts to reign-in the excesses of the American bankruptcy system manifest *de jure* and *de facto* trends toward a more restrictive bankruptcy regime in the United States.

The overall effect of globalization, therefore, probably will not be to create a uniform trend toward American-style bankruptcy systems. Rather, the likely result will be global *convergence* of bankruptcy regimes. Regimes that are excessively prodebtor, such as the United States, will tend to become less so; regimes that are insufficiently prodebtor, such as Europe, will tend to liberalize. The effect of globalization will be to establish a process of

[37] *See* John Armour, Brian R. Cheffins, and David A. Skeel, Jr., "Corporate Ownership Structure and the Evolution of Bankruptcy Law: Lessons from the UK" (working paper, August 2, 2002).

competition in economic policy that will tend to reward countries that adopt efficient economic policies and punish those that do not.[38] Within America's federalist system, competition among states has tended to produce convergence on efficient commercial and corporate law rules.[39] Given the free flow of capital around the world today, it is likely that such pressures will increasingly shape corporate governance rules around the world. Excessively prodebtor regimes such as the United States will be forced to temper their excesses in order to remain competitive in the global environment, whereas Europe and elsewhere will tend to liberalize in order to increase entrepreneurship and capital development in their moribund economies.

Globalization also probably will have the unanticipated effect of weakening the prodebtor ideology that has dominated American bankruptcy law during this century. Progressives defend Chapter 11 as a mechanisms for advancing social goals such as preservation of jobs and communities. This argument is questionable on its face, as inefficient Chapter 11 reorganizations save incumbent businesses and jobs, but only at the cost of reducing the availability of capital for new entrepreneurs and the creation of new jobs elsewhere in the economy.[40] More importantly, the attainment of these progressive policies is dependent on the willingness of private creditors to subsidize it. There is strong evidence that creditors increasingly are unwilling to bear this burden, and as a result are already trying to opt-out of the Chapter 11 system. Globalization amplifies this reluctance, producing pressures toward the adoption of efficient economic policies, whether tax, trade, securities, labor, or bankruptcy policies. In the past, creditors were forced to bear these costs of social engineering because of the difficulty of escaping the reach of national bankruptcy laws. To the extent that social benefits were provided, creditors may have been more willing to subsidize inefficient reorganizations when the beneficiaries were other Americans.

But in the modern world, capital is not tied to any particular country. Thus, it is far easier to escape the "tax" imposed by a nation's inefficient bankruptcy laws. It also is doubtful that international investors will be willing to allow American bankruptcy judges to redistribute their wealth to subsidize American workers and lawyers through Chapter 11. To the extent that Chapter 11 raises the costs and risks of investing in America, international investors will direct their capital to more efficient markets. In short, the pressures on the United States to adopt more efficient bankruptcy laws is much greater than in the past. As Chapter 11 hampers American competitiveness, policymakers will find it increasingly expensive to indulge the ideological desires of bankruptcy progressives, thus their influence should wane.

In the consumer bankruptcy arena, the BRA reflects a similar trend in the direction of greater restrictions on access to bankruptcy. American society is gradually reestablishing traditional values in the wake of what Francis Fukuyama has dubbed "the Great Disruption" of the past several decades.[41] Promiscuous consumer bankruptcy laws were just one of the many

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[38] *See* John O. McGinnis, *In Praise of the Efficiency of Decentralized Traditions and Their Preconditions*, 77 N.C. L. REV. 523 (1999).
[39] *See* Bruce H. Kobayashi and Larry E. Ribstein, *Evolution and Spontaneous Uniformity: Evidence from the Evolution of the Limited Liability Company*, 34 ECON. INQUIRY 464 (1996).
[40] *See* Zywicki, Book Review, *supra* note, at 373-74.
[41] FRANCIS FUKUYAMA, THE GREAT DISRUPTION: HUMAN NATURE AND THE RECONSTITUTION OF SOCIAL ORDER (1999).

social experiments of recent decades that have proven contrary to human nature and the needs of successful societies.[42] The movement toward greater accountability in consumer bankruptcy represents a necessary step of social self-correction after a period of chaos and revolution.

IV. Conclusion

David Skeel has written a brilliant and comprehensive book on the history of bankruptcy law in America. The use of cutting-edge analytical tools makes it possible for him to not only to persuasively explain the history of American bankruptcy law, but to offer insightful predictions about the future evolution of bankruptcy law in America. It is certainly the most important book on bankruptcy law that has been published since Thomas Jackson's acclaimed *The Logic and Limits of Bankruptcy*. Given the prominence of bankruptcy in today's business and political headlines, this is a book that should gain a wide audience among bankruptcy specialists and commercial and corporate law generalists alike.

[42] Zywicki, *Bankruptcy Law as Social Legislation*, *supra* note, at 430-31.