The Business Bankruptcy Project: The Work in Progress

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We feel like sculptors who have stopped work for a day to invite their patrons to view the work in progress. The Business Bankruptcy Project is in full swing, scanning case files, calling debtors, coding cases, and running endless repetitions of tables--the daily work of a large empirical study. We are pleased to report to the National Conference of Bankruptcy Judges on what we have found and to give some idea of the interesting lines we are currently pursuing, although with the understanding that we have to leave draped some of the loveliest parts, because they are not yet presentable. In this report, we provide preliminary findings from our survey of case files, our survey of debtors, and our survey of the judges themselves.

I. The Study

Three of us--Warren and Westbrook plus Dr. Teresa Sullivan, distinguished sociologist, as well as Vice-President and Graduate Dean of The University of Texas at Austin--received a substantial grant from the Educational Endowment of the National Conference of Bankruptcy Judges[2] to conduct an empirical study of business bankruptcy. Because so little information has

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[2]It would take a full volume to thank all the people and organizations who have helped with this project. We intend to offer those more detailed thanks in the publications to follow because they are too numerous to contain in a mere footnote. With a consciousness of inadequacy and injustice, we mention a few here. We begin with those who provided funding, the essential ingredient for empirical work: The Endowment for Education of the National Conference of Bankruptcy Judges has been the principal sponsor of the study; without their generous support, there would be no Business Bankruptcy Study. The National Bankruptcy Conference provided essential funds for specialized equipment. Significant portions of the study have also been funded by the Arthur Moller Research Chair in Bankruptcy and Commercial Law and the Cox and Smith Fellowship, both at The University of Texas, and by the Harvard Law School. We have a contract with the Small Business Administration covering certain parts of the study. Needless to say, none of these organizations, to which we are deeply grateful, is responsible for any of our conclusions or results.

The idea for this study did not originate with the principal researchers. Instead, we were urged, egged on, teased, and pushed into this study by three bankruptcy judges. The Honorable Samuel Bufford, the Honorable Lisa Fenning, and the Honorable Keith Lundin are separately and collectively responsible for the generation of the undertaking. Once the project was underway, nearly all the judges in the districts we studied were cooperative and helpful, and we offer them our deepest thanks. Various staff in the Administrative Office, notably those in the

been available about the business bankruptcy system, the study was intended to be wide-ranging rather than focused on narrow and specific hypotheses. It was also to be a longitudinal study, following cases over some five years. By using this approach, we hoped to have sufficient data both to discover unanticipated connections among various parts of the business bankruptcy system and to develop a comprehensive view of how the system works. We also hoped to create a foundation of data that would support research by other scholars by identifying potential sources of difficulty in sample selection and data gathering.

For this paper, we briefly summarize below the design of the study. A more complete description of the sampling and data-gathering methods used can be found in an article by our sociologist co-author.[3]

The two most important decisions that we made in designing the study were to study cases from all three general business chapters and to conduct a telephone survey of debtors as well as a survey of the case documents. At first, we, like some who had urged us to do the study, thought of this work as a Chapter 11 study, but as we analyzed the problem we realized that it was essential to study all three business chapters to understand any of them, much less the system as a whole. Chapter 7 liquidation is fundamental and--we keep telling our students--is the backdrop against which reorganization decisions are made. If we do not understand the operation and results in Chapter 7, how can we ask intelligible questions or make rational decisions about the rest?

By the same token, the statistics published by the Administrative Office of the United States courts (the "AO") suggested that more than half of all business reorganization cases were being filed in Chapter 13.[4] Although knowledgeable observers, including the AO, knew there

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Technology, Training and Support Division in San Antonio, were remarkably patient and generous with their time. The number of bankruptcy clerks and their staff who helped and bore with us during data collection is awesome and humbling. We offer our public thanks to each of them.

Our project has benefitted from the able leadership of two directors, Maria Vinall and Chip Trenckmann, skillfully assisted by Gretchen Zopatti. Patti Guiffre did a terrific job with the telephone survey work, as did Jennifer Frasier. Matthew Ploeger has done a superb job with the statistical and programming work. Without them, there would be no Business Bankruptcy Project.

[3]Teresa A. Sullivan, Methodological Realities: Social Science Methods and Business Reorganizations, 72 Wash. U. L. Q. 1291 (1994).

[4]In 1997, for example, the AO lists the number of business reorganizations in Chapter 11 as 9,694 and in Chapter 13 as 11,095. Business and Nonbusiness Bankruptcy Cases commenced, by chapter of the Bankruptcy Code, During the Twelve Month Period Ended December 31, 1997, Administrative Office of the United States Courts (1998).

were ambiguities lurking in the statistics, the importance of Chapter 13 in the overall business reorganization picture seemed clear. Thus, we concluded that no realistic business study could avoid looking at all three chapters.

We debated at length the wisdom of a telephone survey of debtors. We knew such surveys are very expensive and time consuming. We also knew that every earlier survey in the bankruptcy field had very low response rates, including surveys that were able to spend much more per person than we could.[5] We finally decided a survey was essential, despite all the difficulties and inadequacies to be anticipated, because it would make available information about the bankrupt businesses and their constituencies that could never be developed from the files.

It must be understood that a price is always paid for any decision to expand the database. To look at all three chapters meant we could not afford to ask and answer all the detailed questions about Chapter 11 that interest us and others. To do a telephone survey consumed substantial resources that could have been devoted to a larger case file survey or to gathering and coding the case data substantially faster. In the end, it was our judgment that those funding the study saw it as a baseline for work to come for many years in the future, so we opted for a broad and comprehensive approach.

We sampled 150 cases in each district chosen: 50 Chapter 7's, 50 Chapter 13's, and 50 Chapter 11's, drawing the cases evenly during four calendar quarters. To select cases without inappropriately skewing the process, we established a neutral selection criterion of the first twelve or thirteen cases filed[6] during each calendar quarter within a specific chapter within a district.[7]

Even with generous support from the NCBJ and others, a complete national sample was far beyond the available resources, so we started by sampling cases from two districts in each judicial circuit. The circuit approach gave us two advantages. Circuit-level rulings are a conceivable influence on the operation of the courts. Moreover, this design gave us a suitable

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[5]See Teresa A. Sullivan, Elizabeth Warren, and Jay L. Westbrook, Bankruptcy and the Family, 21 Marr. and Fam. R. 193, 196 (1995).

[6]In some high volume districts, one day's filings may exceed the number of cases needed for the sample for the quarter. In order to minimize any bias in the selection of such cases, we selected the sample randomly from the first filings among all the divisions in the district proportionately. In some low volume districts, by contrast, the thirteen week quarter would end before we had achieved our goal of 12 or 13 business cases in each chapter.

[7]If within the first twelve cases there was a case that was linked to a preceding case (for example, several partners who have filed serially), the second and all subsequent linked cases were ineligible for inclusion, so that the sample would not be dominated by the failure of a single business enterprise. We have collected data on related cases, but they are not part of this report.

geographic distribution of districts and also tended to represent equally the parts of the country that were experiencing good economic times and those that were not doing as well.

It seemed plausible there might be important differences between high filing and low filing districts. To capture that difference, we established, as our initial criteria, the selection of the district with the highest number of business filings and the district with the lowest number of business filings. Within a district, we sampled all the sites in order to capture the full range of variation in cases within the district.

We deviated from this general approach in a few respects. First, we took our sample from twenty-three districts, adding a third Ninth Circuit district.[8] Second, it was especially important to have sufficient Chapter 11 cases to conduct a statistically valid study, so we set ancillary criteria: for a district to be chosen, at least 50 Chapter 11 cases must have been filed during the twelve months ending in June, 1993 (the most recent time period for which we had filing statistics). Further, we wanted our sample to include a district with a self-identified fast-track case management system. The Eastern District of North Carolina was selected as the low-filing district from the Fourth Circuit, even though it would have ranked only third within that circuit as the low-filing district that fit our other criteria.[9] Because we emphasized the importance of a sufficient number of Chapter 11 cases in our selection criteria, we ended up with some districts that yielded fewer than 50 business Chapter 13 cases. Despite our projections from the preceding year, we still had two districts that produced fewer than 50 Chapter 7 or Chapter 11 filings.

The districts chosen because they had the highest business filings in their circuit were: Massachusetts, Southern District of New York, New Jersey, Maryland, Northern District of Texas, Eastern District of Michigan, Northern District of Illinois, Minnesota, Central District of California, Colorado, and the Middle District of Florida.

The districts chosen because they had the lowest business filing rate in 1993 in their circuit, but had at least 50 Chapter 11's, were: New Hampshire, Connecticut,[10] Delaware, Eastern District of North Carolina, Eastern District of Louisiana, Western District of Tennessee, Eastern

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[8]We added the Western District of Washington. The Ninth Circuit currently accounts for about one-third of the bankruptcies in the country, which argues for its greater inclusion in the district samples in order to better reflect the actual filings. In addition, because there is pending a proposal to create a new Twelfth Circuit, we wanted to have at least one district that would become part of the new Twelfth Circuit. Of the potential Twelfth Circuit districts, Western Washington would be the "high-filing" district.

[9]It would actually have been only fifth-best as a low-filing district, but two other low-filing jurisdictions were already disqualified as not having enough Chapter 11 cases.

[10]Connecticut, for example, was the second lowest filing district in the Second Circuit, but it was chosen because it had at least 50 Chapter 11's.

District of Wisconsin, Nebraska, Western District of Oklahoma, Hawaii, and Middle District of Georgia. These choices included some deviations from our basic model, generally because districts with low Chapter 11 filings often have even lower numbers of business Chapter 13 filings.[11]

In total, our twenty-three districts represented about 40% of all the business cases filed in the United States in the year ended September 30, 1993, according to the data provided by the Administrative Office of the U.S. Courts.

The criteria for determining a case to be a "business" bankruptcy have proven to be far more complicated than we anticipated. A study based on partial data from the Project has tended to show that we were correct in suspecting that the official designations might be imperfect.[12] Because of that concern, we developed independent criteria for defining a case as a business case. For purposes of this study, a case was considered a "business" bankruptcy if any of the following indicia was present: 1) the lawyer checked "business" in the business-nonbusiness box on the face sheet of the petition; 2) the petitioner's name had a business style (e.g., "Corp.," "Inc.," Co."); 3) the petitioner had a designation as "doing business as," of "formerly doing business as," or "also known as," if the latter designation was a business. We accepted a case that met any of the three criteria.

Thanks to outstanding and generous cooperation from the Administrative Office, especially the computer and training staff in San Antonio, along with a large number of dedicated computer specialists in clerks' offices, we were able to use PACER and BANCAP to locate cases using these criteria. On the other hand, the elaborate process required to be reasonably certain we were drawing business cases was very costly in time and money. It was an obstacle we had importantly underestimated. The cost of future studies would be dramatically reduced if a uniform and reliable system of properly designating business and consumer cases in the courts' computer existed. Such a system would also enhance the reliability of the business bankruptcy data currently reported.

The objective of these selection procedures was to minimize human judgment that might introduce bias into the sample and to make the sample as representative as possible across a broad range of variables.

II. **The Case Files**

Finding the Facts at the Courthouse

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[11]Insisting on a sufficient number of Chapter 13 business filings as well would have eliminated many low volume districts entirely and skewed the sample toward high volume districts generally. In light of some of the data reported below, one can debate whether we made the right choices.

[12]Jennifer Connors Frasier, Caught in a Cycle of Neglect: The Accuracy of Bankruptcy Statistics, 101 Comm. L. J. 307 (1996)[hereinafter "Frasier"].

Once we had drawn the sample, we proceeded to send hardworking contract staff around the United States copying almost 3,400 case files. Thanks to a generous grant from the National Bankruptcy Conference, the field staffers carried with them two Canofiles, computers that permitted the files to be scanned directly on to optical disks that could then be converted to computer-disk storage. This method was greatly superior to photocopying, although inevitably it involved its own logistical problems. As of the first quarter of 1998, we had scanned more than 3,300 cases and the work continues. Not only did we have excellent cooperation almost everywhere, but in some districts judges and clerks went above and beyond cooperation to provide essential assistance, including copying some cases for us. We are in their debt.

From these hundreds of thousands of pages, we are close to completing the first round of coding. Our staff coders read the scanned files on one computer and enter the coded data into a second computer based on forms and instructions in a standard coding form we have developed. We have begun a second round of copying at courthouses to pick up new additions to the bankruptcy files in open cases. This scanning process will continue throughout the next year.

For various technical reasons, different districts are in different stages of completion. We call a case "processed" when it is completely copied and coded in the first round[13] and is part of a group of cases reasonably verified for accuracy and completeness. For the case file section of this report, we use samples that vary in size from 14 to 18 districts (out of 23), depending on our confidence in the completeness and accuracy of the data concerning the particular variables involved in the analysis.[14] We will report soon on every district for the first round of copying and coding. Although we are reasonably confident that the major findings of this report will remain robust when the entire first-round sample is reported, later reports may differ because of the addition of districts and cases within districts.

The reader should note that our tables include "Ns," the number of cases in each reported analysis, and "Missing," the number of cases that do not include the variable reported, as well as the "Standard Deviation," a measure of the range of results within the cases analyzed.[15] These

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[13]Of course, some of these cases were still open when copied in the first round and some remain open.

[14]The districts in the 14 district sample are Central California, Connecticut, Delaware, Middle Florida, Middle Georgia, Hawaii, Northern Illinois, Eastern Louisiana, Massachusetts, Nebraska, New Jersey, New York Southern, Eastern North Carolina, and Northern Texas. For the 16 district sample, we add Eastern Michigan and Eastern Wisconsin. The 17 district sample adds Western Oklahoma.

[15]A Standard Deviation is the positive square root of the variance. The variance of a set of n sample measurements is the sum of the squared deviations of the measurements from the mean divided by (n-1). The standard deviation is frequently used to measure dispersion. In a normal distribution, 68% of the observations lie within +/- 1 standard deviation from the mean. Tai, Social Science Statistics: Its Elements and Application (1978) 83.

are key statistical indicators essential for later comparability of the data and for testing its internal consistency. Such data have been omitted from some highly publicized studies in our field, an approach we hope is never repeated. In most cases, "Missing" means that certain case files in the courthouse did not contain the type of information reported. For example, a surprising number of case files (more than 10%) did not contain complete schedules so that the information from those schedules can be listed only as "missing."

The Demographics of Bankruptcy

Because so little empirical work has been done in the business bankruptcy field,[16] the first and most fundamental task of the Business Bankruptcy Project is to provide a "demographic" picture of the businesses who file for bankruptcy. There are many different characteristics we might want to identify and relate to various policy issues. In this section, we offer a first look at some of the most basic characteristics of business bankrupts. We report on size, type of business, type of debtor (natural persons versus legal persons), and solvency. We also begin to explore how each of these characteristics correlates with each of the others--how, for example, size relates to type of business and to solvency. Along the way, we will discover some insights and some twists not previously apparent--or at least not previously demonstrable.

Size

The only multi-district empirical work on business bankruptcies in recent years examined public companies only. Because we already knew that many small businesses file for bankruptcy, even in Chapter 11, it was obvious that an examination of public companies, valuable as it was, would not provide a picture of the overall operation of the business bankruptcy system. Indeed, the availability of information about large companies while the rest of the system remains opaque exacerbates the tendency of policy makers to envision huge Chapter 11 cases when they make any careful consideration of bankruptcy reform.

Furthermore, these studies of public companies by definition did not include privately held companies, no matter how large. Because many of the largest companies in the United States are privately held, there was a substantial hole in the data even in the description of large businesses. One of the major purposes of the Business Bankruptcy Project was to examine

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[16]LoPucki and Whitford conducted an important empirical study, but it was limited to public companies. Lynn LoPucki & William Whitford, Bargaining Over Equity's Share in the Bankruptcy Reorganization of Large, Publicly Held Companies, 139 U. Pa. L. Rev. 125 (1990); Lynn LoPucki & William Whitford, Corporate Governance in the Bankruptcy Reorganization of Large, Publicly Held Companies, 141 Penn. L. Rev. 669, at 722 n. 184 (1993). The only other comprehensive study was done thirty years ago by Brookings. D. Stanley and M. Girth, Bankruptcy: Problem, Process, Reform (1971). For some of the other recent work in the field, see Elizabeth Warren & Jay L. Westbrook, Searching for Reorganization Realities, 72 Wash. U. L. Q. 1257, 1258, n.1 (1994).

business bankruptcy across the range of company size, from Tina's Tanning Salon & Tax Consulting, Inc. to Memorex.[17]

There are many different measures of a company's size. Typical ones are assets, debt, revenues, and number of employees. Before the Business Bankruptcy Project is finished, we expect to report size from a number of perspectives and to relate one size measurement to another. In this report, we focus on assets and debt as a way to rank businesses by size.

Assets

Tables 1 and 2 give a graphic representation of what property the debtors have when they come to the bankruptcy courthouse. Overall, more than half (51.5%) of the companies served by the bankruptcy system schedule less than $100,000 in assets at the time of filing.[18] Only 15% have more than $500,000 in total assets and about 10% have as much as $1 million of assets. Just as the great majority of businesses in the United States are small businesses, so are the great majority of businesses in bankruptcy. When the assets are added together for all the debtors, the mean (average) asset level is $840,868. But that number is inflated by the few cases with very large assets. The median (middle) asset level is a more modest $94,757.

Table 1: Total Assets of Bankrupt Businesses in 14 Districts, 1994.

Total Assets			Cumulative	
	Frequency	Percent	Frequency	Percent
Under $100,000	836	51.5%	836	51.5%
$100,000-500,000	533	32.8	1,369	84.3
$500,000-1,000,000	93	5.7	1,462	90.0
$1,000,000-5,000,000	109	6.7	1,571	96.7
$5,000,000 or More	53	3.3	1,624	100.0
Total	1,624	100.0		
Missing	227			

Source: Business Bankruptcy Study

[17]Both these businesses are in our sample. The tax and tanning salon is a true business name in our files, with just a slight change to maintain anonymity. Of course, the considerations that support anonymity for small businesses do not apply to the Memorexes of the world.

[18]Our figures are based upon the schedules filed by the debtors. Although the schedules are filed under penalty of perjury, debtors may overstate the value of the assets--or, perhaps, understate them. Although the schedules ask for fair market value, debtors may use book value, especially since balance sheets prepared by accountants often use cost less depreciation.

Table 2: Total Assets of Bankrupt Businesses in 14 Districts, 1994.

Total Assets

Mean	$840,868	25th Percentile	17,235
Standard Deviation	4,309,798	Median	94,757
Valid N	1,624	75th Percentile	254,196
Missing	227		

Source: Business Bankruptcy Study

Because our figures are based directly on the schedules that debtors are required to file under oath, they may well differ from those used in other studies that derive their data solely from the "face sheets" that a debtor's lawyer completes when a case is filed. We are also interested in the face sheet data and we report them in various ways, but unfortunately face-sheet data are subject to more types of error than the schedules themselves. Recent work with partial data from the Business Bankruptcy Project has shown that face-sheet data on assets and debts may be materially different from the data on the schedules in perhaps 30 percent of the Chapter 11 and Chapter 13 business cases.[19]

The diversity of sizes of businesses and the high proportion of small businesses is particularly evident among the Chapter 7 cases. The businesses that choose to file in Chapter 7 in the first instance are nearly all concentrated among the smallest businesses in bankruptcy. Only 5% of the businesses that file initially in Chapter 7 have assets greater than $500,000. Put another way, about 85% of the businesses with assets of $500,000 or more file first in Chapter 11.[20] For businesses over $1,000,000 in assets--which is not all that much nowadays--nine out of ten (93%) file in Chapter 11.

There are a number of implications that stem from the fact that almost all businesses of any significant size file first in Chapter 11, regardless of their financial or business circumstances. One important implication is that success rates in Chapter 11, however success is defined, may be very misleading. The data make it clear that most businesses of any size file in Chapter 11 even though some may not have a prayer of successfully reorganizing. The Chapter 11 failure rate may be deceptively inflated; if one considered the only those companies that stay in Chapter 11 and at the outset have some realistic chance of reorganization, the failure rate would be much lower. These data might support a contrary argument that Chapter 11 should have a greater gatekeeper function, at least for businesses larger than tiny, because too many companies file in Chapter 11 when an initial filing in Chapter 7 would lead to less expense and delay and a greater recovery for creditors. Yet a third lesson might be that Chapter 11 is not being abused as a reorganization device, but is simply being used far more often for the purpose

[19]See Frasier, supra note 12.

[20]Of these cases over $500,000 in assets, 12% file in Chapter 7 and 3.5% in Chapter 13.

of liquidation than has been realized or documented previously.[21] Not only do we intend to explore these issues more deeply as we proceed in the present study, but these data should provide the necessary starting point for more specific research on these questions in the future.

Chapter 13 figures are very different from Chapter 11. Almost half of the Chapter 13 business cases schedule less than $100,000 in assets and almost all are below $500,000. The lack of highest-end debtors is not surprising, given the debt limits in section 109(e), but the debt limits do not explain the concentration of cases with total assets under $100,000. By comparison, in Chapter 11, almost three-quarters of the cases exceed $100,000 in assets and more than 40% exceed $500,000. Indeed, 30% of the Chapter 11 cases involved more than $1 million in assets. As one would expect, the difference in asset size between the two business reorganization chapters is statistically significant.[22]

Debts

Only in bankruptcy would we consider measuring size by looking at a company's debts. In fact, this proposal to measure size has gained primacy, both in the policy debates and in Congress. Here we give the overall picture of the size of business bankrupts as measured by their total scheduled liabilities.[23] As with assets, we have taken these data directly from the schedules filed by the debtors and therefore they are likely to differ from data taken from the face sheets, which are subject to substantial errors.[24]

Tables 3 and 4 show the overall spread of cases throughout our fourteen district sample across all three chapters. Once again, influenced by the cases with the largest debts, the mean debt is $1,103,487, while the median debt is a much more modest $166,577.

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[21]The statute expressly authorizes the use of Chapter 11 for liquidation. Code section 1123(b)(4).

[22]For all purposes, we use the .05 level to test statistical significance. For these and other cross-tabs, we use a t-test. Here $p < .001$. We do not always report the results of these tests, unless the value is close to the cutoff.

[23]Except as otherwise noted, all figures in this section reflect total debt, secured and unsecured, of all types.

[24]See supra note 12.

Table 3: Total Liabilities of Bankrupt Businesses in 14 Districts, 1994.

Total Liabilities

Under $100,000	534	33.1%
$100,000-500,000	742	46.1
$500,000-1,000,000	128	7.9
$1,000,000-2,000,000	78	4.8
$2,000,000-4,000,000	52	3.2
$4,000,000-5,000,000	20	1.2
$5,000,000 or More	57	3.5
Total	1,611	99.8
Missing	240	

Source: Business Bankruptcy Project

Table 4: Total Liabilities of Bankrupt Businesses in 14 Districts, 1994.

Total Liabilities

Mean	$1,103,487
Standard Deviation	6,475,462
25th Percentile	75,069
Median	166,577
75th Percentile	412,438
Valid N	1,611
Missing	240

Source: Business Bankruptcy Study

If we think of the lower end of the scale in terms of debtors that are Very Small (debts under $100,000) and Small (debts over $100,000 but under $500,000), the data show that two-thirds of the cases are larger than very small, over $100,000 in debt. About 20% are larger than small, over $500,000 in total liabilities.

This provides an interesting picture of business debtors in bankruptcy as they are grouped by their debts. As Table 5 illustrates, about a third of all the debtors (33.1%) have debts less than $100,000. Nearly half of all the business debtors (46.2%) have debts between $100,000 and $500,000. And about a fifth (20.8%) have debts greater than $500,000. In the collective world of business bankruptcy, the divisions are in the half-million-and-under classes. In a relative sense, by the time debts exceed half a million, the case is already one of the "big" bankruptcies.

Table 5: Total Liabilities of Bankrupt Businesses in 14 Districts, 1994.

Total Liabilities

	Chapter			
	7	11	13	Total
Under $100,000	263	61	210	534
Column %	40.5	12.7	43.6	33.1
$100,000 or More	387	418	272	1,077
Column %	59.5	87.3	56.4	66.9
Total	650	479	482	1,611
Column %	100.0	100.0	100.0	100.0

$c^2 = 129$, $p < .001$.

	Chapter			
	7	11	13	Total
Under $500,000	570	231	475	1,276
Column %	87.7	48.2	98.5	79.2
$500,000 or More	80	248	7	335
Column %	12.3	51.8	1.5	20.8
Total	650	479	482	1,611
Column %	100.0	100.0	100.0	100.0

$c^2 = 417$, $p < .001$.

Source: Business Bankruptcy Study

Type of Business

The academic literature largely ignores questions of business type in considering the functioning of the bankruptcy system, as if all economic activity were fungible. Policymakers have the same tendency, with the notable exception of real estate cases, which are regularly given special treatment. We have taken a preliminary look at business type, beginning with a

strong suspicion that different types of businesses may present very different issues in bankruptcy.

Table 6 shows the relative proportions of various types of businesses overall and in each chapter of our sample of 14 districts.[25] If we look only at the data as reported on the face sheets, but eliminate the unresponsive categories ("other," "unspecified," and "missing") by far the most common type of bankrupt business is "retail/wholesale," at 37.4% of the specified types of businesses. The second most prominent is real estate (21.6%), followed closely by construction (17.3%). A substantial number of businesses, almost one in ten (9.0%) characterize themselves as "professional."

Table 6: Business Type of Bankrupt Businesses in 14 Districts.

Business Type	Frequency	Percent
Farming	17	2.3%
Professional	66	9.0
Retail/Wholesale	275	37.4
Railroad	1	.1
Transportation	40	5.4
Manufacturing/Mining	43	5.8
Stockbroker	1	.1
Commodity Broker	7	1.0
Construction	127	17.3
Real Estate	159	21.6
Total	736	100.0

Unspecified	579
Other	451
Missing	85

Source: Business Bankruptcy Project.

[25]These data are taken from the face sheets filed with each case and therefore are subject to the caveats mentioned earlier about face-sheet data. See supra note 12. More than one-third of the cases have marked "other" for business type on the face sheet. We are in the process of examining face-sheet data as to business type to determine its accuracy as compared to what is revealed by examining case files themselves. In addition, we hope that we can generate more particular categories from the large "other" designation (37%) in the face-sheet data, although many of the "other" cases lack useful descriptions in the files as well.

The representation of various types of businesses differs among chapters in statistically significant ways. Perhaps the most notable datum here is that manufacturing, often taken as the paradigm for a business case, makes up only 5.8% of the cases, even after dropping the "other" category. More than two-thirds of the manufacturing cases are filed in Chapter 11, so that manufacturers are a very small part of Chapters 7 and 13.

If we look at business type in Chapter 11 generally, we find that real estate and retail/wholesale dominate. Each of these categories represents about 20% of the total Chapter 11 cases and each is about one-third of Chapter 11 cases if we eliminate "other." So real estate and retail/wholesale cases between them represent about two-thirds of all specified Chapter 11 cases.

In Chapter 13, omitting "other," retail/wholesale sinks to 30% and real estate falls to 19%. Construction and professional are larger in Chapter 13, 23% and 10% respectively. Transportation, which includes everything from taxis to trucking companies, is three times higher than in Chapter 11, at 10%. Overall, there is a statistically significant difference in the types of businesses filing in each chapter.

In Chapter 7, retail/wholesale and construction are utterly dominant, at 46% and 23% respectively. Real estate cases represent only 10% of the cases filed initially for liquidation.

The Legal Entity

From various perspectives, including social policy, the distinction between the bankruptcy of natural persons and that of corporations is of special significance. For immediate purposes, we have divided business bankrupts into natural persons (both individual and joint filers) versus corporations, partnerships, and other legal persons. Our figures are apt to differ from those of other studies because, as discussed above, we did not rely on the clerks' characterization of a case as business or consumer. Because it seemed likely that the absence of national standards for business classifications would lead to inaccuracy in that regard, we applied an independent test to each case to determine if it was business or consumer.

As Table 7 illustrates, the corporate/individual status of the debtors in Chapter 7 and Chapter 11 are mirror images of each other. More than one quarter of the debtors (30.0%) who file initially in Chapter 7 are corporations, while under a quarter (28.1%) of the Chapter 11 debtors are not.[26] Of course, the surprising point may be that one in four of the Chapter 11 business debtors are natural persons. In fact, the situation is more surprising than that.

Table 7: Debtor Type by Chapter, Bankrupt Businesses in 14 Districts, 1994.

[26]Of course, by law only natural persons can file in Chapter 13, although we have 11 face sheets that claim otherwise! Code section 109(e).

Debtor Type

	Chapter 7	11	13	Total
Person	473	130	520	1,123
Column %	70.0	23.1	98.5	63.6
Corporation	203	432	8	643
Column %	30.0	76.9	1.5	36.4
Total	676	562	528	1,766
Column %	100.0	100.0	100.0	100.0

$c^2 = 687$, $p < .001$.

Source: See text.

Because we had anticipated that all Chapter 11 cases were likely candidates for the business bankruptcy sample, we captured the first Chapter 11 filings regardless of whether the case was styled "corporation" or similarly met the criteria for the business study. Later we reviewed these cases, planning to eliminate the few cases that were not consumer cases. We were surprised to find that we had picked up 155 Chapter 11s filed by consumers as we gathered the total Chapter 11 sample. Looking at a 16 district sample, as we can for this purpose, we find 131 consumer cases.[27] In those same districts, the sample selection yielded 478 processed Chapter 11 business cases, of which 142 were filed by natural persons. Thus 36% (273) of all the Chapter 11 cases--business and consumer--were filed by natural persons. This figure is utterly at variance with the structure of Chapter 11 in the Code[28] and with the exemplar that most commentators and policymakers have in mind when they discuss Chapter 11 reform.

These data suggest that a very substantial part of Chapter 11 is devoted to sorting out the problems of live human beings. As our earlier work suggested, business and consumer cases tend to overlap substantially in the case of small business owners, whether or not the business itself is incorporated. Thus, all of the 329 Chapter 11 cases filed by persons certainly include consumer debt. It is also likely, given marketplace trends, that much of the business debt has been incurred on a "consumer" basis--e.g., run up on credit cards not issued as business cards.

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[27]We use a 16-district sample here because we have sufficient processed cases for this purpose.

[28]For example, the courts have struggled with applying property of the estate concepts to an individual's earnings, in part because the drafters were not thinking of natural persons in the Chapter 11 context. E.g., In re Johnson, 178 B.R. 216 (9th Cir. BAP 1995)(ace driver's post-petition non-compete payments).

If our figures are representative of national trends, then in 1997, 2,424 of the 9,694 business reorganization cases filed in Chapter 11 were business-consumer cases filed by natural persons. When one adds the 11,095 business Chapter 13 cases,[29] it would mean that about 65% of all business reorganizations last year would have been of the combined variety filed by individuals.

On the other hand, our figures may not be representative. The number of consumer Chapter 11s varied greatly by district. Over half of them in our 16 district sample were concentrated in just three districts: New Jersey, Connecticut, and Massachusetts. Thus the filing of consumer 11s may be a function of local legal culture[30] or of very high real estate prices, although in the latter case we cannot explain why there would not have been more consumers in Chapter 11 in the Central District of California. It is also possible that some other localized phenomenon is at work.

It is possible that the debt caps in Chapter 13 drove many individual filers into Chapter 11 during the first 10 months of 1994, but that the 1994 amendments might have changed things. When we look at the entire sample, almost two-thirds of the consumer Chapter 11s would have fallen within the new Chapter 13 limits. Of course, we do not know if they failed to file in Chapter 13 solely because of the debt limits or for other reasons.

Solvency

One of the most interesting distinctions between U.S.-style bankruptcy and that found in most parts of the world is that we do not require a finding of insolvency as a condition for bankruptcy.[31] Thus it may not surprise some of our international neighbors to find that many debtors in bankruptcy (25% overall)[32] report themselves solvent, at least on a balance-sheet basis. For some who think waiving the insolvency requirement in the 1978 Code had no effect, however, this statistic might come as a surprise.

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[29]The AO figure may substantially understate the number of business Chapter 13s. See Frasier, supra note12.

[30]See Teresa A. Sullivan, Elizabeth Warren, and Jay L. Westbrook, The Persistence of Local Legal Culture, 17 Harv. J. L. & Pub. Pol. 801 (1994).

[31]A certain sort of insolvency test is applied for involuntary cases, Code section 303(h), but section 301 has no insolvency requirement for voluntary bankruptcies.

[32]All of the numbers and percentages relating to solvency are based on those cases that contained schedules for both debt and assets. Approximately 14% of the files were missing one or both schedules and the summary of schedules. We are in the process of trying to determine why schedules are not found in those cases--early dismissals, filing problems, or whatever.

To explore the relative solvency (or insolvency) of the debtors, we created an insolvency ratio(assets divided by debts) for each debtor. A debtor whose assets perfectly matched its debts would be solvent at 1.0--although just barely. A debtor with more assets, say $150 in assets for every $100 in debt, would have a higher ratio, 1.5 in this example. A debtor with fewer assets, say, $50 for each $100 in debt, would have a lower ratio, .5 in this example. As shown in Table 8, the mean insolvency ratio was just over 1.2 for 14 districts.

Table 8: Total Assets, Liabilities, and Insolvency Ratios, by Chapter, Bankrupt Businesses in 14 Districts, 1994.

Total Assets

	Chapter			
	7	11	13	Total
Mean	183,126	2,429,275	138,756	840,868
s.d.	1,472,423	7,463,632	132,665	4,309,798
25th %ile	4,200	87,503	44,349	17,235
Median	26,600	379,000	107,115	94,757
75th %ile	108,930	1,483,235	189,131	254,196
Valid N	661	485	478	1,624
Missing	38	114	75	227

Statistical Tests:	t value	
7 v 11	6.53	***
7 v 13	.77	
11 v 13	6.76	***

Total Liabilities

	Chapter			
	7	11	13	Total
Mean	468,006	2,925,501	149,791	1,103,487
s.d.	2,781,214	11,221,395	137,567	6,475,462
25th %ile	53,475	190,800	61,741	75,069
Median	133,070	534,400	116,871	166,577
75th %ile	275,657	1,874,055	206,588	412,438
Valid N	650	479	482	1,611
Missing	49	120	71	240

Statistical Tests:	t value	
7 v 11	4.69	***
7 v 13	2.91	**
11 v 13	5.41	***

Insolvency Ratio

	Chapter 7	11	13	Total
Mean	.741	1.966	1.165	1.229
s.d.	5.253	8.330	2.017	5.753
25th %ile	.057	.275	.520	.185
Median	.288	.711	.878	.583
75th %ile	.659	1.278	1.165	1.004
Valid N	644	469	476	1,589
Missing	55	130	77	262

Statistical Tests:	t value	
7 v 11	2.80	**
7 v 13	1.67	
11 v 13	2.02	*

* p < .05
** p < .01
*** p < .001

Source: Business Bankruptcy Study

It would strike many as unexpected that a sample of businesses in bankruptcy, including those in liquidation, would on average be solvent. Part of the answer is statistical in origin: there is a huge standard deviation, 5.753,[33] which suggests some very solvent companies may be pulling up the average for all the companies. That must be the case, because the median (middle) case in the sample is one with assets only 58% of liabilities (a ratio of .58). Nonetheless, these data document the fact that many companies in bankruptcy in the United States claim to be solvent when they file.

By Chapter

In Chapter 7 overall, less than 8% of the debtors claim solvency on the date they file their schedules, which does not seem surprising. As Table 9 demonstrates, even in Chapter 7 there are great variations in solvency from one case to another. The standard deviation in Chapter 7 is

[33]With a mean of 1.229, the range is -4.524 to 6.982, so that those at the top have $6,982 in assets for each $1,000 of debt!

even greater than it is overall and the mean is greatly increased by the effect of some solvent cases.

Table 9: Solvency by Chapter, Bankrupt Businesses in 14 Districts, 1994.

Solvency

	Chapter			
	7	11	13	Total
Insolvent	594	299	294	1,187
Column %	92.2	63.8	61.8	74.7
Solvent	50	170	182	402
Column %	7.8	36.2	38.2	25.3
Total	644	469	476	1,589
Column %	100.0	100.0	100.0	100.0

$c^2 = 177$, $p < .001$.

Source: Business Bankruptcy Study

On the other hand, more than a third of the business debtors in both Chapter 11 and Chapter 13 claim balance-sheet solvency when they file. These data are reported in more detail in Table 7. There is no statistically significant difference between these otherwise very different chapters as to the solvency of the debtors when they come to bankruptcy court.[34] Once again, that statistical result is affected by the much larger standard deviation in Chapter 11 and the uneven spread of the cases in that chapter. At the middle, the degree of insolvency in Chapter 11 and Chapter 13 is roughly comparable, but at the ends Chapter 11 is more extreme--producing a larger cohort of debtors that are very insolvent and a larger cohort of debtors that are more solvent than their counterparts in Chapter 13. This gives us a sense of the shape of solvency in each chapter, even if the statistical results remain murky.

Much of the variation as to solvency is explained by district-level variation. The level of solvency for bankruptcy cases is quite different from one district to another in our 14 district sample. Even in Chapter 7, solvency claims differ greatly by district and the difference is statistically significant. As shown in Table 10, 15% of debtors filing for liquidation in Delaware claim to be balance-sheet solvent, while only 2% make that claim in Massachusetts. There are variations between those extremes throughout the districts.

[34] Chi-square = 0.399.

Table 10: Solvency by District, Chapter 7, Bankrupt Businesses in 14 Districts, 1994.

District	Solvency		
	Insolvent	Solvent	Total
Central California	41	5	46
Row %	89.1	10.9	100.0
Connecticut	40	2	42
Row %	95.2	4.8	100.0
Delaware	34	6	40
Row %	85.0	15.0	100.0
Middle Florida	41	4	45
Row %	91.1	8.9	100.0
Middle Georgia	51	1	52
Row %	98.1	1.9	100.0
Hawaii	43	5	48
Row %	89.6	10.4	100.0
Northern Illinois	45	0	45
Row %	100.0	0.0	100.0
Eastern Louisiana	44	4	48
Row %	91.7	8.3	100.0
Massachusetts	46	1	47
Row %	97.9	2.1	100.0
Nebraska	48	1	49
Row %	98.0	2.0	100.0
New Jersey	41	5	46
Row %	89.1	10.9	100.0
Southern New York	45	2	47
Row %	95.7	4.3	100.0
Eastern North Carolina	44	2	46
Row %	95.7	4.3	100.0

Northern Texas	31	12	43
Row %	72.1	27.9	100.0
Total	594	50	644
Row %	92.2	7.8	100.0

$c^2 = 42$, $p < .001$.

Source: Business Bankruptcy Study

These local variations are also found in the two reorganization chapters. In fact, district-level variations in insolvency is statistically significant overall and in each chapter. Tables 8-10 show the percentage of solvent businesses by district in each reorganization chapter. For example, districts as distant and disparate as Los Angeles, New Orleans, and Honolulu show nearly 50% solvent Chapter 11 businesses, while in Connecticut, Nebraska, and New Jersey only about a quarter of the Chapter 11 businesses are claimed solvent. At least on paper, the differences in the financial condition of the business filers is extraordinary.

Table 11: Solvency by District, Chapter 11, Bankrupt Businesses in 14 Districts, 1994.

District

Solvency

	Insolvent	Solvent	Total
Central California	23	24	47
Row %	48.9	51.1	100.0
Connecticut	23	8	31
Row %	74.2	25.8	100.0
Delaware	17	7	24
Row %	70.8	29.2	100.0
Middle Florida	29	11	40
Row %	72.5	27.5	100.0
Middle Georgia	15	6	21
Row %	71.4	28.6	100.0
Hawaii	19	16	35
Row %	54.3	45.7	100.0
Northern Illinois	24	15	39
Row %	61.5	38.5	100.0
Eastern Louisiana	20	18	38
Row %	52.6	47.4	100.0
Massachusetts	27	12	39
Row %	69.2	30.8	100.0
Nebraska	9	3	12
Row %	75.0	25.0	100.0
New Jersey	32	9	41
Row %	78.0	22.0	100.0
Southern New York	28	12	40
Row %	70.0	30.0	100.0
Eastern North Carolina	13	17	30
Row %	43.3	56.7	100.0
Northern Texas	20	12	32
Row %	62.5	27.5	100.0
Total	299	170	469
Row %	63.8	36.2	100.0

$c^2 = 23$, $p < .05$.

Source: Business Bankruptcy Study

Table 12: Solvency by District, Chapter 13, Bankrupt Businesses in 14 Districts, 1994.

District

Solvency

	Insolvent	Solvent	Total
Central California	22	26	48
Row %	45.8	54.2	100.0
Connecticut	28	10	38
Row %	73.7	26.3	100.0
Delaware	7	1	8
Row %	87.5	12.5	100.0
Middle Florida	27	18	45
Row %	60.0	40.0	100.0
Middle Georgia	38	12	50
Row %	76.0	24.0	100.0
Hawaii	4	4	8
Row %	50.0	50.0	100.0
Northern Illinois	23	20	43
Row %	53.5	46.5	100.0
Eastern Louisiana	1	1	2
Row %	50.0	50.0	100.0
Massachusetts	33	14	47
Row %	70.2	29.8	100.0
Nebraska	28	3	31
Row %	90.3	9.7	100.0
New Jersey	27	15	42
Row %	64.3	35.7	100.0
Southern New York	14	22	36
Row %	38.9	61.1	100.0
Eastern North Carolina	20	13	33
Row %	60.6	39.4	100.0
Northern Texas	22	23	45
Row %	48.9	51.1	100.0
Total	294	182	476
Row %	61.8	38.2	100.0

$c^2 = 39$, $p < .001$.

Source: Business Bankruptcy Study

By Size

Assets

It is also instructive to look at solvency as a function of size. As a statistical matter, a debtor may have $100 in assets and owe $150 and be as statistically insolvent as a debtor who had $100,000,000 in assets and owed $150,000,000. We explored whether debtors with more assets were more likely to have proportionately more debt or less debt than their counterparts with less debt. In other words, was insolvency more likely in the bigger operations (at least as measured by assets and debt) or in the smaller ones.

The data show that the size of the business's assets is highly related to claimed solvency at both the $100,000 and $500,000 levels. For example, in the 14 district sample, dividing the Chapter 11 cases between those under $500,000 in total assets and those over, the data show that 55% of the Chapter 11 business in the higher group claim to be solvent, versus about 22% of those with less than $500,000 in assets. We found the same results in all three chapters: debtors with more assets were more likely to be solvent. We also ran correlations between size and solvency and found statistical significance at each level.

There has long been a theory that size was related to reorganization success, but generally people supposed that the reason was that larger businesses would present both a greater threat to various constituencies if they failed and they would have greater resources to support a rescue. It has not been suggested that size was important because it predicted solvency. It would seem intuitive that solvency would correlate with success in reorganization, but it is by no means obvious that bigger implies more solvent.

There are a number of possible explanations for this relationship. One might be that larger businesses file bankruptcy sooner, while they are more likely to be solvent, but there is no obvious reason that should be true. Perhaps they receive better legal advice or their financial consultants make them aware of bankruptcy long before they collapse. Of course, it is also possible that larger businesses claim to be solvent by overvaluing their assets more often than smaller businesses do, but neither intuition nor evidence supports that idea.

Debts

Puzzled by all this, we ran the numbers again, using liabilities as a measure of size. Dividing the cases at the same levels and several more, we found no statistically significant relationship between size as measured by debt and solvency or insolvency, despite the powerful relationship between solvency and size measured by assets. Of course, higher debts could mean greater insolvency, but that relationship is not borne out in the data. Perhaps the lack of relationship is a statistical quirk, but we intend to find out.

By Type of Business

Another way to look at solvency is to explore the relationship between the type of business filing for bankruptcy and its solvency. We were surprised at the results, shown in Table 13 for the 14 district sample.

Table 13:Solvency by Business Type, Bankrupt Businesses in 14 Districts.

Business Type

	Solvency		
	Insolvent	Solvent	Total
Farming	14	1	15
Row %	93.3	6.7	100.0
Professional	43	16	59
Row %	72.9	27.1	100.0
Retail/Wholesale	195	47	242
Row %	80.6	19.4	100.0
Transportation	23	10	33
Row %	69.7	30.3	100.0
Manufacturing/Mining	23	10	33
Row %	69.7	30.3	100.0
Stockbroker	0	1	1
Row %	0.0	100.0	100.0
Commodity Broker	3	4	7
Row %	42.9	57.1	100.0
Construction	86	26	112
Row %	76.8	23.2	100.0
Real Estate	61	58	119
Row %	51.3	48.7	100.0
Total	448	173	621
Row %	72.1	27.9	100.0

$c^2 = 45$, $p < .001$.
Source: Business Bankruptcy Study

Although there is no statistically significant difference in solvency among types of business in Chapters 7 and 13, there are such differences in Chapter 11. The biggest difference is with real estate cases, which are more often described as solvent. In our 14 district Chapter 7 cases, only about 9% of the cases were solvent, but 20% of the real estate cases were so listed, as were 17% of the manufacturing cases. Our first reaction was that the real estate debtors might be overvaluing the property, perhaps by using historic cost in a currently depressed market, but we were not sure there was a similar explanation for manufacturing. In any case, the differences are not statistically significant, although they seem substantial.

The big difference is in Chapter 11 cases, where another run showed that the sample as a whole contained 39% claimed-solvent cases, but real estate cases were listed as solvent 57% of the time. Transportation was next at 44% and no other type of business was close. The same explanations might be offered and might be more persuasive as to real estate in Chapter 11.[35] We hope that further exploration will reveal the answer.

By Type of Debtor

Given the relationship we had discovered between size of debtor and solvency, it seemed to us likely that there would be a connection between solvency and type of debtor, natural person or legal person. We were wrong. There was no statistically significant difference between the solvency rate in cases filed by natural persons and those filed by corporations and other legal persons. In both chapters in which legal persons can file--Chapter 7 and Chapter 11--there were about the same percentage of solvent natural persons as corporations.

The Policy Implications

Although the focus has been on consumer issues since the issuance of the report of the National Bankruptcy Review Commission, both the Commission's recommendations and the pending legislation address business cases as well. Two of the issues that have generated substantial controversy relate to size and business type of cases. One proposal would eliminate the current dollar limit on the special provisions governing single asset real estate cases ("SAREs"), making those provisions applicable to all SAREs. Another would impose special restrictions on small business cases, expanding on the provisions now in the Code for such cases.

Real Estate Cases

The Bankruptcy Commission endorsed two competing recommendations on single asset real estate cases. One proposal recommended that the present $4 million dollar debt cap on the SARE category be raised to $15 million.[36] The whole category came into effect just in the last quarter of the Project's study year, so we began our analysis by investigating how many real

[35]The percentages of types of business of solvent debtors in Chapter 13 were much less varied, with most of the categories near the mean of 36%.

[36]Report of the National Bankruptcy Review Commission, Recommendation 2.6.1, 2.6.1A (October 20, 1997). We necessarily ignore the effect of the recommendation that the substantive definition of a SARE be changed, because we do not have the data to include that change.

estate cases might have fallen within it under the $4 million cap.[37] We had sufficient data to use a 17 district sample for this analysis.

As Table 14 shows, about 28% of the Chapter 11 real estate cases would have exceeded the present SARE cap. The great majority of such cases therefore are already subject to the special SARE provisions. Another run shows that 93% of the real estate cases in our sample would have been subject to the SARE provisions with the $15 million cap recommended by the NBRC.

Table 14:Total Liabilities by Chapter,
Bankrupt Real Estate Businesses in 17 Districts.

Total Liabilities

	Chapter			
	7	11	13	Total
Under $4,000,000	24	61	22	107
Column %	96.0	71.8	100.0	81.1
$4,000,000 or More	1	24	0	25
Column %	4.0	28.2	0.0	18.9
Total	25	85	22	132
Column %	100.0	100.0	100.0	100.0

$fac^2 = 14$, $p < .01$.
Source: Business Bankruptcy Study

This is not to say that there would be no effect from raising the cap on SAREs. Instead, these data suggest that it would be possible to study the effects of the $4 million cap to determine what has happened in the large majority of SARE cases–perhaps as a prelude to proposals for any further changes in the law.

[37]We have not tried to identify cases that would qualify as SARE cases, aside from the dollar limitation on debt, by looking directly at the schedules of real estate assets versus other assets, a very complex and perhaps impossible task for the computer. We have not yet decided whether we will try to do it by hand. The data reported in the text reflects the debtor's identification of itself as a "real estate" debtor. Although some self-identified real estate debtors might not qualify as a SARE, aside from the dollar limitation, under the section 101(51B) definition, we think it is probable that the great majority would. Similarly, we may try to assess the impact of the SARE provisions in the last 2.5 months of our study year, but the effects may be too subtle, especially given the experience that such reforms often have a delayed effect.

Small Business Cases

A closely divided Bankruptcy Commission also recommended that small businesses be subject to special rules.[38] A small business was defined as one with secured and unsecured debt of $5 million or less. Again we ran a 17 district sample to see how many small businesses would be included with that cap. The results are listed in Table 15.

Table 15:Total Liabilities by Chapter, Bankrupt Small Businesses in 17 Districts.

Total Liabilities

	Chapter			
	7	11	13	Total
Under $5,000,000	24	67	22	113
Column %	96.0	78.8	100.0	85.6
$5,000,000 or More	1	18	0	25
Column %	4.0	21.2	0.0	18.9
Total	25	85	22	132
Column %	100.0	100.0	100.0	100.0

$c^2 = 9$, $p < .01$.
Source: Business Bankruptcy Study

We found that almost 80% of the Chapter 11 cases would be classified as small business cases under the Commission recommendation. The dominant Chapter 11 bankruptcy practice would be under the so-called "Small Business" rule, making today's Chapter 11 procedures and practices the "Big Business" exceptions to the de facto rule.

As the study progresses, we look forward to being able to apply more sophisticated and complex analysis to these and other policy proposals, but these two examples illustrate how empirical fact might inform--and perhaps surprise--those who propose changes in our bankruptcy laws.

III. Interviews with the Debtors

While the bankruptcy files contain an enormous amount of information about the debtors and creditors in the bankruptcy system, the picture one can paint with them is necessarily limited. The financial information is detailed, but there are other questions that the files don't

[38]NBRC Recommendation 2.5.1.

answer. Why is this business in bankruptcy? How many employees will be affected by this business' liquidation? What role does the IRS play in business failures? Do the objectives of businesses filing in Chapter 7 differ sharply from those in Chapter 11 or Chapter 13? What proportion of businesses are closed by the time they file? How long before bankruptcy did the problems start? This information remains outside the reach of those studying only the bankruptcy files.

Sometimes a file will contain information about the number of employees in a firm or the disputes that drove the business into bankruptcy, but such information is not regularly reported in each file. This means that the files are not a reliable source for a systematic study of such questions. In order to determine more about the debtors in the system, we developed a second database comprised of telephone interviews with bankrupt debtors.

The Survey Database

Once we had our sample of cases for the Business Bankruptcy Study, we set about trying to find each debtor and ask a series of questions about the company and its problems. Ultimately, we were able to complete interviews for 797 business debtors that filed during 1994. The debtors were divided among all three chapters, with 263 in Chapter 7, 302 in Chapter 11, and 232 in Chapter 13. The debtors represented all twenty-three districts in the study. The target time period for interviewing each debtor was approximately six months after filing, although the times varied based on how quickly we could draw the sample and whether we were able to reach the debtors.

Our initial contact with each debtor was by a letter from the Project Office describing the business bankruptcy study and explaining that we would call for an interview. We were at some pains to ensure that the letter would not be confused with junk mail. It was typed on university letterhead and stamped with a first-class commemorative stamp to attract the recipient's attention. The letter also offered the recipient the alternative of calling us or answering the questions by mail. We established a 1-800 number so that debtors could contact us at their convenience; this number was staffed a number of hours each day and night and had an answering machine for calls at other hours.

Unless the debtor contacted us to request a mail questionnaire or to make an appointment for a phone interview, we attempted to telephone each debtor. In order to complete an interview, we located the telephone number of the business and made up to ten attempts to reach the debtor by phone. If the contact person was willing, we scheduled a time to call the debtor for a telephone interview. Some debtors were willing to answer questions, but they preferred to respond in writing. In that case, we mailed a written form of the interview, which is attached in Appendix A.

We attempted to reach every debtor in the sample. The expectation that often appears in the literature, that there is little or no stigma attached to business bankruptcy, led us to believe that our response rates in this survey might be higher than those in which consumer debtors had been called and asked about their bankruptcies. This was not the case. We were able to complete surveys for almost exactly a quarter of the business debtors in our sample (24.8%).

This rate was about equal to the best any bankruptcy study has achieved.[39] Our low response rate was due to two factors: a high rate of non-location, and a high rate of refusal among those debtors whom we could contact.

The location of telephone numbers was one of our initial difficulties. For businesses that had already closed, there was often no phone number (and no forwarding address for our letter). We used several commercial tracing services, city directories, and Internet sources to try to identify home or office phone numbers for any debtors named in the petition. Sometimes these efforts were successful; in many cases, however, we finally had to contact the debtor's attorney in an effort to communicate with the debtor. Some attorneys passed our letters on to their clients, but others refused. We tried to work with trustees to reach the debtors, but most were unwilling or unable to help.

Once we contacted the debtors, many of them refused to talk with us. Others, however, were more than willing to talk. One large company had established a public relations office, complete with packets of information, for the purpose of describing its bankruptcy to the press. Our relatively low rate of contacting debtors, and their subsequent refusal to talk with us, parallels the findings of other researchers both in the United States and abroad. It seems that talking about bankruptcy is still a painful process for many debtors.

In the interviews, we asked a series of questions about the business and its history. The responses were recorded into an interactive computer database by the interviewer. This database incorporated skip-patterns to skip non-relevant questions. If, for example, a company was not publicly held, then the interviewer would see no further questions relative to shareholders on her screen. The software also provided pre-coded responses to many of the questions for which a small number of discrete answers were likely. Interviewers typed verbatim responses to open-ended questions, and these responses were later coded for analysis. In subsequent interviews, the interviewer was able to use the data from the initial interview to refer to the respondent's previous answers to questions and to avoid duplicating questions or asking non-relevant questions.

How Many People Are Affected by these Bankruptcies?

It is impossible to read the legislative history of the 1978 Code without noting Congress' keen awareness of how bankruptcy law may affect jobs and local communities. The looming failure of a huge business such as Chrysler in the late 1970s drove home the possibility that closing a business could put literally thousands of people out of work and destroy small communities throughout the country. As airlines, steel mills and retailers have filed for bankruptcy, the newspapers will periodically run stories about what it means to work, to draw health insurance, and to plan for a pension from a business that could literally disappear.

But most debates pay scant attention to the impact of bankruptcy law on employees. In larger companies, employees are rarely mentioned in the policy debates. In smaller companies, filings, either individually or collectively, are even less likely to raise questions about

[39] See supra, note 5.

employees. Notwithstanding Congress' traditionally sharp eye on the effects of bankruptcy policy on employment, academic discussions about how (and whether) to restructure businesses generally focus on a simplified model about the interests of debtors and creditors.

The interview data, documented in Table 16, offer an interesting mix of information. For about a third (about 36%) of the businesses in bankruptcy (all chapters combined) there are no employees. The owner/operator is the business. To be sure, that may not have always been the case. Many businesses have had more employees, but cut back the number by the time of filing. For a significant share of the businesses, these data show that, at least by the time of filing, bankruptcy is a matter of the owner/operator and family alone trying to deal with the operations and debts of a very small or now-defunct operation.

Table 16: Number of Employees of Businesses in Bankruptcy, 1997

# of employees/company	# of companies	percent
0	289	36.9
1	70	8.9
2	60	7.7
3	41	5.2
4	52	6.6
5	28	3.6
6	28	3.6
7	12	1.5
8	24	3.1
9	16	2.0
10	13	1.7
11	7	.9
12	15	1.9
13	5	.6
14	10	1.3
15	8	1.0
16	1	.1
17	4	.5
18	4	.5
19	3	.4
20	8	1.0
21	1	.1
22	3	.4
24	4	.5
25	3	.4
26	1	.1
28	2	.3

29	2	.3
30	5	.6
35	5	.6
37	1	.1
38	2	.3
39	1	.1
40	5	.6
44	1	.1
45	2	.3
48	1	.1
49	2	.3
50	3	.4
51	2	.3
52	2	.3
65	2	.3
70	4	.5
72	1	.1
85	2	.3
87	1	.1
90	1	.1
100	1	.1
104	1	.1
119	1	.1
120	1	.1
125	1	.1
140	1	.1
150	2	.3
155	1	.1
175	1	.1
180	1	.1
183	1	.1
218	1	.1
299	1	.1
400	1	.1
450	1	.1
499	1	.1
500	1	.1
900	1	.1
1500	1	.1
2500	1	.1

3000	1	.1
5200	1	.1
10000	1	.1
23000	1	.1

Mean	70.347	25th Percentile	.000
Std dev	926.918	Median	2.000
Sum	55082.000	75th Percentile	8.000

Valid cases (n) 783 Missing cases 14 .

Source: See text

For the remaining two-thirds of the businesses, however, employment is a very significant part of the picture. In a random sample of 783 cases in which we received a response to a question about employees, there were a total of 55,082 employees. If our sample is representative of all the business bankruptcies (which is the subject of another paper), a very rough and preliminary approximation would suggest that about two million people were currently working for businesses as they filed for bankruptcy during 1997.[40] Or, to put it another

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[40]It is possible to make this estimate using two different statistical models. Beginning with these data from the AO:

1997 total business filings	54,027
1997 Ch 7 business filings	32,255
1997 Ch 11 business filings	9,694
1997 Ch 12 business filings	949
1997 Ch 13 business filings	11,095

METHOD 1: GENERALIZING FROM THE MEAN

Here are the mean number of employees for the chapters for which we collected data (which treats all Chapter 12 cases as having no employees):
Chapter 7: 7.931 (N=261)
Chapter 11: 174.866 (N=298)
Chapter 13: 4.027 (N=224)
Total: 70.347 (N=783)

So, if, on average, each business in chapter 7 had 7.931 employees, and

way, even in these boom times, about twice as many people went into bankruptcy last year as the employees of businesses that filed than went into bankruptcy by filing themselves.

If, for the purposes of more detailed analysis, we eliminate the third of the businesses that have no employees at the time of filing, there would be an average of about 112 employees for each business case in bankruptcy. More information on the businesses with one or more employees is identified in Table 17.

Table 17:Number of Businesses in Bankruptcy with 1 or more employees, 1997

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there were 32,255 businesses in chapter 7, 255,814 (i.e., 7.931 X 32,255) people were employed by businesses that filed chapter 7.

Chapter 7: 7.931 X 32,255 = 255,814 employees
Chapter 11: 174.866 X 9,694 = 1,695,151 employees
Chapter 13: 4.027 X 11,095 = 44,680 employees
- -
Total: 1,995,645 employees

METHOD 2: WEIGHTING

Here are the total number of employees for the chapters in the sample (again setting the number of employees in Chapter 12 at zero):

Chapter 7: 2,070 (N=261)
Chapter 11: 52,110 (N=298)
Chapter 13: 902 (N=224)
Total: 55,082 (N=783)

Chapter 7: 32,255/261 = 123.58238 (weight)
123.58238 X 2,070 (total employees) = 255,816
Chapter 11: 9,694/298 = 32.530201
32.530201 X 52,110 = 1,695,149
Chapter 13: 11,095/224 = 49.53125
49.53125 X 902 = 44,677

Ch 7: 255,816 employees
Ch 11: 1,695,149 employees
Ch 13: 44,677 employees

Total: 1,995,642 employees

(By Chapter)

	Chapter 7	Chapter 11	Chapter 13	Total
Total Employees				
Mean	14.48	227.55	7.39	111.5
Std. Deviation	38.96	1706.03	18.13	1165.43
25th Percentile	2.0	4.0	2.0	2.0
Median	4.0	9.0	4.0	5.0
75th Percentile	8.0	24.0	7.0	13.0
Sum	2070	52110	902	55082
Valid n	143	229	122	494

Source: Business Bankruptcy Study

But aggregated data can hide a wealth of important detail. At one end of the spectrum are the one-third of the businesses that have no employees. At the other end is one business with 10,000 employees and another with 23,000 employees at the time of filing.

Just as the businesses with lots of assets end up in Chapter 11, whether they have good business prospects or not, the businesses with lots of employees also end up in Chapter 11. There were eleven businesses in the sample with 300 or more employees. Every one of those businesses was in Chapter 11. Altogether, the Chapter 11 cases in the sample represented 52,110 employees. This is about 95% of all the employees working for companies that filed for bankruptcy.

At the same time, Chapter 7 and Chapter 13 cannot be dismissed as irrelevant to employment issues. The 261 companies in the sample that initially filed in Chapter 7 collectively employed 2,070 people. Again, we can eliminate those Chapter 7 businesses that employed no one (about 45% of the Chapter 7 sample). In that case, the remaining Chapter 7 businesses employ an average of 14.5 workers for each business that files.

The Chapter 13 cases involved the fewest employees. The 224 cases in Chapter 13 collectively employed 902 people. Again, if we eliminate the cases in which the Chapter 13 debtor employed no one, the average per case was about 7 workers for each business that filed.

We are just beginning to explore the linking of these data with the data from the case files, including size and type of business and the relationship of both to chapter and other variables. The process of doing so is large, technical, and daunting, but we are looking forward to it.

Employment, as Congress has understood instinctively for many years, is a significant event in the bankruptcy system. These data show how significant. They also show that employees are involved in bankruptcies of all size and in all chapters.

The Policy Implications

Two million employees listed in the 1997 business bankruptcies makes a strong argument for cautious reflection on any change in the laws that make liquidation of a business more likely.

In some sense, the employees are only the most visible tip of the iceberg of casualties when a company fails. Many of these companies may have followed the outsourcing trend that reduces the number of direct employees, but not the number of individuals and families that rely on the business. Moreover, the community effects--effects on other suppliers, taxing authorities, other jobs in the community--of bankruptcy may be only indirectly represented by the data on employees.

These data may also raise questions about whether the division in treatment of businesses should not be along dollar lines, but should instead be based on other criteria that may encompass whether the debtor provides jobs in the local community. While no economy can prosper if inefficient businesses are eternally subsidized, the presence of so many employees in bankrupt companies is a powerful reminder of the collateral consequences of any business failure.

The documentation about the presence of many employees in bankrupt businesses should add another dimension to all the bankruptcy debates.

Why Bankruptcy?

Bankruptcy is a solution to a problem. The debtor, or very occasionally the creditor, chooses bankruptcy as a way to fix something that the filer perceives as broken. But there is no consensus about what the problem is that bankruptcy is supposed to fix. Without a clearer vision of the problem (or problems), it is difficult to evaluate the effectiveness of bankruptcy as a tool to accomplish these ends or the legitimacy of the ends themselves.

In the phone surveys we asked the debtors why they filed for bankruptcy. What went wrong that they ended up in the bankruptcy courthouse? Of course, judges and lawyers have heard all of the reasons we heard and more. But we counted them. The result is the first report for many years systematically reporting the debtors' explanations for why their businesses went into bankruptcy.

We asked the debtors for their view of what went wrong, recognizing that they might not give an objectively correct answer of what was actually wrong. It is possible that an outside analyst would disagree with the honest, but mistaken, reason given by the debtor. For example, a debtor might describe a cash flow problem, while an independent analyst might see the trouble as a crooked employee or an ill-considered investment decision. We do not pretend to establish an omniscient view of the problems that lead to bankruptcy. All we have are the debtors' own explanations, which we offer as the view of the party who generally initiates the bankruptcy filing.

Once we asked, the reasons for bankruptcy tumbled out. The 781 debtors[41] gave a total of 1,461 responses. All the debtors listed here gave at least one reason. More than half the debtors (58%) identified at least two reasons, and about a quarter (22%) gave three reasons. A few even gave four or five. Because of the multiple responses, the percentages in Figure 1 add to more than 100%.

The question was open-ended, with no clues or multiple choice responses. The debtors were free to say whatever they wanted, and we tried to write down as faithfully as possible the response the debtors gave. Altogether, we coded 65 discrete types of answers, ranging from union problems to drug problems. The list of reasons is replicated in Appendix A.

With 65 categories of responses, we had lots of information, but not much of an overall picture of what was going on. We decided to re-group the answers, collecting them into related reasons. We developed eight groupings:

•Business operations: This grouping included factors such as the debtor's admitted mismanagement of the business, a decline in production, a bad location, the loss of major clients, and the inability to collect accounts receivable.

•Financing: This grouping included identification of the financial structure of the business, such as high debt service, loss of financing, or the inability to get financing.

•Outside business conditions: This grouping included factors such as new competition, increases in rent, insurance or other costs of doing business, declining real estate values, declining farm prices, and the like.

•Tax: This grouping included problems with the IRS, or state or local taxing officials.

•Calamities: This grouping included fraud or theft by an outsider, natural disasters, industrial accidents, and restricted access to the business, such as road work.

•Disputes with a particular creditor: This grouping included a number of different problems with a specified creditor, sometimes in different states of resolution at the time of filing, including foreclosures, lawsuits, contract disputes, failed negotiations, trouble with the FDIC, and simply, as some debtors put it, "a problem with one creditor." Some of the disputes are collection disputes, but many are about underlying disagreements over who owes what obligations to whom.

•Other: Here we have everything that was left, including buying time, trying to sell the business, and involuntary petitions.

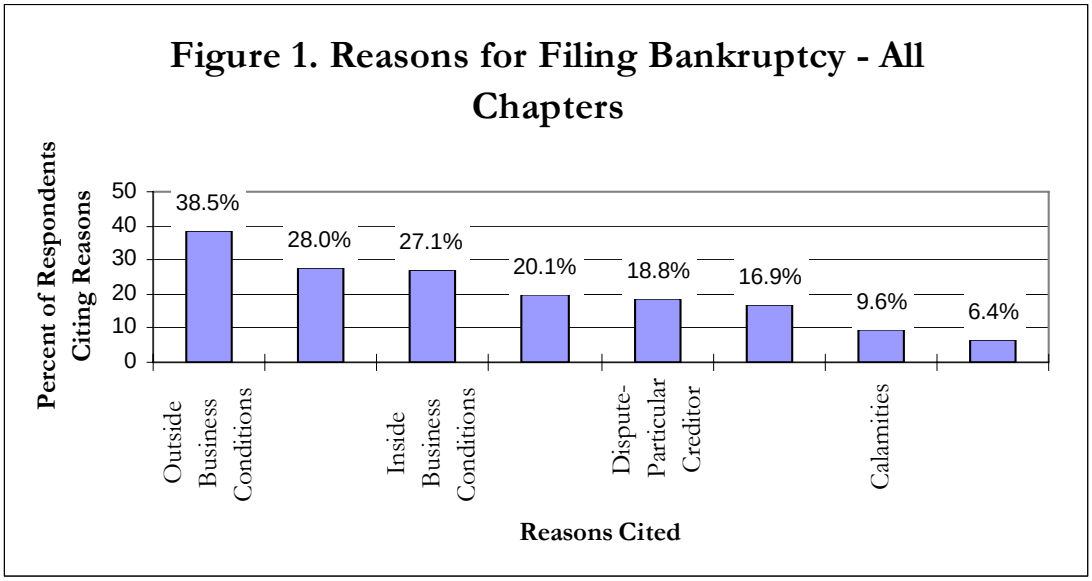
The groupings are not perfect. Some of the debtors' responses are ambiguous, and some could overlap one or more categories. A theft by an employee could reasonably be called a part of ongoing business operations (or operations that failed to supervise employees) or a calamity (an bad event that strikes without warning); we chose the latter, but we could see that others might

[41]Sixteen debtors either did not talk long enough for us to ask the question or could not give any response to the question. The 16 debtors who gave no response of any kind to this question here are excluded from the analysis.

make a different classification. But the ambiguous responses were relatively uncommon, so that shifts in classification would make only slight differences in the groupings. As such, the groupings give a fairly reliable measure of what the debtor characterizes as the problem that brought the business to the bankruptcy court. (See Appendix B)

Business Reasons

The debtors' responses are illustrated in Figure 1. The most obvious point of this graph is that a collection of business reasons dominate the business filings. The three most frequently listed reasons are those having to do with the external business climate generally (38.5%), those having to do with the financial structure of the business (28.0%), and those related to the operations of the business (27.1%). In fact, about seven out of ten (72.6%) of all businesses in bankruptcy cite at least one of these three business-oriented reasons.



In one sense, this is an expected finding. When businesses fail at business, they file for bankruptcy. In terms of startling responses, this is right up there with our finding ten years ago in our consumer studies that most of the people who file for bankruptcy are in financial trouble. The finding has at least some significance however; it demonstrates that, at least in some sense, the system seems to work the way it is supposed to work. Businesses choose bankruptcy to solve business problems.

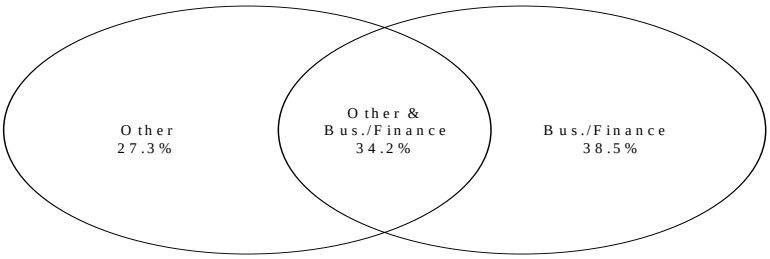
It is possible, of course, that every debtor gives only a self-serving answer and tries to dress up the responses with "business-like" answers, but most of the responses here are fairly specific. Debtors discuss their reduced factory output, the maturity of a balloon note they could not pay, or the "realization that the market for large printing machines had dried up." Whether

they are objectively right or not, they have certainly identified a number of individual business problems that they believe caused their businesses to fail.

But like so much of our data, the half-empty/half-full quality of what it shows is the most interesting. Not all the debtors blamed their trip to the bankruptcy courts solely on a business problem as such. About half of the debtors who identified a business/economy reason also identified another reason that was not tied to the economy generally or to the operations of the business. For these debtors, various personal problems and calamities prompted their business failures. For some, it was trouble with a particular creditor or pressure from the IRS that pushed them into bankruptcy. In fact, as Figure 2 demonstrates, the debtors divide into three roughly equal groups--those that identify only business/economic problems, those that identify only non-business problems (other), and those that identify both kinds of problems. The division is a reminder that business debtors come to bankruptcy to do more than deal with general business problems.

Figure 2

Reasons for Business Bankruptcy Filing



Source: Business Bankruptcy Study

Tax Troubles

As Figure 1 shows, the fourth most frequent single response was a problem with the taxing authorities. One in every five businesses in bankruptcy identifies a problem with the IRS or a state or local taxing agency as the reason for its filing. A few debtors mentioned state and local taxing authorities: 5% mentioned the state, while .4% mentioned local taxing problems. The overwhelming response of the debtors, however, was trouble with the IRS. Just over one in five failed businesses (20.1% of the total sample) specifically identify the IRS by name as the source of their troubles and the reason they ended up in the bankruptcy court.

Comments recorded from the debtors give some idea of the relationship between bankruptcy and the IRS:

IRS stepped in and took over their bank account.

The IRS threatened to repossess [our] tools of trade if [we] did not pay the $20,000 back taxes immediately.

Pressure from IRS. The IRS is "merciless".

When the IRS agent told us that they will put padlock on our doors if we can't come up with the money in one month.

IRS was attempting to reach the non-debtor wife's income (i.e., levy) for the tax liabilities, which all preceded her marriage to the debtor.

The IRS changed the locks on the business, and the business had to declare bankruptcy in order for the owners to be able to even get into their building.

Not everyone described the IRS in an entirely hostile manner. A number of debtors indicated that IRS agents told them either directly or indirectly that if the debtors would file for bankruptcy, the IRS agents would have greater leeway in negotiating a repayment arrangement.

Legal Disputes

The data also confirm the contentious nature of debtor-creditor practice. Nearly one in five debtors (18.8%) identify a problem with a specific creditor as the reason for filing bankruptcy. (See Figure 1) Like most of the responses about the IRS, the responses here were also often heated. The debtor would not be in bankruptcy if only the customer/ bank /mortgage company/landlord/ supplier/franchiser/abutter were not such a jerk. The debtors often described what they believed were viable businesses, sometimes even highly profitable businesses, brought low by a dispute over a contract or other obligation.

Within the dispute category are a number of disputes that had already escalated to the formal legal action. For more than one in ten of the debtors in the sample (11.4%), the reason given for the bankruptcy filing was to deal with a pending legal action--a lawsuit, a foreclosure, an eviction or some other action in court. By the time they file for bankruptcy, a significant portion of the business debtors are no strangers either to courts or lawyers.

Personal Profiles

The business/personal distinction in bankruptcy is one that seems to drive a great deal of the organizational structure of the profession. Conferences, law school courses, and practitioner identification clearly distinguish “business bankruptcy” from “consumer bankruptcy.” But in a sample of nothing but business bankruptcies, the number of personal problems that drive these

filings is significant. About three out of every twenty (16.9%) so-called business bankruptcies are initiated because of a personal problem of the business owner (See Figure 1).

Again, the comments of the debtors give some flavor of the kinds of problems that they see as causing the bankruptcy filings for their business:

Bank was not going to refinance her business because of divorce settlement.

Inability to control blood glucose level, cholesterol, etc. due to stress of dealing of creditors.

His wife had a nervous breakdown. He just knew they couldn't handle their bills.

The injury to his arm

She could not pay her medical bills. She filed bankruptcy as soon as she couldn't pay her bills, rather than get behind in payment.

Creditors were hounding him to pay his wife's credit card (he had not canceled the cards after the divorce. He returned his but never closed his account). Started summons from sheriff.

I had lost court case in trying to settle child support but lost. Was given 48 hours to settle $36,000 of debt which was impossible.

The explanations of these debtors are a reminder that despite the legal device of the independent business, many companies remain dependent on the financial stability of their owners and operators. Divorce and medical problems of key people may affect the financial survival of the business.

Calamities

For just under one in ten of the debtors (9.6%), the problem may not be personal, but it is the kind of calamity for which businesses have a hard time planning. (See Figure 1) Again, the debtors give the best explanations:

One of the trucks he owned the engine blew in it and they couldn't afford to buy another one.

His van was stolen and he could no longer transport the equipment necessary to carry on his business.

The organization they were linked with sold out and was taken over by another organization that was hard to work with.

The gas explosion.

Death of foreman.

The State came in and tore up the road.

Some of these problems, such as the inability to repair the truck, reflect the incredibly thin margins on which some businesses operate. Others, such as the death of the foreman, show how some operations may rely on a key person--and not necessarily the owner. But others, such as the gas explosion, show that even a large and prosperous business can be just one big dose of bad luck away from a bankruptcy filing.

There are also statistically significant variations among chapters as to the reasons given. As the study progresses, we look forward to developing all of these data in relationship to the size and type of businesses filing in each chapter and various other variables as well. We suspect we will see some intriguing relationships.

The Policy Implications

The range of responses is broad, and there are others to be explored in greater detail. But even these preliminary responses illuminate some key points:

•Most businesses in bankruptcy are struggling with operational and financial problems

•The IRS is a big player in pushing debtors to file for bankruptcy

•A significant proportion of business bankruptcies stem from personal problems

It is too early to draw policy conclusions from these early views of the data, but these three observations raise a number of important questions. For example, the fact that more than seven in ten of all bankruptcies are described as business problems raises these questions: Do businesses in bankruptcy receive adequate help in dealing with their business problems? Is it reasonable to expect that these businesses will reorganize or even liquidate efficiently if their managers are already describing business and finance problems they have been unable to solve? Should debtor screening and plan confirmation involve more formalized reference to parties with established business expertise?

Conversely, the fact that more than three in twenty business filings deals with a personal problem should prompt questions in the opposite direction: Is the business bankruptcy system too cumbersome for the resolution of what is essentially a consumer debtor problem but which must be handled as a business filing because of the debtor's intertwined business and consumer legal affairs? To what extent is Chapter 7 a reorganization chapter when the debtor plans to protect the business by discharging consumer debt? Is a different legal structure for personal/business bankruptcies needed?

The large number of comments about the IRS raises other questions. Does the IRS follow collection policies that drive debtors into bankruptcy? Would different approaches cut the costs of debt collection for the IRS and for all other creditors as well? Should the treatment

of the IRS in bankruptcy be different to discourage debtors from using bankruptcy as a way to deal with the IRS?

As we develop these data more fully, the policy implications are likely to multiply.

IV. The Judges' Survey

In order to understand better who uses the businesses bankruptcy system, we talked with the debtors and examined the information in their files. But to understand what happened to those businesses while they were in the system we realized that we also needed information about the most important repeat players in bankruptcy--the judges.

Our original survey design had included only an examination of cases and interviews of debtors. In 1995, however, we decided to expand the reach of the study by learning more about the bankruptcy judges. We developed a questionnaire to explore the judges' attitudes toward case management. We also gathered information about the judges. These data are useful to tell us about who sits on the bench and how their views differ from district to district, filling in yet another perspective about the bankruptcy system.

For this part of the project we were very fortunate to work with two very able law students, Stacey Kleiner Humphries, Harvard Law School Class of 1996, and Robert L. R. Munden, University of Texas Law School Class of 1996. As part of their senior thesis at their respective schools, they worked with us to perfect the questionnaire for the judges, distribute the questionnaire, and collect and code the responses. Their own analysis of the data is now published in Painting a Self-Portrait: A Look at the Composition and Style of the Bankruptcy Bench.[42] Ms. Humphries' and Mr. Munden's work on this project was outstanding.[43] With their help, we have been able to create a third database that we can connect with our first two databases, thereby expanding the reach and implications of the Business Bankruptcy Study.

In this section, we present some different data from a somewhat different perspective than their original approach to the data. Among other things, we have collapsed some response categories and performed some correlations to focus on the relationships among the judges' perceptions of how they manage their cases.

For this section, we use the responses of all the judges around the country, not just those in the 23 sample districts. We note, however, that for each variable tested, there is no statistically significant difference between the judges in the 23 sample districts and the judges in the non-sample districts.

The Survey Database

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[42] 14 Bankr. Dev. J. 73 (1997).

[43] We believe that this was the first joint student empirical project between law schools. As part of our ongoing effort to drag law schools into empirical research, we are especially pleased with the results of their work.

We developed a questionnaire to learn more about different judicial approaches to business bankruptcy cases. Thanks to former judge Roger Whalen of Washington, D.C., we were able to pre-test the questionnaire on a group of retired bankruptcy judges. The survey questions were much improved as a result.

The questionnaire was comprised of six questions intended to enable judges to describe their professional managerial style. Recognizing that individual cases may require differing management styles, judges were asked to describe their general approach to administration in business bankruptcy cases as a whole. The first four questions of the questionnaire were intended to investigate four different aspects of managerial judging. We hoped that judges' responses to those four questions together would provide an overall image of a judge's managerial style.[44] The fifth question utilized the same approach as the first four, but dealt only with adversary proceedings or contested matters.[45] We hoped that a comparison of the judge's style in the first four questions might reveal whether judges seek more control in adversary proceedings than in non-contested matters. Finally, the sixth question asked the judges to pick one of four descriptions of four judging styles that best matched their own. The choices--fast track case managers, active case managers, discretionary case managers, and judicial dispute resolvers--gave another perspective and overall self-assessment from the judges.[46] A copy of the questionnaire is in Appendix C.

We mailed a questionnaire entitled "Judging Styles Inventory" to all of the active bankruptcy judges listed with the Administrative Office of the Courts in October, 1995.[47] In February, 1996, we conducted a second mailing of the survey to the judges who had not yet responded in an effort to generate responses from them.[48] To protect the confidentiality of respondents, each questionnaire contained a code number linked to the name and district of each judge. The results of the survey are published in statistical summaries in order to protect the identities of individual judges.

Our first discovery from the Judges' Questionnaire was that the judges were both a lot easier to find and a lot more willing to respond to questions about bankruptcy than were the

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[44] For discussion of the responses to question one through four, see *infra* Section IV.A.2.a.d.

[45] For discussion of the responses to question five, see *infra* Section IV.A.2.e.

[46] For discussion of the responses to question six, see *infra* Section IV.A.2.f.

[47] The "Judging Styles Inventory" was developed and pretested by the Business Bankruptcy Project. A copy of the Judging Styles Inventory is reproduced in Appendix A. An in-depth explanation of our coding decisions is included in Appendix B.

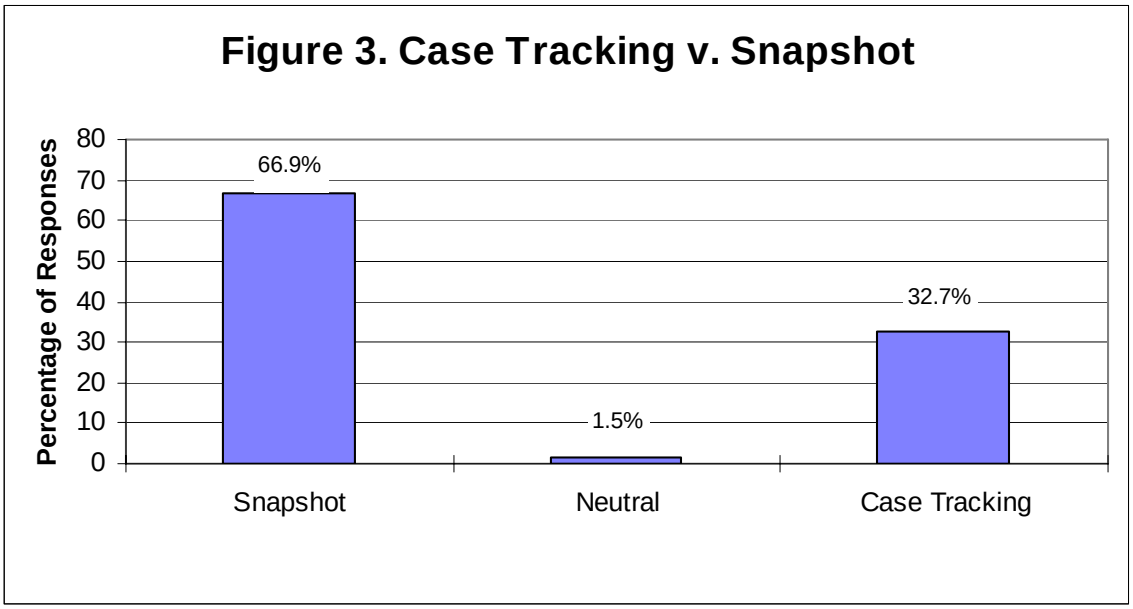
[48] The substantial logistics involved in printing, mailing, and collecting hundreds of questionnaires was executed masterfully by Mark MacDonald, Esq. of the Dallas bar, chair of the ABA Business Bankruptcy Committee. We are grateful to him and the ABA for their help.

debtors. Altogether, we received 224 valid survey responses, which gave us an overall response rate of 71.3%. This extraordinarily high completion rate increases the confidence in the representativeness of our sample. It also gives us a good sampling of judges who have very different views about case management.

Case Administration: Hands On/Hands Off

There has been extensive discussion over whether cases should be more actively managed. "Fast-track" has become something of a bankruptcy in-crowd buzz word, although its specific meaning can be illusive. We used the judges' survey to try to assess various aspects of case management.

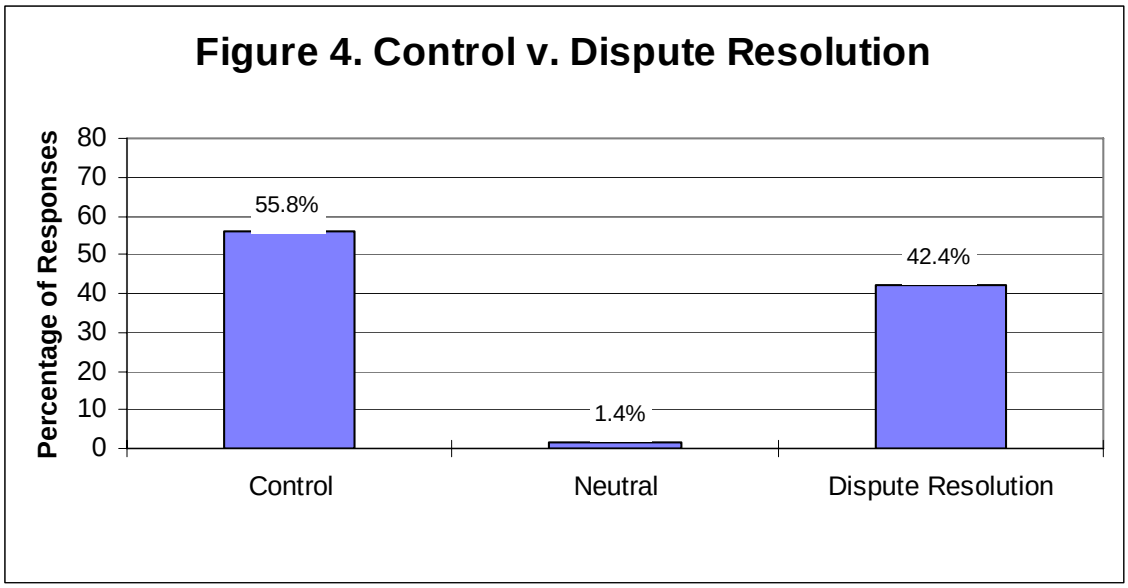
One of the questions we asked focused on the judges' view of the need for involvement as part of optimal caseload management. We asked the judges whether they regarded themselves judges who were more likely to hold hearings on specific matters and receive "snapshot" progress reports at that time or, at the other extreme, like judges who were more likely to track each pending case with regular reviews. The judges expressed strong preferences. Only 1.5% of the judges put themselves in the middle of this question, with the remainder firmly anchored at either end. For more than two-thirds (69.6%) of the judges, "snapshots" look like the best case management technique. But for a third (32.7%), more active case management is the preferred approach. These difference are illustrated in Figure 3.



An
other aspect of case management is the extent to which the court will involve itself in administration of cases rather than limit its interest to resolution of disputes. We realize that,

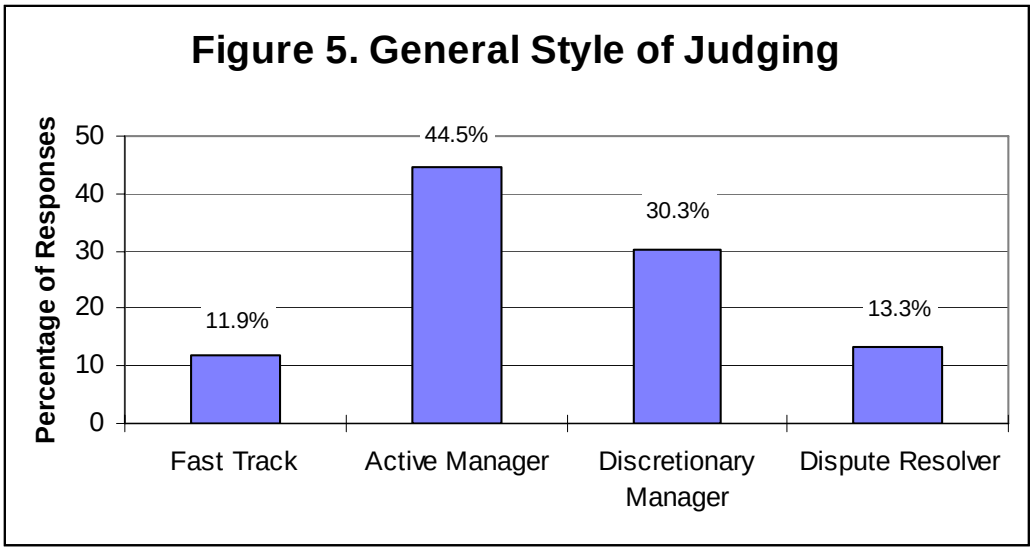
like all the questions in the survey, asking about whether the courts should be involved in case administration or only in dispute resolution is asking about a long line that is colored with shades of gray. Even so, the responses gave us some insight into different judges' proclivities to get involved in matters they deem administrative. The question also gives some insight about how active (or pro-active, in the current business school parlance) the judges are in dealing with their cases. Should they "control" their cases even if they risk engaging in administering cases, or should they wait to resolve disputes brought before them and carefully avoid administrative tasks?

A more balanced split among the judges was discovered. More than half (55.8%) of the judges said they believed case control was important, even if it involved administrative rather than strictly judicial work. Less than half (42.4%) saw it the other way: dispute resolution should be their function to the exclusion of case administration. These results are illustrated in Figure 4.



We had assumed that the relationships between the responses to these two questions would have been positive. In other words, judges who favored "snapshot" management would be more focused on dispute settlement in cases brought to the judge, while judges who wanted more active case management would be more willing to engage in administrative work.

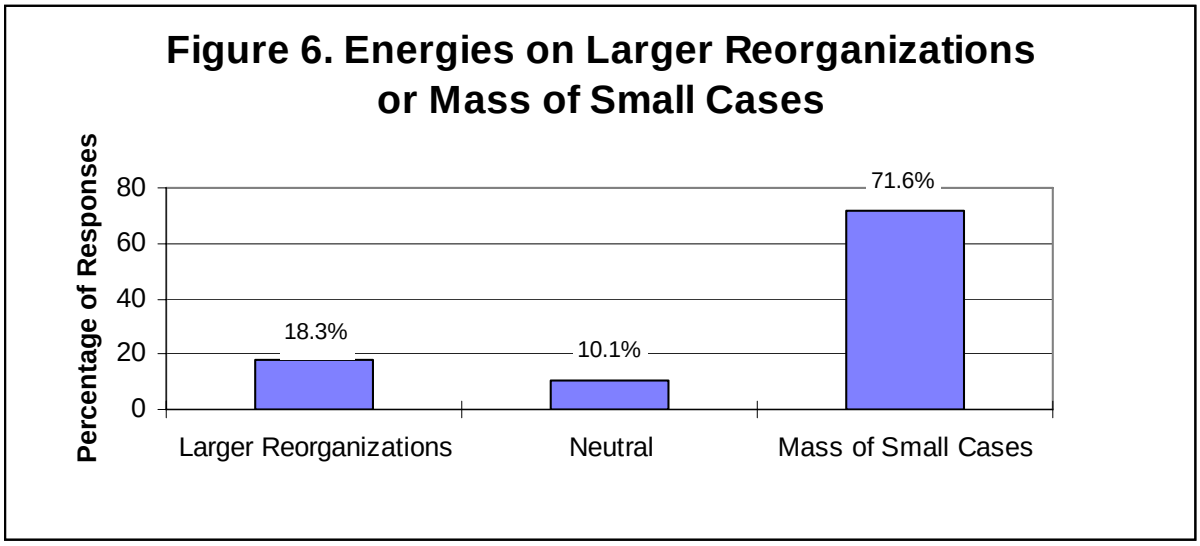
We were able to enhance these competing portraits of the active case manager and the dispute resolver with a third question, summarized in Figure 5. This question was directed toward the judges' own view of his or her "style." In it we described four styles of judging, which we short-handed into "fast-track," "active manager," "discretionary manager," and "dispute resolver." The more detailed descriptions are in the Survey Form in Appendix B. The four choices gave a rough continuum, from most aggressive case management to least active case management.



In this overt self-description, active case management was the favorite of just under half of the judges (44.5%), with approximately one-third (30.3%) of the judges describing themselves closer to the discretionary managers. The self-descriptions are illustrated in Figure 5. Not surprisingly, there was a positive correlation between those judges who described themselves in this question as fast-track or active managers and those who described themselves as willing to take on management of cases and administrative work in the earlier two questions.

The judges' survey permitted us to look at another aspect of judging that has not been in the news, but relates to a number of other issues in the legal system: whether the judges in a district are focused on small cases or whether they see the opportunity to make a more measurable difference in the management of bigger cases in the jurisdiction. The results are illustrated in Figure 6.

The judges gave another lopsided response to the question about where they focus their energies. For about seven in ten of the judges (71.6%), moving the mass of small cases along to dismissal or confirmation is a major responsibility of a bankruptcy judge. By contrast, about two in ten of the judges (18.3%) thought that their most effective time was spent on larger reorganization cases where judicial energy and creativity would make the most difference. Interestingly, on this question, there were more judges in the middle. About one out of ten judges (10.1%) could not describe their views in either direction--far more than in the middle on any other question.



The Policy Implications

While it is very interesting to know something about the diversity of approaches on the bench to questions of managerial style, the value of these data will increase dramatically as we are able to link the judges' responses with information from the files about the cases. These data will give us some opportunity to test whether self-described "fast-tracking" makes a significant difference in the progress of cases through the court system.

Because the database on the court files is so much more detailed than a simple report about how long the debtor remained in the system, we can explore other implications about managerial styles, such as their impact on confirmation rates and creditor pay outs. We can also control for differences among the cases to see whether current evaluations of managerial styles are measuring differences in what judges do or differences in the cases that come through their courthouses.

As these data suggest, it is linking the databases that will expand exponentially the range of questions we can explore in the Business Bankruptcy Study.