

# The Myth of the Disappearing Business Bankruptcy

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Robert M. Lawless & Elizabeth Warren

## INTRODUCTION

Much is contested about why American businesses and families are failing economically, but there is at least one Conventional Story on which most everyone agrees.<sup>1</sup> This Conventional Story teaches that of the 1.6 million bankruptcies filed annually in the United States, only a small fraction are business failures. Business bankruptcies peaked in 1985 at 18.3% of all filings and have steadily declined ever since to their 2003 level of about 2.3%.<sup>2</sup> Thus, the Conventional Story holds that the bankruptcy system has diverged from a mixed consumer-business system, becoming, in effect, a completely consumer-dominated operation punctuated by a small number of huge business failures. The entrepreneur who gambles on a new business undertaking seems to have virtually disappeared from the bankruptcy system.

Accordingly, the Conventional Story's lesson is that the nature of failure has changed. Previously, as the story goes, the inevitable ebb and flow of the business cycle drove a significant number of debtors into bankruptcy court. Business cycles came and went, but they happened and when they happened, they were beyond any one person's control. A debtor who filed for bankruptcy because of a downturn in the business cycle was an

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1. The causes of rising bankruptcy filing rates are hotly debated. For example, Edith H. Jones & Todd J. Zywicki attribute the rise to two factors: "(1) changes in the law and the bankruptcy system that have increased the net economic benefit of filing bankruptcy and (2) a decline in the personal shame and social stigma traditionally attached to filing bankruptcy." *It's Time for Means-Testing*, 1999 BYU L. REV. 177, 210. See also F.H. Buckley & Margaret Brinig, *The Bankruptcy Puzzle*, 27 J. LEGAL STUD. 187 (1998) (providing econometric analysis suggesting that changes in social norms might account for the increased bankruptcy filings). In another article, Henry J. Sommer contends that increased lending to riskier borrowers is a primary contributor to rising bankruptcy filings. *Causes of the Consumer Bankruptcy Explosion: Debtor Abuse or Easy Credit*, 27 HOFSTRA L. REV. 33 (1998). Yet another academic article argues that "the extraordinary increase in consumer bankruptcies is connected to the decline of unions and wage stagnation." Steven H. Kropp, *The Safety Valve Status of Consumer Bankruptcy Law: The Decline of Unions as a Partial Explanation for the Dramatic Increase in Consumer Bankruptcies*, 7 VA. J. SOC. POL'Y & L. 1, 3 (1999). Despite their disparate conclusions, all of these articles rely on the same underlying data from the Administrative Office of U.S. Courts. See Buckley & Brinig, *supra*, at 188-89; Jones & Zywicki, *supra*, at 177, nn.1, 3; Kropp, *supra*, at 2; Sommer, *supra*, at 35.

2. See *infra* Table 1.

unfortunate victim of economic circumstance. The Conventional Story, however, appears to show that business conditions no longer play a role in bankruptcy filings. With the exception of the rare but spectacular mega-bankruptcy, the apparently disappearing business bankruptcy means that most failures now result from consumer overspending.

As a result, the Conventional Story has set the stage for legislators and policymakers to recast bankrupt debtors from unfortunates caught up in the caprices of unforgiving market changes to overspenders responsible for their own misfortunes.<sup>3</sup> Throughout American history, the story about the nature of failure always has influenced the legislative agenda, and this influence has proven to be true yet again.<sup>4</sup> Indeed, members of Congress, their staffs, and lobbyists representing interests of those who would

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3. Consider Representative George Gekas's words in introducing a bill that would have restricted consumers' ability to receive effective bankruptcy relief, castigating modern-day debtors as unworthy spendthrifts:

The greatest, and perhaps most dangerous, irony I have come across in the past decade is that despite economic growth, low inflation, low unemployment, and increasing personal income, our nation has seen as [sic] alarming increase in the number of bankruptcy filings—1.3 million in 1997 to be exact. Think about that for a second. That's more than one family per every hundred in the United States and over \$40 billion in debt that has been erased—in a year of strong economic growth. It only further illustrates the problem when you consider that the number of filings in the '90s is eight times as many, per household, as there were during the Depression. . . .

When irresponsible spenders who can afford to pay all or some of their debt declare bankruptcy, you and I get stuck with the bill. It's a \$40 billion bill that we share this year, or \$400 per household. I don't know about you but \$400 dollars is 5 weeks' worth of groceries or 20+ fill-ups at the gas pump to me. It has also been estimated that it takes 15 responsible borrowers to cover the cost of one bankruptcy of convenience.

144 CONG. REC. E87, E88 (daily ed. Feb. 4, 1998) (statement of Rep. Gekas).

4. Our thoughts in this paragraph quite deliberately build on the ideas of other scholars. According to legal historian Bruce Mann, the issue of whether bankruptcy was a consequence of moral failure or the natural result of entrepreneurial risk was hard fought in revolutionary America. He traces changing attitudes through sermons, pamphlets, private letters, and public documents, illustrating the class-based nature of attitudes toward failure and how the Bankruptcy Clause made it into the Constitution. BRUCE H. MANN, *REPUBLIC OF DEBTORS: BANKRUPTCY IN THE AGE OF AMERICAN INDEPENDENCE* (2002). Edward Balleisen picks up the story with the enactment of a second federal bankruptcy act in 1841 and what he calls "commercial moralism," aiming to inhibit both the "cunning tricks, delays, concealments, and frauds" of debtors and the unseemly grasping of creditors. Balleisen documents the efforts of the moralists to exhort debtors to repay. EDWARD J. BALLEISEN, *NAVIGATING FAILURE: BANKRUPTCY AND COMMERCIAL SOCIETY IN ANTEBELLUM AMERICA* 96 *passim* (2001). John Witt reviewed these two books, along with DAVID A. SKEEL, JR., *DEBT'S DOMINION: A HISTORY OF BANKRUPTCY LAW IN AMERICA* (2001), skillfully weaving the evidence across the centuries into a tale of how the characterization of debtors and the reasons for their failure shaped legislative choices. John Fabian Witt, *Narrating Bankruptcy / Narrating Risk*, 98 *Nw. U. L. REV.* 303 (2003) (book review). Professor Witt explores the competing narratives about financial failure that have been used throughout U.S. history and argues that the shifting nature of bankruptcy law reflects shifting narratives about the nature of failure (or, in his term, "risk"). *Id.* at 329. Specifically, Professor Witt identifies two competing narratives: one treating financial failure as a moral problem and another treating it as a risk of the marketplace. *Id.* at 320-27. When both debtor interests in discharge and creditor interests in efficient collection coalesced, the narrative converged on the risk of the marketplace. We see a similar struggle being played out with the shift in the bankruptcy data.

weaken bankruptcy protection have seized upon the Conventional Story and invoked it as evidence of a shift in the nature of bankruptcy.<sup>5</sup>

Yet, there is a significant problem with the Conventional Story: it is not true. The Conventional Story does not capture the reality of the federal bankruptcy system. In this Article, we present data and evidence demonstrating substantial, systematic errors in the official statistics. The official report of business filings, pegged at 2.3%, is wrong. Based on new research from the Consumer Bankruptcy Project,<sup>6</sup> if historical measures were used, we estimate as many as 17.4% of all current bankruptcy filings involve the failure of a business. Extrapolating to all filings, we estimate that rather than the 37,000 business filings reported by the Administrative Office of the U.S. Courts (AO) for 2003, there were between 260,000 and 315,000 bankruptcies that historically would have been counted as business filings but that in 2003 were not.<sup>7</sup> Thus, we estimate that the AO failed to count as business filings approximately 220,000 to 280,000 filings by entrepreneurs, self-employed individuals, and independent contractors who needed bankruptcy relief as part of their efforts to recover from a failed undertaking.<sup>8</sup>

These findings have implications for bankruptcy scholars generally and the legislative debates about bankruptcy reform specifically. By any count, consumers remain the majority of bankruptcy filers, but the Conven-

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5. For example, in arguing for more restrictive consumer bankruptcy laws, banking industry lobbyist Philip Corwin has contrasted the declining business filing rate with the burgeoning consumer filing rate. See Philip S. Corwin, *Bankruptcy Commission's Report Will Soon Face Congressional Review*, BANKING POL'Y REP., Aug. 4, 1997, at 1; see also Ruth Simon, *Bankruptcy Bill Would Make It Harder to File for Chapter 7*, WALL ST. J., Apr. 23, 2002, at D3 (identifying Philip Corwin as a lobbyist for the American Bankers Association). Senator Sessions's comments on the floor of the Senate similarly contrast the declining business filing rate with the rising consumer rate:

Last year there were over 1.4 million bankruptcies filed in America. That comes out to almost 4,000 filings every day of the year. Since 1990, personal bankruptcies are up 94.7 percent. This dramatic increase in personal bankruptcies occurred in spite of the fact that over that same period business bankruptcies fell 31 percent and the country enjoyed a healthy and expanding economy. These statistics demonstrate there is need for reform immediately.

145 CONG. REC. S11,091 (daily ed. Sept. 21, 1999) (statement of Sen. Sessions); see also 150 CONG. REC. H147 (daily ed. Jan. 28, 2004) (statement of Rep. Watt) ("Business bankruptcies actually fell last year . . . Personal individual bankruptcies increased by about the same percentage."); 145 CONG. REC. S14,248 (daily ed. Nov. 8, 1999) (statement of Sen. Grassley) (citing newspaper article about rising consumer bankruptcies and declining business bankruptcies); 145 CONG. REC. E891 (daily ed. May 6, 1999) (statement of Rep. Kennedy) ("Last year, 1.4 million personal bankruptcies were filed, an increase of 94.7 percent over 1990. By contrast business filings have remained steady over the last two decades."). The National Governors Association also has cited the high proportion of consumer filings in its policy position endorsing changes to the Bankruptcy Code. National Governors Association, *Bankruptcy Reform Policy* (EDC-21), at 21.1, available at [http://www.nga.org/nga/legislativeUpdate/1,1169,C\\_POLICY\\_POSITION^D\\_514,00.html](http://www.nga.org/nga/legislativeUpdate/1,1169,C_POLICY_POSITION^D_514,00.html) (last visited Jan. 21, 2005).

6. See *infra* note 61 and accompanying text (describing the Consumer Bankruptcy Project).

7. Throughout this Article, we will be reporting annual bankruptcy filing data for twelve-month periods ending June 30 of each year, the historical end of the government's fiscal year. This reporting convention allows comparison with historical government data, which were reported on the same period as the government's fiscal year.

8. See *infra* Part II.C.

tional Story has missed a significant portion of bankruptcy filers who are small businesses. Because the AO bankruptcy filing statistics are used as a key indicator of business success and failure, the data reported here change what we understand about success and failure in our economy.<sup>9</sup> In addition to addressing broader economic issues, our data also change what we understand about the role bankruptcy plays in the economy. Our data upset the traditional assumption that bankruptcy plays an increasing role in consumer economics but a diminishing role for small businesses. About one in seven persons appearing in bankruptcy court as a consumer is actually there in connection with his or her own business. These persons are being made to fit into a bankruptcy system designed to deal with consumer problems.

Our data are just a beginning, but they suggest new avenues for research about small business and entrepreneurial activity. Has the nature of small business and entrepreneurship changed? Is work that traditionally would have been done by salaried employees now outsourced to the same individuals who are labeled “consultants” and who now bear far more risks than they did as employees? Has the line between consumers and businesses blurred where the failure of a small business necessarily means the failure of its owner? Are social trends, such as the decline in health insurance among middle-class families, actually the result of more self-employment and more stress on the self-employed? This Article is the beginning of a long-term project about the odyssey of entrepreneurs who try, fail, and try again. Future work will deal with the financial and social characteristics of the self-employed who travel through the bankruptcy courts, and we hope to address some of these questions.

In this Article, we document the incidence of business bankruptcy filers. Part I explains both the data-collection methods of the official record keeper for bankruptcy statistics, the AO, and the uses of that data. We also explore how the AO data began to diverge from other data sets in the mid-to late 1980s. In retrospect, it is less surprising that the AO data diverged from reality and more surprising that hardly anyone has noticed. Part I also explains how the widespread use of automated form software created the opportunity for distortion of the official statistics. We believe this is the most plausible explanation for the difference between our data and those from the AO. In addition to explaining our methodology, Part II then presents our findings. From examining court records and answers provided in response to questions we asked of bankrupt debtors, we find that the incidence of business bankruptcy should be much higher and that our estimates of business filers are closer to historical trends than the AO figures. Our data change what we know about small businesses in bankruptcy, and in

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9. See *infra* Part III.C.

Part III, we explore the implications of our data for the economy generally and for bankruptcy law specifically. Part IV concludes.

## I ORIGINS OF THE UNDERCOUNT

In this Part, we first describe and graphically present the AO's count of the number of business bankruptcy filings. We compare the AO numbers to figures from other data sets. In Section B, we describe how the AO uses court documents to gather its data. In Section C, we explain how attorneys' use of automated form software systematically biases the AO data to show fewer business filers than actually exist.

### A. *The Administrative Office Data*

As the official administrative arm of the federal judiciary, the AO counts each bankruptcy petition filed in federal court. The AO data are widely used. Whenever books, academic articles, or media reports reference bankruptcy filing statistics, these reports use the underlying AO data. What we know about bankruptcy filing rates, we know from the AO data. The AO statistics are not merely the most widely used data; they are the only source of information about total bankruptcy filings.<sup>10</sup>

The AO tallies each bankruptcy petition as one bankruptcy filing whether the case went through the entire bankruptcy process or the court dismissed it at an early stage.<sup>11</sup> The AO then releases these data as official

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10. We have used the AO's data ourselves in previous works. *See, e.g.*, Elizabeth Warren, *The Market for Data: The Changing Role of Social Sciences in Shaping the Law*, 2002 WIS. L. REV. 1, 15 n.52; Robert M. Lawless, *The Relationship Between Nonbusiness Bankruptcy Filings and Various Basic Measures of Consumer Debt*, at <http://www.law.unlv.edu/faculty/rlawless/busbkr/filings.htm> (last visited Jan. 21, 2005). A Westlaw search for the terms "business bankruptcy filings" or "nonbusiness bankruptcy filings" uncovered ninety-eight articles in the law journals alone that cite the AO's data, and other search strategies would undoubtedly uncover more. For some specific examples, see Peter C. Alexander, *Building "A Doll's House": A Feminist Analysis of Marital Debt Dischargeability in Bankruptcy*, 48 VILL. L. REV. 381 (2003); Richard M. Hynes, *Overoptimism and Overborrowing*, 2004 BYU L. REV. 127, 141 nn.60-61; Thomas E. Plank, *The Erie Doctrine and Bankruptcy*, 79 NOTRE DAME L. REV. 633, 634 n.2 (2004). In addition, books cite to the AO's data. *See, e.g.*, KAREN GROSS, *FAILURE AND FORGIVENESS: REBALANCING THE BANKRUPTCY SYSTEM* 74-78 (1997); SKEEL, *supra* note 4, at 187-88. Articles in the popular press also cite the AO. *See, e.g.*, Kate Berry, *Weakening Junk Bond Quality Could Cause More Bankruptcies*, L.A. BUS. J., Apr. 26, 2004, at 50; Allison Linn, *Bankruptcy Break: State Filings Soar, But Business Cases Decline Nearly 5%*, ROCKY MTN. NEWS, Sept. 2, 2003, at 1B; Paul Wenske, *Bankruptcy Filings for 2003 Linger in Record Territory*, KAN. CITY STAR, Feb. 26, 2004, at C2.

11. Since the Bankruptcy Code went into effect in 1980, married couples may file a joint petition. *See* 11 U.S.C. § 302 (2000). A joint petition counts as one bankruptcy filing, although it involves two individuals. From 1980-1983, the AO reported the bankruptcy filing figures by counting each joint petition twice, on the theory that before 1980 each joint petition formerly would have required two filings, one for the husband and one for the wife. In 1984, the AO restated its figures and has counted a joint petition as just one filing ever since. *Compare* ANNUAL REPORT, DIRECTOR OF THE ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS 12 (1983) *with* ANNUAL REPORT, DIRECTOR OF THE ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS 13 (1984). For a thorough

quarterly and annual compilations of the number of bankruptcies filed. In addition to these traditional paperbound releases, bankruptcy statistics are available electronically at the AO's website as well as third-party websites, such as the one hosted by the American Bankruptcy Institute.<sup>12</sup>

1. *The Apparent Decline in Business Bankruptcies as a Percentage of All Filings*

Table 1 reports fifty years of AO data on business and nonbusiness bankruptcy filings. Since 1985, business filings have dramatically declined as a percentage of all filings. In the period 1954–1985, business filings averaged 12.3% of all filings, with a low of 8.0% in 1967 and a high of 18.6% in 1983. During these thirty-one years, the filing rates ebb and flow, with an increase in sixteen years and a decrease in fifteen years. Beginning in 1986, however, the statistical pattern becomes monotonic as business filings began to decline as a percentage of all filings, and each year is less than the previous year (with the exception of 2000 when the numbers are essentially the same as the preceding year). The past nineteen years are dramatically different than the thirty-one years that came before them. For the years 1986 through 2003, business filings average only 6.8% of all bankruptcy filings, tapering to an all-time low of 2.3% in 2003.

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explanation of the AO's initial count of joint petitions, see Robert B. Chapman, *Missing Persons: Social Science and Accounting for Race, Gender, Class, and Marriage in Bankruptcy*, 76 AM. BANKR. L.J. 347, 368-69 (2002).

Our data and remarks do not take into account involuntary bankruptcy cases. Creditors may file an involuntary bankruptcy petition against a debtor. See § 302. The number of involuntary cases is so small that the AO ceased to publish data on them several years ago, and it is exceedingly unlikely that the number of involuntary cases has any meaningful effect on the number of cases counted as business or nonbusiness. There are no involuntary bankruptcy cases in our study.

12. The Federal Judiciary, Bankruptcy Statistics, at <http://www.uscourts.gov/bnrpctystats/bankruptcystats.htm> (last visited June 8, 2004); American Bankruptcy Institute, at <http://www.abiworld.org> (providing repackaged AO statistics) (last visited June 8, 2004). Some articles cite statistics from the American Bankruptcy Institute without any apparent awareness that these statistics are merely data repackaged from the AO. See, e.g., Jonathan D. Glater, *For Lawyers, Is Boom Near in Insolvency?*, N.Y. TIMES, Dec. 26, 2000, at C1.

Table 1: AO Figures for Nonbusiness and Business Bankruptcy Filings 1954–2003 (Twelve Months Ending June 30)<sup>13</sup>

<i>Year</i>	<i>Bus. Filings</i>	<i>Total Filings</i>	<i>Bus. Filings as % of Total Filings</i>	<i>Year</i>	<i>Bus. Filings</i>	<i>Total Filings</i>	<i>Bus. Filings as % of Total Filings</i>
<b>1954</b>	8,888	53,136	16.7%	<b>1979</b>	29,500	226,476	13.0%
<b>1955</b>	9,185	59,404	15.5%	<b>1980</b>	36,449	277,899	13.1%
<b>1956</b>	9,478	62,086	15.3%	<b>1981</b>	47,415	360,329	13.2%
<b>1957</b>	10,144	73,761	13.8%	<b>1982</b>	56,423	367,866	15.3%
<b>1958</b>	11,404	91,668	12.4%	<b>1983</b>	69,818	374,734	18.6%
<b>1959</b>	11,729	100,672	11.7%	<b>1984</b>	62,520	344,625	18.1%
<b>1960</b>	12,284	110,034	11.2%	<b>1985</b>	66,651	364,536	18.3%
<b>1961</b>	15,241	146,643	10.4%	<b>1986</b>	76,281	477,856	16.0%
<b>1962</b>	15,655	147,780	10.6%	<b>1987</b>	88,278	567,266	15.6%
<b>1963</b>	16,302	155,493	10.5%	<b>1988</b>	68,501	594,567	11.5%
<b>1964</b>	16,510	171,719	9.6%	<b>1989</b>	62,534	642,993	9.7%
<b>1965</b>	16,910	180,323	9.4%	<b>1990</b>	64,688	725,484	8.9%
<b>1966</b>	16,430	192,354	8.5%	<b>1991</b>	67,714	880,399	7.7%
<b>1967</b>	16,600	208,329	8.0%	<b>1992</b>	72,650	972,490	7.5%
<b>1968</b>	16,545	197,811	8.4%	<b>1993</b>	66,428	918,734	7.2%
<b>1969</b>	15,430	184,930	8.3%	<b>1994</b>	56,748	845,257	6.7%
<b>1970</b>	16,197	194,399	8.3%	<b>1995</b>	51,288	858,104	6.0%
<b>1971</b>	19,103	201,352	9.5%	<b>1996</b>	52,938	1,042,110	5.1%
<b>1972</b>	18,132	182,869	9.9%	<b>1997</b>	53,993	1,316,999	4.1%
<b>1973</b>	17,490	173,197	10.1%	<b>1998</b>	50,202	1,429,451	3.5%
<b>1974</b>	20,746	189,513	11.0%	<b>1999</b>	39,934	1,391,964	2.9%
<b>1975</b>	30,130	254,484	11.8%	<b>2000</b>	36,910	1,276,922	2.9%
<b>1976</b>	35,201	246,549	14.3%	<b>2001</b>	37,135	1,386,606	2.7%
<b>1977</b>	32,189	214,399	15.0%	<b>2002</b>	39,201	1,505,306	2.6%
<b>1978</b>	30,528	202,951	15.0%	<b>2003</b>	37,078	1,649,660	2.3%

Even as absolute figures, the official AO statistics indicate a decline in business bankruptcies. The absolute number of business filings peaked in 1987 at 88,278, but by 2003, the number had fallen to 37,078. Although the absolute numbers do not show the monotonic decline that the percentage figures display, the overall pattern displays a dramatic downward

13. Table 1 contains the AO's official statistics for the past fifty years of bankruptcy filings. For each year listed, the filings reflect the number of filings for the twelve months ending June 30, the end

trend. Indeed, the AO numbers would have us believe that the twelve months ending June 30, 2003, experienced just about the same number of business filings as the same period in 1980 when the population of the United States was 22% smaller and inflation-adjusted GDP was 50% smaller.<sup>14</sup> In other words, the AO data indicate that the absolute number of business filings was the same in 2003 as when the U.S. population and economy were dramatically smaller.

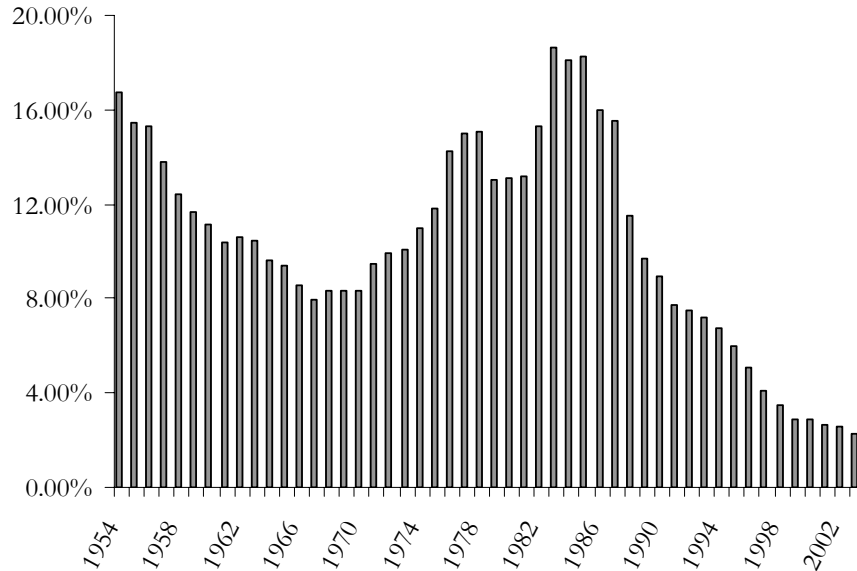
Figure 1 graphically depicts this decline in business bankruptcies as a percentage of all bankruptcy filings for a fifty-year period. All data are from the official AO statistics and are for the twelve-month period ending June 30 for each year. Beginning in 1986, business bankruptcies began to decline as a percentage of all bankruptcy filings, dropping to a low of 2.3% for the twelve months ending June 30. With one exception in the years 1999–2000, when the numbers were virtually identical, each twelve-month period from 1986–2003 exhibited a decline in the percentage of business filings.

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of the government's fiscal year until 1977 and the historical reporting date for annual bankruptcy filings. With one exception, all data are from various editions of the *Annual Report, Director of the Administrative Office of the United States Courts*. The one exception is for the year 1980, when the transition to the current Bankruptcy Code and changes in the AO's reporting methods caused the *Annual Report* not to contain a full twelve months of bankruptcy filing data. Instead, the 1980 data appear in the *Statistical Abstract of the United States*. U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE UNITED STATES: 1985-1986 (1985). Before 1980, the AO totaled four occupational categories to calculate business filings: farmers, professionals, merchants, and others in business.

14. See U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE UNITED STATES: 2004-2005, at 7 table 2 (2004) (providing population figures); Bureau of Economic Analysis, GDP Figures, at <http://www.bea.doc.gov/bea/dn/gdplev.xls> (last visited Dec. 13, 2004).

Figure 1: Business Filings as Percentage of All Bankruptcy Filings 1954–2003 (Twelve Months Ending June 30)



The official decline in business bankruptcies is remarkable and, standing alone, begs for explanation. All things being equal, business bankruptcies should increase in absolute number as the country grows and should remain roughly proportional to overall filings. It certainly is possible to speculate that some dramatic economic and social change occurred in the 1990s, which led to a decline in business filings. The 1990s were a period of great economic growth, but business filings continued to decline even after the economy soured in the late 1990s. There is no readily apparent explanation for why business filings have come to represent such a small proportion of all bankruptcy filings. In hindsight, it is apparent that sometime between 1980 and the present, the AO data ceased to capture the reality of the bankruptcy system.

## 2. Comparing the Administrative Office Data to Other Sources

Because the AO data purport to capture business bankruptcies, they should correspond with other records on business failures and closings outside of bankruptcy. When one compares the AO data to other data sets, however, the AO data become the anomaly. This analysis further suggests that it is the official court statistics that have diverged from the underlying reality of the cases.

a. *The Dun & Bradstreet Statistics*

Through 1998, the credit-reporting and business information firm of Dun & Bradstreet (D&B) tracked business failures, defined as businesses with court proceedings or voluntary actions involving losses to creditors. D&B gathered these data from its proprietary databases—sources that are independent of the AO data series.<sup>15</sup> For the period 1954–1985, there is a strong positive association between the D&B figures and the AO’s count ( $r = 0.73$ ,  $p < 0.01$ ).<sup>16</sup> D&B listed fewer business failures than the AO’s count of business bankruptcies, but the direction of change for both data sets remained in synch. For more than thirty years, as D&B showed more businesses failed, the AO also showed more businesses failed.

The correlation then reversed sharply. Beginning around 1986, the year in which the AO figures begin their decline,<sup>17</sup> the D&B data diverge from the AO data. For the last twelve years of the series (1986–1998), the D&B data on the number of business failures are actually negatively correlated ( $r = -0.13$ ,  $p = 0.68$ ) with the AO data on the number of business bankruptcies. This means that as D&B showed more businesses were fail-

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15. In each annual release of its data set, D&B outlined its definition of “business failures”:  
 Dun & Bradstreet’s business failure statistics include businesses that ceased operations following assignment or bankruptcy; ceased operations with losses to creditors after such actions as foreclosure or attachment; voluntarily withdrew leaving unpaid debts; were involved in court actions such as receivership, reorganization or arrangement; or voluntarily compromised with creditors.  
 Business Failures vs. Business Discontinuances [sic]: Business failures do not represent total business closings, which consist of both business failures and business discontinuances. As defined in Dun & Bradstreet’s statistics, business failures consist of businesses involved in court proceedings or voluntary actions involving losses to creditors. In contrast, businesses that discontinue operations for reasons such as loss of capital, inadequate profits, ill health, retirement, etc., are not recorded as failures by Dun & Bradstreet if creditors are paid in full. Although they represent only a percentage of total closings, failures have the most severe impact upon the economy.

THE DUN & BRADSTREET CORP., BUSINESS FAILURE RECORD: A COMPARATIVE STATISTICAL ANALYSIS OF GEOGRAPHIC AND INDUSTRY TRENDS IN BUSINESS FAILURES IN THE UNITED STATES 19 (Neil DiBernardo ed., 1996).

16. Because the D&B figures were for the calendar year and because we use the AO’s data for the twelve-month period ending June 30, we calculated correlation coefficients between the two data sets with a one-year lag (i.e., the preceding year), a one-year lead (i.e., the trailing year), and the average of the current year and a one-year lag. The results were similar to that reported in the text above, with positive and statistically significant coefficients for the period 1954–1985 and negative and statistically insignificant coefficients for the period 1986–1998.

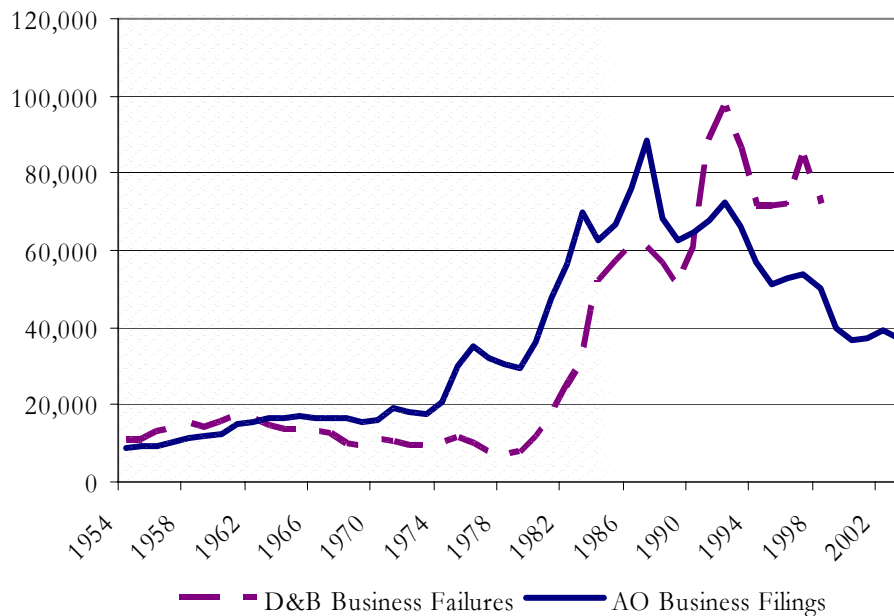
Beginning in 1984, D&B began to include business failures from agriculture, forestry and fishing, finance, insurance, and real estate and expanded to include all failures from the services industries. *See id.* We cannot exclude the possibility that D&B’s added coverage might have caused its data series to diverge from the AO’s numbers, although we cannot think of a ready explanation for why D&B’s expansion in coverage would have caused its numbers to become less accurate. Also, looking just at the period after D&B’s expansion in coverage, the increase in the D&B figures contrasts sharply with the decrease in the AO’s figures. From 1984 to 1997, D&B tracked business failures as rising from 52,078 to 83,384, while over the same time period the AO showed business bankruptcies dropping from 62,250 to 37,078.

17. *See supra* Table 1.

ing, the AO showed fewer failed. The year 1998 provides an example. In that year, D&B reports 71,857 business failures, an increase of 10,241 failures compared to 1986. Instead of an increase for the comparable time period, the AO instead reports a decrease of 26,079 business bankruptcies.

The D&B data series comes from its own proprietary data sources, and thus one would not expect it to match the AO data series perfectly. Still, the two data series purport to capture the same underlying phenomenon: business failure. The two data series should at least move in the same direction, which they did for thirty years until approximately 1985, as illustrated in Figure 2.

Figure 2: Dun & Bradstreet's Business Failures Compared to the AO's Business Bankruptcy Filings, 1954-2003<sup>18</sup>



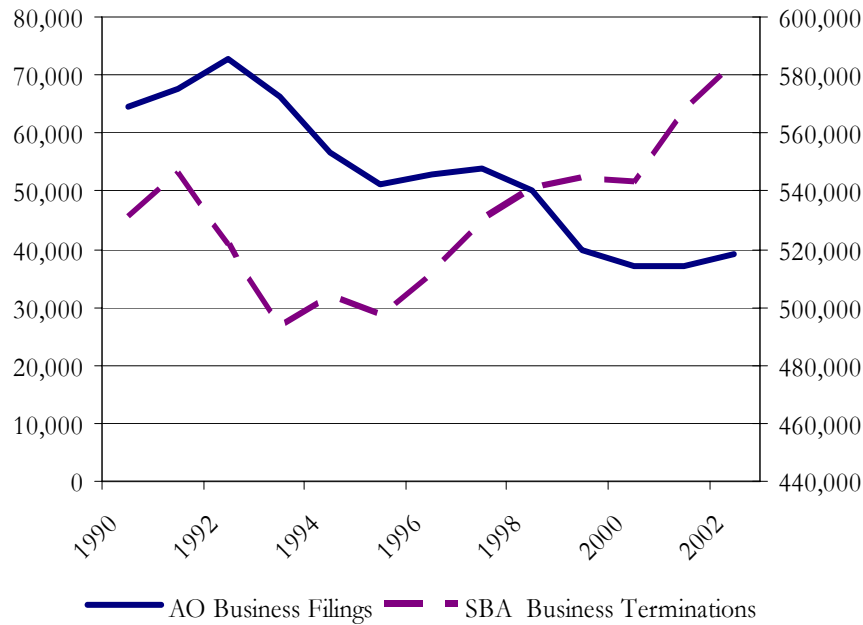
#### b. *The Small Business Administration Statistics*

A data series on business terminations maintained by the Small Business Administration (SBA) also shows the absence of a relationship with the AO numbers. Using census data, the SBA's Office of Advocacy com-

18. Figure 2 displays the relationship between fifty years of data for business failures as reported by D&B and business bankruptcy filings as reported by the AO. The D&B data are for the calendar year, and AO's data are for the twelve-month period ending June 30 for each year shown. The D&B data are from the company's annual *Business Failure Record*, which ended in 1998. "Business failures" are businesses involved in court proceedings or voluntary actions involving losses to creditors. D&B collected the business failure data by tracking changes to its databases. The shaded area represents the period through 1985, the year business bankruptcies began to decline as a percentage of all filings.

piled data on “employer firm terminations” from 1990-2002.<sup>19</sup> An “employer firm” is one with employees, and the SBA counts any business closure as a termination, regardless of whether it resulted from a retirement or other reasons not connected to financial distress. Consequently, the SBA numbers are of a much larger magnitude than the AO statistics for business bankruptcies.

Figure 3: SBA Business Terminations Compared to the AO Business Bankruptcy Filings, 1990-2002<sup>20</sup>



Both data sets capture business failures and thus should bear some relationship to each other. There are differences in the two data sets, however, meaning the correlation will not be perfect. Most significantly, the SBA data set contains some firms that did not fail but instead closed for other reasons. Nonetheless, the two data sets should bear some relationship to each other. In fact, the two data sets actually tend to move in the opposite direction relative to each other ( $r = -0.60$ ,  $p = 0.03$ ).<sup>21</sup> From 1990 to

19. See OFF. OF ADVOCACY, SMALL BUS. ADMIN., SMALL BUSINESS ECONOMIC INDICATORS FOR 2002: A REFERENCE GUIDE TO THE LATEST DATE ON SMALL BUSINESS ACTIVITY, INCLUDING STATE & INDUSTRY DATA 13 table 3 (2003), at <http://www.sba.gov/advo/stats/sbei02.pdf>.

20. Figure 3 compares the SBA figures on employer firm terminations to AO's figures on business bankruptcies for the period 1990-2002. The SBA's figures are not available for other time periods. The SBA's figures are for a calendar year, and the AO's figures are for the twelve-month period ending June 30 for each year.

21. As with the D&B data, see *supra* note 16, we compared the SBA data for a calendar year with the AO data for the twelve-month period ending June 30. We again compared the two data sets

2002, the SBA shows employer firm terminations increasing 10.0%, from 531,400 in 1990 to 584,500 in 2002. During the same time period, the AO shows a 39.4% decrease in business bankruptcies, from 64,688 in 1990 to 39,201 in 2002. Although there are differences between the SBA and AO data sets, the negative correlation between the two data sets provides yet another anomaly that must be explained away for the AO data to make sense.

### 3. Summary

Thus, the accuracy of the official AO data is called into doubt. While the official AO data show business bankruptcies have declined precipitously since approximately 1986, other data sets that track business failures and closings show modest increases over the same time.

In addition to running contrary to these other data sets, the AO data fly in the face of common sense: a growing population and greater numbers of businesses should lead to more business filings. In isolation, any one piece of evidence can be explained away: the economy improved significantly, legal culture changed, data sets measured different things in different ways, and so forth. To explain away all of the differences between the AO data and other data sets requires numerous heroic assumptions. Considered as a whole, however, the simpler explanation is that the AO data are anomalous. The next Section attempts to account for the anomaly by tracing the development of the AO data-collection method—automated techniques that were subject to distortion as new technologies emerged in the 1980s.

#### B. *How the Administrative Office Collects Its Data*

To appreciate how the AO data became susceptible to distortion, it is necessary to understand how the source documents used by the AO changed through the years. Until 1991, these source documents were statistical cover sheets used by bankruptcy clerk offices for each new bankruptcy case. Because these statistical cover sheets were not official court forms, they do not appear in old government publications, making it exceedingly difficult to track precisely when these forms were first used. Nevertheless, we have been able to piece together a history of the documents used by the AO to track business versus nonbusiness filings. The narrative tells a story of data forms that increasingly guided filers away from identifying themselves as business filers. Also, as the task of completing the forms shifted from bankruptcy court clerks to debtors' attorneys, the forms became susceptible to systematic bias as attorneys increasingly relied on software to complete the bankruptcy forms.

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with a one-year lag, a one-year lead, and the average of the current year and a one-year lag. The results were not qualitatively different.

### 1. *The Origins of the Business/Nonbusiness Distinction*

Since 1980, the AO divides all bankruptcy filings into two categories—business and nonbusiness/consumer—but it was not always so. Before Congress passed the current Bankruptcy Code in 1978, the AO categorized all individual debtors into seven different occupational groups: (1) farmers, (2) professionals, (3) merchants, (4) manufacturers (5) others in business, (6) employees, and (7) others not in business.<sup>22</sup> The AO counted “employees” and “others not in business” as the nonbusiness filings and lumped together the remaining five categories to make up the business filings.<sup>23</sup>

The current Bankruptcy Code became effective on October 1, 1979, making 1980 the first complete calendar year that the Bankruptcy Code was in effect. Hence, in reporting the 1980 data, the AO made a number of changes to its bankruptcy statistics. Among these changes was dropping the seven-category occupational groupings in favor of a simple business/nonbusiness distinction.<sup>24</sup> The AO’s change in recordkeeping apparently did not have much effect on the percentage of filings counted as business filings. In 1979, the AO counted 13.0% of all filings as business, a figure not materially different from the 13.1% and 13.2% figures reported for 1980 and 1981, respectively.<sup>25</sup>

In the new business/nonbusiness coding, the AO initially relied on court clerks to distinguish between business and nonbusiness cases, with haphazard results. Reporting on the 1981 phase of the Consumer Bankruptcy Project, one of us (Warren) and her coauthors stated, “[T]he basic AO information on business versus consumer bankruptcies is poorly compiled. Each bankruptcy clerk classifies the local cases, and despite some AO efforts at standardization, we learned in our study that each clerk has a distinct and different method of interpreting the classifications.”<sup>26</sup> In addi-

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22. See, e.g., ANNUAL REPORT, DIRECTOR OF THE ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS 163 (1960).

23. ANNUAL REPORT, DIRECTOR OF THE ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS 85 n.\* (1976).

24. See ANNUAL REPORT, DIRECTOR OF THE ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS 137 (1980).

25. See *supra* Table 1.

26. TERESA A. SULLIVAN, ELIZABETH WARREN, & JAY L. WESTBROOK, AS WE FORGIVE OUR DEBTORS 16 (1989) [hereinafter AS WE FORGIVE]. The footnotes elaborate on the problems in the data:

The AO’s data cause persistent problems for those trying to segregate the business cases from the consumer cases. . . . There appear to be no effective standardized procedures to guide the local clerks who must decide when a petition represents a “business 7” or a “business 13” petition rather than a nonbusiness equivalent. Although one clerk told us that some guidelines existed for classifying cases as “business or “nonbusiness,” we saw a variety of procedures in use. The cases that were relatively easy to identify had docket sheets that used a corporate name or listed individuals with a “doing business as” (dba) designation. The harder cases involved the “formerly doing business as” designation or were filed by a self-employed entrepreneur who had not designated dba. Some clerks asked the attorney to make the “business-nonbusiness” designation; others looked through the filing papers themselves.

tion, there appear to have been significant classification errors. When Philip Shuchman examined the bankruptcy petitions and schedules filed in nine judicial districts during 1979-1981, he reported that 12% of Chapter 7 filings that were identified as personal bankruptcies were in fact business-related.<sup>27</sup> In similar single-state studies, Shuchman found that 12% of Chapter 7 filings in New Jersey during 1980-1982 and 13% of Chapter 7 filings in Connecticut in 1980 were actually business-related although the court filings denominated them as consumer bankruptcies.<sup>28</sup>

## 2. *The Mid- to Late 1980s and the Unofficial Cover Sheet*

Sometime in the early 1980s, the AO started using a statistical cover sheet for each bankruptcy petition.<sup>29</sup> Reports differ on who filled out the cover sheets—local clerks in the bankruptcy courts or attorneys for the debtors. The cover sheet included a checkbox, which the AO used to categorize bankruptcy cases, a practice that continues to this day.<sup>30</sup> Among other information, the earliest version of this cover sheet asked whether the nature of the debts was “Business” or “Non-business/Consumer.” In filling out the cover sheet,<sup>31</sup> the instructions on the back of the form directed the respondent to consider which type of debt the debtor “primarily” had. If the respondent answered “Business,” the form then directed the respondent to identify the “Form of Organization,” for which the first choice was “Individual.” Thus, the early version of the cover sheet explicitly made clear that a case involving business debts could also involve an individual and that business bankruptcies were not limited to corporations, partnerships, or other legal creations.

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Some clerks declared a filing to be a “business case” if the petitioner’s employer had declared bankruptcy.

*Id.* at 41 nn.1-2.

27. Philip Shuchman, *The Average Bankrupt: A Description and Analysis of 753 Personal Bankruptcy Filings in Nine States*, 88 COM. L.J. 288, 289 (1983).

28. Philip Shuchman, *New Jersey Debtors 1982-1983: An Empirical Study*, 15 SETON HALL L. REV. 541, 553 (1985); Philip Shuchman & Thomas L. Rhorer, *Personal Bankruptcy Data for Opt-Out Hearings and Other Purposes*, 56 AM. BANKR. L.J., 19 n.42 (1982) (“Many of the cases we identified as business-related were filed with no indication of that fact. This suggests that more detailed examination might reveal that the national count of business bankruptcies is understated.”).

29. See *infra* Figure 4.

30. See Email from Edward Flynn, Executive Office of U.S. Trustee, to Robert Lawless, Professor of Law, University of Nevada, Las Vegas, William S. Boyd School of Law (Mar. 5, 2004, 08:59:56 PST) (on file with authors) [hereinafter Flynn Email]; see also Jennifer Connors Frasier, *Caught in a Cycle of Neglect: The Accuracy of Bankruptcy Statistics*, 101 COM. L.J. 307, 312 (1996) (describing AO’s data-collection process for bankruptcy).

31. For information on who filled out the cover sheet, see *infra* Part I.B.4.

Figure 4: 1987 Cover Sheet: Nonbusiness/Business Checkbox

<b>NATURE OF DEBT</b>		
<input type="checkbox"/> Business – Complete A, B, C below	↙	<input type="checkbox"/> Non-business/Consumer
<b>A. FORM OF ORGANIZATION (Check One Box)</b>		
<input type="checkbox"/> Individual		<input type="checkbox"/> Partnership
<input type="checkbox"/> Corporation Publicly Held		<input type="checkbox"/> Corporation Closely Held
<b>B. TYPE OF BUSINESS (Check One Box)</b>		
<input type="checkbox"/> Farmer	<input type="checkbox"/> Transportation	<input type="checkbox"/> Construction
<input type="checkbox"/> Professional	<input type="checkbox"/> Manufacture/Mining	<input type="checkbox"/> Real Estate
<input type="checkbox"/> Retail/Wholesale		<input type="checkbox"/> Other Business
<b>C. BRIEFLY DESCRIBE NATURE OF BUSINESS</b>		

The distinction between business and consumer debt itself was crude and misleading. Ask the average entrepreneur—especially one in serious financial trouble—whether he or she has business or consumer debt, and the answer will probably be “both.” For many entrepreneurs, their personal affairs are so intertwined with their business that it is difficult to distinguish between consumer and business debt.<sup>32</sup> Even if debtors (or, more accurately, their attorneys) honestly attempted to answer the checkbox, the form’s shortfalls made it unclear whether the answer provided meaningful information.

Nevertheless, the inquiry into whether a debtor had primarily consumer or business debts persisted and, beginning in 1984, leapt from the statistical cover sheet into the statutory code. In 1984, Congress amended the Bankruptcy Code in three places to include the phrase “an individual debtor whose debts are primarily consumer debts.”<sup>33</sup> First and most significantly, this phrase identified those debtors who were subject to the new statutory standard of having their Chapter 7 cases dismissed for “substantial abuse.”<sup>34</sup> Only those whose debts were “primarily consumer debts” faced dismissal under the new standard; business debtors escaped such scrutiny. Second, Congress extended protection for preferential payments to creditors who had received transfers of less than \$600 in the case of “an individual debtor whose debts are primarily consumer debts.”<sup>35</sup> This meant

32. See *infra* note 70 and accompanying text (discussing mixed nature of business and consumer debt for entrepreneurs).

33. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, §§ 310, 312, 321, 98 Stat. 333, 355, 357.

34. *Id.* § 312, 98 Stat. at 355 (codified at 11 U.S.C. § 707(b)).

35. *Id.* § 310, 98 Stat. at 355 (codified at 11 U.S.C. § 547(c)(8)).

that the creditors of consumers could keep money that they would have had to return to the bankruptcy estate in a business case. Third, in an obvious attempt to push individual debtors with “primarily consumer debts” into Chapter 13, the court clerks were now required to inform such debtors of each chapter under which they were eligible to file bankruptcy.<sup>36</sup> In effect, consumers were to get an extra piece of paper, while business filers needed no such notification.<sup>37</sup>

At the same time that it made these three changes, Congress added what is now Exhibit B to the bankruptcy petition, requiring the attorney to declare that the relief and eligibility rules for the different chapters had been explained to an individual debtor with primarily consumer debts.<sup>38</sup> Since the Bankruptcy Code’s enactment, it had defined the term “consumer debt” to mean debts incurred by an individual primarily for a personal, family, or household purpose,<sup>39</sup> and various provisions of the Code contained special rules for dealing with consumer debts.<sup>40</sup> The 1984 changes, however, created the new status of being an individual debtor with *primarily* consumer debts.

Because both the statutory changes and the new Exhibit B attached potentially negative consequences to classification as an individual debtor with primarily consumer debts with no corresponding increase in the risks associated with business filings, it would be reasonable to predict that these changes would have deterred self-identification as having primarily consumer debts. According to the AO reports, however, the opposite occurred: the year after these changes, 1985, marked the zenith for business filings, and they have declined as a percentage of overall filings ever since.<sup>41</sup> Of course, it is unlikely that any court would consider the checkbox on the statistical cover sheet as outcome determinative for purposes of determining the debtor’s status. Nevertheless, the official AO statistics did not show any sensitivity to the 1984 changes, a fact that may suggest that the official numbers on business bankruptcies already were beginning to lose touch with the underlying reality they were supposed to measure.

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36. *Id.* § 302, 98 Stat. at 352 (codified at 11 U.S.C. § 342(b)).

37. Congress did not bother to explain how court clerks were to find debtors and explain chapter eligibility before the debtor filed bankruptcy, but that is a story for another day.

38. *Id.* § 322, 98 Stat. at 357-58.

39. *See* 11 U.S.C. § 101(8) (2000).

40. *See* 11 U.S.C. § 521 (requiring filing of a Statement of Intention); *id.* § 532(c)(3)(C) (describing a special dischargeability exception for “consumer debts” for “luxury goods”); *id.* § 722 (allowing redemption of tangible personal property intended for household use securing a lien for dischargeable consumer debts); *id.* § 1222 (allowing different Chapter 12 treatment for certain consumer debts); *id.* § 1301 (permitting Chapter 13 codebtor stay for consumer debts); *id.* § 1305 (allowing certain postpetition consumer debts to be dealt with in a Chapter 13 case); *id.* § 1322 (allowing different Chapter 13 treatment for certain consumer debts).

41. *See supra* Table 1.

### 3. *The Official Cover Sheet, 1991 to the Present*

The next development in the evolution of the AO data-collection procedure occurred in 1991, when the Judicial Conference of the United States merged the official bankruptcy petition and unofficial statistical cover sheet into one document.<sup>42</sup> The stated reason for the merger was “to assist the clerk in providing the statistical information required by the Director of the Administrative Office of the United States Courts.”<sup>43</sup> If nothing else, the placement of the checkbox on the updated official petition meant that, rather than the haphazard process of the past, attorneys and pro se debtors should be making the business/nonbusiness identification rather than someone in the clerk’s office. After all, it is the attorney’s responsibility to complete all official forms submitted in a bankruptcy case. Initially, the new bankruptcy petition presented the distinction between business and non-business debts in a format virtually identical to that of the preexisting cover sheet. In 1997, however, the form was changed once again to the format depicted in Figure 5, which remains the current format.

Figure 5: Official Form for Voluntary Bankruptcy Petition, Nonbusiness/Business Checkbox in 2004

Type of Debtor (Check all boxes that apply)	
<input type="checkbox"/> Individual(s)	<input type="checkbox"/> Railroad
<input type="checkbox"/> Corporation	<input type="checkbox"/> Stockbroker
<input type="checkbox"/> Partnership	<input type="checkbox"/> Commodity Broker
<input type="checkbox"/> Other _____	<input type="checkbox"/> Clearing Bank
Nature of Debts (Check one box)	
<input type="checkbox"/> Consumer/Non-Business	<input type="checkbox"/> Business

The post-1997 checkbox differs in subtle yet important ways from all of the versions previously used. First, the newer form completely omits the portion of the previous versions that asked the debtor to briefly describe the nature and type of the business.<sup>44</sup> More importantly, the older form directs persons who are identified as having primarily business debts to identify their organizational form,<sup>45</sup> and the first possible choice is “Individual.” The newer form allows this choice but does not explicitly direct the user to consider whether a business debtor might be an individual. Thus, the newer

42. See OFFICIAL BANKR. FORM I, advisory committee note (1991). The Judicial Conference of the United States is responsible for promulgating the official bankruptcy forms. See FED. R. BANKR. P. 9009.

43. OFFICIAL BANKR. FORM I, advisory committee note (1991).

44. See *id.* (“The amount of information requested in the boxes labeled ‘Type of Debtor’ and ‘Nature of Debt’ has been reduced.”).

45. We understand the AO has since ceased collecting data on the organizational form of bankruptcy filers that are business entities. See Flynn Email, *supra* note 30.

form more readily suggests to the user a particular interpretation: individuals generally do not have business debts. Because the decline in business bankruptcies began long before the newer form appeared, it is difficult to attribute the entire decline to the change between the two forms. Nonetheless, it is relevant to compare the old and new forms because the new forms remove an important reminder that individuals may be appropriately classified as business debtors.

#### 4. *Who Completed the Cover Sheet*

In addition to the wording of the checkbox, the very existence of an official cover sheet and the way it was usually filled out also changed the dynamic of the reported bankruptcy statistics. Practice materials from the 1980s suggest that it was common practice for attorneys to complete the unofficial cover sheet, often under compulsion of a local court rule.<sup>46</sup> Presumably, attorneys would be in a better position to determine whether their own clients' cases involved primarily business or consumer debt. Nevertheless, the requirement that the attorney complete the cover sheet seems often to have been honored in the breach. At least one bankruptcy judge complained that the cover sheet often was not filed or was filed with incomplete information.<sup>47</sup> In a later article, the same judge noted that attorneys submitted very few statistical cover sheets in the Central District of California, one of the nation's largest districts for bankruptcy filings. Prior to that time, the Federal Judicial Center "reconstructed the necessary data for the Central District by reviewing case files."<sup>48</sup> In other words, the clerks determined the classification in many cases while attorneys did it in others.

The adoption of an official cover sheet in 1991 changed this hodgepodge of practices and required attorneys to submit the cover sheet as part of each bankruptcy filing. Thus, by the end of 1991, the onus of filling out the forms clearly shifted from court clerks to attorneys.<sup>49</sup> Jennifer Connors Frasier examined 1994 business filings and found significant errors in these forms, with 13.9% of all cases inaccurately coding whether the case

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46. See Lisa Hill Fenning, *The Future of Chapter 11: One View from the Bench*, in 650 PRACTISING L. INST., COMMERCIAL LAW AND PRACTICE COURSE HANDBOOK SERIES 317, 326 (1993); C. William Schlosser, Jr., *Chapter 13 Bankruptcy as an Alternative to Chapter 7*, 18 COLO. LAW. 2089, 2094 (1989) (offering practice points to Colorado lawyers in filing Chapter 13 and noting the requirement of filing a "bankruptcy statistical cover sheet").

47. See Fenning, *supra* note 46, at 326 ("The Official Form 1, the voluntary petition, was revised in August 1991 in an effort to capture better statistical data by incorporating that information in the petition itself, rather than using a separate cover sheet—which frequently was not even submitted at all.").

48. Lisa Hill Fenning & Craig A. Hart, *Measuring Chapter 11: The Real World of 500 Cases*, 4 AM. BANKR. INST. L. REV. 119, 125 (1996). This same article found underreporting of Chapter 11 business cases, estimating that 79% of the Chapter 11 cases studied in the article were actually business filers instead of the 72% reported by the AO. See *id.* at 132.

49. For a description of the AO's data-collection process and how it changed in the early 1990s, see Frasier, *supra* note 30, at 312-17.

was a business or nonbusiness filing, regardless of the direction of the error.<sup>50</sup> Although this earlier study never suggested that a systematic undercount of business filings was occurring, it remains important for our purposes because it establishes that nontrivial errors were occurring in the recording and gathering of this data and documents the role that court clerks and attorneys were playing.

Thus, the business/nonbusiness distinction has never enjoyed an unblemished reputation for accuracy. In the early years of transition to the new Bankruptcy Code, the distinction was haphazardly determined. Sometimes, it was a court clerk who made the business/nonbusiness determination; other times, it was the debtor or the debtor's attorney. As the unofficial statistical cover sheet eventually became part of the official court filing, the process became more regularized, as pro se debtors or attorneys were now self-identifying the type of case. But the participation of attorneys rather than court clerks did not assure the accuracy of the data. In fact, it had the opposite effect. First, the form's wording itself suggested that individual debtors generally should be classified as nonbusiness rather than business filers. More importantly, at the same time that these changes took place, bankruptcy form software emerged, playing an additional and unanticipated role in the official bankruptcy data reporting.

### C. *The Role of Automated Form Software*

Bankruptcy form software has played a significant role in the undercount of businesses filings for bankruptcy. Since the mid-1980s, attorneys have had access to software that takes data entry from the attorney—or, in most cases, the attorney's assistant or paralegal—and automatically completes the forms necessary to file a bankruptcy case.<sup>51</sup> The most widely used software programs currently on the market employ a default setting of consumer bankruptcy. In these programs, the attorney completing the forms must act affirmatively (for example, clicking a different box) for the

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50. See *id.* at 331, 351 (tabulating results in Table 5 for "Debt Nature").

51. The dates bankruptcy-form software became available are discussed *infra* notes 56-57 and accompanying text. One can gain an appreciation for the beginning of law firm computerization generally by reading articles and product reviews from legal newspapers and other practitioner-oriented materials from the mid-1980s. See, e.g., C. Rudy Engholm, *Hidden Costs in Buying a Computer for the Firm*, NAT'L L.J., May 16, 1983, at 15 (discussing computer options on the premise that "every sole practitioner ought to buy a microcomputer"); Sharon Geltner, *Home Computers Help to Break New Legal Ground*, LEGAL TIMES, Aug. 20, 1984, at 32 (describing uses attorneys were finding for computers in the home); Stephen A. Glasser & Lynn S. Glasser, *Deep, Not Silent: Currents of Change*, LEGAL TIMES, June 13, 1983, at 2 (identifying cost pressures from essential technology as one of ten "currents of change" in the legal profession); Steve R. Riskin, *Legal Systems Software for the Small Law Office*, 71 A.B.A. J. 119 (1985) (evaluating software packages); Paul Ruskin, *Microcomputers Now Desktop Tool for Many Attorneys*, LEGAL TIMES, May 23, 1983, at 16 (evaluating the transformation of the personal computer into a tool used by many lawyers); Ross A. Susman, *New Family of Microcomputers*, LEGAL ECON., May/June 1982, at 52 (discussing new computers on the market).

case to show up later in the AO's records as a business case. Inertia, laziness, or indifference does not lead to random error. Because the default settings direct the case to be counted as a consumer filing, any failure to act means the AO will *always* count the case as a consumer filing. What otherwise would have been random errors are translated into systematic errors.

We examined demonstration versions of twelve different bankruptcy form software packages currently on the market (Figure 6).<sup>52</sup> Based on reviews of this software from legal newspapers,<sup>53</sup> we believe this list represents most of the bankruptcy form software both historically and currently in use. The companies were understandably reluctant to give us estimates of current market share, but two were willing to share general information. One company estimated that 9,000 law firms with a total of 25,000 to 28,000 individual attorneys used its software, and the company's market share was 30-35%. Another company estimated that 6,000 law firms used its software for a market share of around 20%. Together, the combined estimate of market share for these two companies alone was 50-55% of the total market for bankruptcy form software.<sup>54</sup> Presumably, the other nine companies occupy most of the remaining market share. Although these figures were self-reported estimates of market usage, they reinforced our research that we had identified the important bankruptcy form software currently in use.

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52. In addition to the programs listed in Figure 6, we tried but were unsuccessful in contacting Bankruptcy Master to obtain a demo version of its software. See Bankruptcy Master Bankruptcy Software, available at <http://www.bankruptcymaster.com> (last visited May 10, 2004).

53. For examples of reviews of bankruptcy software, see Barry D. Bayer, *Changes in Bankruptcy Law Foster Changes in BFPS: Topform and Best Case Both Get the Job Done*, LEGAL INTELLIGENCER, Apr. 4, 2001, at 6; Barry D. Bayer, *A Review of Latest Round of Bankruptcy Filing Programs Prompted by Form 7*, LEGAL INTELLIGENCER, Mar. 7, 2001, at 9; Joe Borders, *Lawyerware*, TEX. LAW., June 7, 1999, at 38; Laura Gentile, *Running a Law Firm on \$10 a Day*, N.Y. L.J., Mar. 29, 2002, at 16.

54. We acquired this information through emails with company executives and deliberately have not named these companies to protect the confidentiality of their market information. One other company expressly declined to provide any information about market share.

Figure 6: Bankruptcy Form Software Examined

<i>Name of Software Program</i>	<i>Publisher</i>
1. Bankruptcy 2004 (v. 3.7.0)	New Hope Software, Inc.
2. Bankruptcy Case Software (v. 3.03)	Ruth Technology Corp.
3. Bankruptcy, Esq.	Cerenade, Inc.
4. Bankruptcy Plus (v. 4.21) Group	Cornerstone Computer
5. BankruptcyPRO (v. 6.2)	LegalPRO Systems, Inc.
6. Best Case Bankruptcy (v. 12)	Best Case Solutions, Inc.
7. Blankrupter (v. 3.0)	Blumberg Excelsior, Inc.
8. Chapter 7..13 Form Software (v. 3.01)	WestGroup
9. Collier TopForm Bankruptcy (v. 6.5)	Matthew Bender
10. EZ-Filing (v. 11.0.070)	EZ-Filing, Inc.
11. Fresh-Start Bankruptcy	Seaview Software, Inc.
12. WBank4 (v. 4.53)	Puritas Springs Software

At the same time as the emergence of new bankruptcy filing programs in the mid-1980s, the AO's yearly reports began demonstrating a decline in business filings. Business filings peaked in 1985 at 18.3% of all bankruptcy filings and have declined every year since then.<sup>55</sup> Interestingly, two of the software products we examined (BankruptcyPRO and West's Chapter 7..13 Form Software) were first available in 1985, and another (Collier TopForm) was first available in 1988.<sup>56</sup> More programs, including some of the most popular programs, became available in the early 1990s (in 1991, Best Case; in 1993, EZ-Filing; and in 1993, the predecessor version of Bankruptcy 2004), when business filings began to decline dramatically.<sup>57</sup>

Of the twelve filing programs we examined, nine had some sort of default setting that identified bankruptcy filings as consumer cases.<sup>58</sup> Gen-

55. See *supra* Table 1.

56. See *New Products in Brief*, P.C. WEEK, June 21, 1988, at 46 (announcing Collier software); Email from Charles A. Fielder, III, President, LegalPRO Systems, Inc., to Matthew Sarles, Research Assistant to Robert Lawless, Professor of Law, University of Nevada, Las Vegas, William S. Boyd School of Law (Feb. 9, 2004, 09:08:25 PST) (on file with authors); Email from Rose Titus, Sales Representative, WestGroup, to Matthew Sarles (Feb. 9, 2004, 12:45:53 PST) (on file with authors).

57. See Email from Rick Pontalio, Vice President of Operations, EZ-Filing, Inc., to Matthew Sarles (Feb. 6, 2004, 14:45:46 PST) (on file with authors); Telephone Interview by Matthew Sarles with Lucinda Fox, Director of Marketing, Best Case Solutions, Inc. (Feb. 9, 2004); Telephone Interview by Matthew Sarles with Frederick Rogov, President, New Hope Software, Inc. (Feb. 2, 2004).

58. The three bankruptcy programs with no default provisions—Bankruptcy Case Software, Blankrupter, and WBank4—do not account for significant market share. Both the number and the tenor of the software reviews suggest that these are not popular programs, and few official bankruptcy court websites appear to mention these programs in their lists of software to use for electronic case filing.

erally, among the first questions that the programs asked was whether the debtor was an individual and if it was a joint filing. If the user answered affirmatively to either question, the program would then default to identify the case as a nonbusiness case. If the filer was a corporation or other legal entity, the case was marked as a business case. Figure 7 shows the input screens for EZ-Filing, a typical program that used this default system. Three of the nine programs (Bankruptcy, Esq., Bankruptcy Plus, and Best Case Bankruptcy) defaulted to identify the case as a nonbusiness case regardless of how the user identified the debtor. Another program (BankruptcyPRO) did not even contain an option for the user to identify the type of case. In this program, if the user identified the debtor as an individual, the program generated a form automatically identifying the filing as a consumer case, and the converse was true if the user identified the debtor as anything other than an individual.

Figure 7: Default Input Selections for EZ-Filing Software

<i>Debtor Identified as Individual</i>	<i>Debtor Identified as Corporation</i>

Significantly, the increased use of bankruptcy form software coincides almost perfectly with the decrease of business filings as a percentage of all filings. A graph of the decrease in business filings graph looks very much

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Searches on Google for programs using the names of the software programs EZ-Filing, Collier TopForm, and Best Case Software listed 35-40 court websites suggesting the use of these programs. Similar searches listed nine court websites suggesting WBank4, *see, e.g.*, Bankruptcy Petition Software, <http://www.akb.uscourts.gov/ecfq11.htm> (last visited Dec. 8, 2004) (United States Bankruptcy Court for the District of Alaska), eight court websites suggesting Bankrupter, *see, e.g.*, Bankruptcy Preparation Software Packages, [http://www.ndb.uscourts.gov/publicwebcmecf/BK\\_Preparation\\_Software\\_Packages.htm](http://www.ndb.uscourts.gov/publicwebcmecf/BK_Preparation_Software_Packages.htm) (last visited Dec. 8, 2004) (United States Bankruptcy Court for the District of North Dakota), and three court websites suggesting Bankruptcy Case, *see, e.g.*, Petition Preparation Software with CM/ECF Case Data Upload Functionality, [http://www.vtb.uscourts.gov/cmecf/ECF\\_software\\_vendors.html](http://www.vtb.uscourts.gov/cmecf/ECF_software_vendors.html) (last visited Dec. 8, 2004) (United States Bankruptcy Court for the District of Vermont).

like a classic learning curve for the adoption of any new technology. The pattern of the fall, from 18.3% of all cases in 1985 to 2.3% of cases in 2003, mimics the kind of technology adoption curve one would expect to see with a few early adopters in the beginning, a large number of adopters in the middle, and a few late adopters at the tail end.

Our claim is not that attorneys inaccurately categorize each and every bankruptcy case filed with automated form software. Rather, we believe that automated form software has introduced a systematic bias into the reported bankruptcy data. As the filed forms shifted from being filled out by hand to being filled out by computer programs that presumed that individuals were always consumers, the proportion of consumer filings rose while the proportion of business filings steadily declined. This decline in business filings occurred without any relation to macroeconomic factors such as outstanding business debt or business failures, both of which have steadily risen.<sup>59</sup> The rise in the use of form software, along with the common default setting in favor of consumer filings, provides the simplest, most plausible explanation for the dramatic decline in reported business filings.

## II OUR STUDY

The evidence reviewed to this point strongly suggests a systematic undercount of entrepreneurs and small businesses in bankruptcy, but the most direct evidence of an undercount of business filers is gathered by asking the filers themselves. Previous work by one of us (Warren) and her co-authors, Teresa Sullivan and Jay Lawrence Westbrook, estimated that approximately ten percent of the individuals who filed for bankruptcy in 1981 and in 1991 were self-employed at the time of filing and another ten percent were self-employed within the two years before filing.<sup>60</sup> The estimates were only approximate in part because the study focused on individuals filing for Chapter 7 and Chapter 13. Because these studies intended to examine only consumer debtors, they did not include any Chapter 11 cases and excluded all corporations, partnerships, or other business entities that filed under Chapter 7. Because the supposedly declining business filing rates, the official AO figures suggested that there would not be many debtors with primarily business debts in a random sample of people who

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59. In 1990, corporate debt was slightly more than \$18 trillion, and this grew to more than \$49 trillion by 2001. See STATISTICAL ABSTRACT, *supra* note 14, at 488 table 725. This 272% increase in the nominal value of corporate debt far outstrips the 35% increase in overall inflation for the same time period. *Id.* at 463 table 698 (reporting figures for the Consumer Price Index-Urban). For statistics on rising business failures, see *supra* Parts I.A.2.a to I.A.2.b (discussing SBA and D&B datasets).

60. See TERESA A. SULLIVAN, ELIZABETH WARREN, & JAY L. WESTBROOK, THE FRAGILE MIDDLE CLASS 58 (2000) (reporting the 1991 data); AS WE FORGIVE, *supra* note 26, at 111 (reporting the 1981 data).

filed for bankruptcy. The surprisingly high self-employment rates in these previous studies merited further examination when an expanded research team decided to collect data in 2001. Part II describes the results of this more extensive data collection about the self-employed.

#### A. *Methodology*

This Article uses data from Phase III of the Consumer Bankruptcy Project, which builds on two previous empirical studies of bankruptcy conducted by one of us (Warren), Teresa Sullivan, and Jay Lawrence Westbrook. Phase I (the 1981 study) appeared as a book, *As We Forgive Our Debtors*, and Phase II (the 1991 study) appeared as another book, *The Fragile Middle Class*. Phase III of the Consumer Bankruptcy Project was larger in scope than the previous phases of the project and collected data in 2001 from over 1,700 debtors. This Article focuses on the Consumer Bankruptcy Project's data related to the self-employed and entrepreneurs in bankruptcy. Other scholars helped collect the Consumer Bankruptcy Project data and are using these data to study issues relating to family economics, housing policy, women's issues, and other subjects.<sup>61</sup>

In February 2001, we began assembling a core random sample of 1,250 debtors from the federal judicial districts of (1) the Central District of California, which includes Los Angeles; (2) the Northern District of Illinois, which includes Chicago; (3) the Eastern District of Pennsylvania, which includes Philadelphia; (4) the Middle District of Tennessee, which

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61. The Consumer Bankruptcy Project relied on a diverse group of a dozen professors from seven different research universities to design and implement the study, and it is appropriate to credit all of their efforts. Dr. Teresa A. Sullivan, Executive Vice-Chancellor for Academic Affairs of the University of Texas System and Professor of Sociology, Professor Elizabeth Warren, Leo Gottlieb Professor of Law at Harvard University, and Professor Jay Lawrence Westbrook, Benno Schmidt Professor of Law at the University of Texas, took principal responsibility for designing the basic questionnaire and telephone survey. In addition, Professor Michael Schill, then Professor of Law at New York University and Director of the Furman Center for Real Estate and Urban Policy and now Dean at the U.C.L.A. School of Law, and Dr. Susan Wachter, Professor of Real Estate and Finance, The Wharton School, University of Pennsylvania, were principal drafters of survey questions about housing and real estate. Dr. David Himmelstein and Dr. Steffie Woolhandler, both Associate Professors of Medicine, Harvard Medical School, designed the medical questions. Bruce Markell, then the Doris S. and Theodore B. Lee Professor of Law at the University of Nevada, Las Vegas, and now a bankruptcy judge for the United States Bankruptcy Court for the District of Nevada, and Robert Lawless, Gordon & Silver, Ltd., Professor of Law, at the University of Nevada, Las Vegas, drafted the small business questions. Katherine Porter, Visiting Associate Professor of Law at the University of Nevada, Las Vegas, John Pottow, Assistant Professor of Law at the University of Michigan, and Dr. Deborah Thorne, Assistant Professor of Sociology at Ohio University, served, in turn, as Project Director, each with a hand in both the design of portions of the project as well as direct oversight of the data collection. These dozen principal investigators brought expertise from a number of policy areas such as family economics, demographics, employment, health care finance, housing policy, small business, women's issues, law, sociology, business, and economics, as well as specific skills in data collection and analysis. For more details about the Consumer Bankruptcy Project, see ELIZABETH WARREN & AMELIA WARREN TYAGI, *THE TWO-INCOME TRAP: WHY MIDDLE-CLASS MOTHERS AND FATHERS ARE GOING BROKE* 181-88 (2003).

includes Nashville; and (5) the Northern District of Texas, which includes Dallas.<sup>62</sup> The districts were chosen from five different states and encompassed five major metropolitan areas to provide geographic diversity and to take into account different legal cultures. The 2001 core samples were also drawn from some of the same districts as in 1981 and 1991 to maintain some continuity for researchers. In each district, we first randomly selected Chapter 7 and Chapter 13 filers in the same proportion as the numbers of Chapter 7 and Chapter 13 bankruptcies filed in that district. In addition to this core random sample, the Consumer Bankruptcy Project created a supplemental sample of 521 homeowners in bankruptcy from the judicial districts in California, Illinois, and Pennsylvania.<sup>63</sup> Thus, the expanded sample consisted of 1771 debtors. Business entities such as corporations and partnerships were omitted from the sample. All of the debtors are individuals, including individuals filing jointly.

We used three instruments to gather data. The first was a questionnaire that was distributed and collected at the section 341 meetings.<sup>64</sup> For each filer who filled out a questionnaire, we also copied the corresponding court records and recorded detailed data from these documents. Finally, those debtors who indicated on their questionnaires that they were willing to complete a telephone survey were contacted and interviewed. The interviews were conducted by interviewers who were trained in interview techniques and data entry. Each debtor who completed an interview was paid fifty dollars.

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62. For further elaboration of why we chose these particular districts, see *id.* at 182-83.

63. A separate part of the Consumer Bankruptcy Project examined the relationship between housing, mortgages, and bankruptcy. Toward this end, the research design included supplementary collections of homeowners in bankruptcy, drawn from Los Angeles, Chicago, and Philadelphia. The files in the supplemental homeowners sample were drawn at random from the case files in those bankruptcy courts.

Because the supplemental homeowners sample is heavily weighted toward Chapter 13, we were concerned this might skew our results, but that did not turn out to be the case. In the telephone interviews, the incidence of persons reporting self-employment in the supplemental homeowners sample was 12.9%, as compared to 13.8% in the core random sample. The difference is not statistically significant (chi-square = 0.134,  $p = 0.715$ ). The same was true for persons reporting self-employment on the questionnaires, which was 17.6% for the supplemental homeowners sample, as compared to 17.3% in the core random sample (chi-square = 0.018,  $p = 0.893$ ).

Excluding persons from the supplemental homeowners sample would not change our results, but including these persons allows for larger sample sizes and correspondingly more powerful quantitative analysis. Therefore, we have included in this Article persons who were part of the supplemental homeowners sample.

Within Phase III of the Consumer Bankruptcy Project, other researchers surveyed and interviewed 449 additional debtors as part of a study of Iowa and Tennessee rural debtors. These 449 additional debtors are excluded from all calculations in this Article.

64. The United States trustee convenes a section 341 meeting, also called a "first meeting of creditors," shortly after the start of a bankruptcy case. See 11 U.S.C. § 341 (2000). At that meeting, creditors may question the debtor. In actual practice, it is uncommon for creditors to appear at the section 341 meeting. The bankruptcy judge does not preside over or even attend the section 341 meeting.

Because the study was designed to draw debtors into the sample only if they were willing to complete a questionnaire, we have questionnaires for every debtor in the sample. This data-collection technique introduces a possible bias in the sample: it could be possible that people who were willing to fill out questionnaires share a tendency toward certain characteristics. Applied to this study, for example, it might be possible that business owners were systematically more (or less) likely to fill out questionnaires than other filers. Such systematic biases are difficult to detect. Moreover, we cannot think of a reasonable hypothesis why business debtors might be more likely to complete the questionnaire. To the contrary, persons with businesses tended to have bigger bankruptcy cases, meaning they were perhaps busier at the courthouse with their attorneys and with the creditors. If anything, they would seem to be less likely to take the time to complete a questionnaire. Although we do not believe this bias is present in our sample, if it were, it would actually mean our data would have been biased against finding persons with businesses. Our data would thus represent a conservative estimate of the number of entrepreneurs in bankruptcy.

Court records were publicly available, so we also have court records for 100% of the debtors in the sample. The total number of debtors for whom we have telephone interview data relating to self-employment is 911, for a response rate of 51.4% of all debtors who completed a questionnaire. Because debtors sometimes skipped answers in the questionnaire, in their court records, or in their telephone interviews, the number of observations for each data point may vary somewhat. For clarity, we report the number of valid responses separately for each data run.

### *B. Our Count*

In this Part of the Article, we present our findings about the rate at which the debtors in our study report self-employment. First, we report far higher rates of self-employment among bankrupt debtors than the official AO statistics would indicate. Our reported rates of self-employment come from three sources: the debtors' questionnaires, telephone interviews, and court records. Because we used three sources, we next compare and reconcile the rates of self-employment reported from these various sources. We also analyze the rates of self-employment we find and compare those rates to the count of business filers that the AO would report from the exact group of debtors we studied. Finally, we examine the small number of persons in our study who checked the cover-sheet checkbox to indicate the business/nonbusiness nature of the case and compare those figures to the official reports of business filers for the same districts from the same time period. We conclude that it is likely that the business filings currently reported by the AO are largely limited to legal entities such as corporations and partnerships, omitting many debtors who are self-employed.

### 1. Rates of Self-Employment

Table 2 reports the rates of self-employment from our study and compares the official AO count of how many debtors checked the business/nonbusiness box on the voluntary petition with the indicia of self-employment present in the court records, questionnaires, and interviews in the Consumer Bankruptcy Project study. The conclusion is unmistakable: to identify business debtors, it is essential to go beyond the checkbox on the statistical cover sheet.

Table 2: Indicia of Self-Employment Compared to Official AO Data

	<b>Combined Chapters 7 &amp; 13</b>	<b>Chapter 7</b>	<b>Chapter 13</b>
<i>Checked Box as Business Filers</i>			
AO data <sup>a</sup>	1.8%	3.3%	0.8%
Consumer Bankruptcy Project <sup>b</sup>	0.5%	1.1%	0.2%
<i>Reported Self-Employment</i>			
Questionnaire <sup>c</sup>	17.4%	16.9%	17.8%
Interviews <sup>d</sup>	13.5%	14.1%	13.1%
<i>Petition Data Relating to Self-Employment</i>			
Statement of Financial Affairs Business Owner <sup>e</sup>	4.9%	6.3%	3.7%
Reports Schedule I Business Income <sup>f</sup>	3.3%	2.8%	3.7%
<i>Any Indicia of Self-Employment in Questionnaire, Interview, Statement of Financial Affairs, or Schedule I<sup>g</sup></i>			
	19.5%	19.3%	19.7%

<sup>a</sup> five districts in CBP, including corporate and individual filers

<sup>b</sup> individual filers only, N = 1771

<sup>c</sup> individual filers only, N = 1763

<sup>d</sup> individual filers only, N = 911

<sup>e</sup> individual filers only, N = 1733

<sup>f</sup> individual filers only, N = 1771

<sup>g</sup> individual filers only, N = 1771

The AO data reported in Table 2 are for the first quarter of 2001 and include only Chapter 7 and Chapter 13 filings for the same five districts we studied, replicating the time period and cases involved in our study. The first two rows compare the proportion of debtors who identified themselves

as business debtors in the bankruptcy petition checkbox. The AO reported that, when it combined all debtors (corporate and individuals), the proportion of those that were business bankruptcies in Chapter 7 was 3.3%. In Chapter 13, where only individuals may file,<sup>65</sup> the AO reported a business filing rate of only 0.8%.<sup>66</sup> In our data, the individuals (no corporations) checking off the business designation boxes were 1.1% and 0.2% for Chapter 7 and Chapter 13, respectively.<sup>67</sup>

The next two rows in Table 2 compare two types of debtor self-reports from our data. In the questionnaire we asked whether the debtor or joint petitioner was self-employed, either at the time of filing bankruptcy or within the preceding two years.<sup>68</sup> As Table 2 shows, we found significantly higher percentages of debtors reporting self-employment than the official AO data would suggest. Overall, 17.4% of all debtors in our sample reported self-employment on the questionnaire. We asked a similar question in the telephone interviews, and 13.5% of the debtors said they were self-employed.<sup>69</sup>

The fifth and sixth rows report the proportion of debtors for whom court records indicate the debtor has operated a business. The court records are the Statement of Financial Affairs (Form 7), in which debtors identify themselves as officers or managing executives of a corporation, partnership, or sole proprietorship, or as a self-employed professional, and the Current Income of Individual Debtor(s) (Schedule I), on which debtors must report income from a business at the time of filing. Although both the Statement of Financial Affairs and Schedule I are court records, they are not the documents used by the AO to identify business filers. The AO uses the checkbox on the statistical cover sheet and thus our count from the Statement of Financial Affairs and Schedule I is different than the AO's count. Only 4.9% of the debtors on the Statement of Financial Affairs and 3.3% on Schedule I gave an indication in the court records that they owned a business or had business income. These figures were far fewer than those who told us they were self-employed, but far more than the proportion identified by the AO as business filers.

If it were possible, examining the debts reported in the bankruptcy schedules would allow the most direct comparison of our data with the AO figures on business filings. After all, the official AO distinction between

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65. See 11 U.S.C. § 109(e) (2000).

66. We compiled the AO's data from its press release for the first quarter of 2001, which is available at [http://www.uscourts.gov/Press\\_Releases/301f2\\_3.xls](http://www.uscourts.gov/Press_Releases/301f2_3.xls) (last visited Dec. 8, 2004).

67. See *infra* Part II.C for a discussion of why the Consumer Bankruptcy Project's compilation of checkboxes might differ from the AO's compilation.

68. On the questionnaire, the precise question was, "At any time during the past two years, were you self-employed?" The question was asked of both the primary debtor and any joint petitioner.

69. See *infra* n.71 and accompanying text for a discussion of the differences between the questionnaire and the interview statistics.

business and nonbusiness cases rests on whether the debts involved in the case were primarily of a business or nonbusiness nature. One would simply add up the debts related to a business in the bankruptcy schedules, decide if the business debts predominate over nonbusiness debts, and compare those calculations to the AO figures. Unfortunately, the bankruptcy schedules do not require a sufficient amount of detail to reveal whether any particular debt arose from the operation of a business. Ronald Mann has explained that many small businesses now finance themselves with credit cards.<sup>70</sup> An American Express card balance could represent a personal vacation or equipment for a business just as a second mortgage could represent cash sunk into home improvements or into a business venture. Even if it were possible for researchers to know for what purpose a particular debt had been incurred, they would still not necessarily have an accurate picture of the debtor's financial circumstances. A family might pay for groceries and utilities with credit cards while every penny of revenue from the fledgling business was being reinvested in inventory and supplies. The line between personal and business debt for an entrepreneur trying to get a small business off the ground may be so blurred that any subsequent effort to segregate the debt is doomed. Indeed, this observation may explain why using debt as the basis for declaring whether a case was a business bankruptcy became so prone to error.

Without a detailed debtor balance sheet, we turn to what the debtors themselves say about their filings. The debtors report themselves as self-employed far more often than they checked the official boxes. In our sample, only 0.5% of the debtors checked the box on the cover sheet to say they were business filers, but those same debtors were about twenty-five to thirty-five times more likely to describe themselves as currently or recently in business. The first conclusion is inescapable: the AO data are vastly undercounting the number of bankruptcies involving failed or failing small businesses.

## 2. *Reconciling the Different Counts of Self-Employment*

The magnitude of the undercounting must still be determined. However, we must first explain the difference in the reports between the 17.4% self-employment reporting rate in the written questionnaires and the 13.5% rate in the telephone interviews. The wording of the two questions was very similar and designed to elicit the same responses, so we had expected a similar response to either the questionnaire or the interview.<sup>71</sup> An expla-

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70. See Ronald J. Mann, *The Role of Secured Credit in Small-Business Lending*, 86 GEO. L.J. 1, 14-15 (1997).

71. The written questionnaire asked the question quoted *supra* note 68. The telephone interviewers asked two questions:

nation for the difference may be that the debtors filling out the written questionnaires had a greater opportunity to shape their answers without challenge. A person who is out of money, out of work, and out of options may be more willing to list “self-employment” on a questionnaire than a person in a telephone interview who knows that a detailed series of follow-up questions about his or her small business will follow. Of course, the promise of follow-up questions has its own downside: even a debtor who had operated a failed business might realize the wisdom of reporting to a telephone interviewer that there was no business. When the interviewer asked whether the debtor had operated a business, a debtor who simply said “no” was able to skip an entire section of the telephone survey and complete the interview in substantially less time. Payment was the same regardless of the number of subject areas probed.

Regardless of which insight is correct, we are confident that the telephone interview establishes the minimum number of self-employed individuals in bankruptcy because the series of follow-up questions about the business would have quickly exposed anyone who was merely looking for a better description of persistent unemployment. We also cannot determine with certainty whether we also received some strategic “no” responses from debtors who did not want to sit through a longer, more probing interview. The results are consistent with our hypotheses. In the telephone interviews, 13.5% of the debtors reported self-employment at filing or within the previous two years, a figure somewhat lower than the 17.4% reporting self-employment on the written questionnaires. From this we conclude that at least 13.5% of our sample was self-employed, and that this number might be as high as 17.4%.

The court records outside the check box also indicated misidentified business debtors, albeit at considerably lower levels than in the questionnaires and interviews. There are two places in the court records where we also looked for a debtor to indicate self-employment. The Statement of Financial Affairs asks all debtors to state whether they are “in business,” which is defined as the following:

An individual debtor is “in business” for the purpose of this form if the debtor is or has been, within the six years immediately preceding the filing of this bankruptcy case, any of the following: an officer, director, managing executive, or owner of 5 percent or more of

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1. The following questions focus on issues of self-employment. At the time you filed for bankruptcy, were either you or your spouse or partner self-employed or did either of you run your own business, either full-time or part-time?
  2. Within the past two years, in either 1999 or 2000, were either you or your spouse or partner self-employed or did you run your own business, either full-time or part-time?

We considered persons who responded they were in “partnership” with someone to have been running a business. If the respondent answered affirmatively to either of these questions, the interviewers then asked a series of follow-up questions about the business’s start-up, organization, and financial circumstances.

the voting or equity securities of a corporation; a partner, other than a limited partner, of a partnership; a sole proprietor or self-employed.<sup>72</sup>

Under this definition, 4.9% of all debtors in our study identified themselves as “in business.”<sup>73</sup> The instructions for the Statement of Financial Affairs suggest a more formal status to be considered in business rather than the more direct and straightforward inquiries about self-employment asked in our questionnaires and interviews. It is possible that people who have somewhat smaller and less complex businesses believed the Statement of Financial Affairs was inapplicable to their circumstances even if they described themselves as self-employed in response to the interviews or questionnaires.

A second place in the court records where it was possible to identify potential business filers was Schedule I, where the debtor is supposed to list current income.<sup>74</sup> This form directs debtors to identify income from a business, including income from a business operated by a spouse.<sup>75</sup> Schedule I, however, only reports income from a business operated at the time of the bankruptcy filing. Because Schedule I asks only about current income, it necessarily understates the number of persons in bankruptcy who, in the period leading up to bankruptcy, had received income from a business that has since closed. In our interviews, self-employed debtors were much more likely than other filers to cite “job problems” or “failure of employer’s business” as reasons for the bankruptcy filing, suggesting the undercount here would be substantial. In our study, 3.3% of debtors disclosed current business income either for themselves or a spouse.

The formality and structure of the questions in the official court records tend to discourage debtors from self-identifying as business filers. Even so, the number of debtors identifying as business owners in the Statement of Financial Affairs or reporting business income on Schedule I dwarfs the number of debtors in our sample who checked the cover-sheet box as being business filers. Of the eighty-four people who identified themselves as business owners in the Statement of Financial Affairs, only three checked the business classification box on the petition; the rest were all listed as nonbusiness cases. Of the fifty-eight debtors who reported business income, only one marked a business filing on the petition. As a percentage of all persons in our database, more than nine times as many people identified themselves as business owners (4.9%) on the Statement of Financial Affairs and more than six times as many debtors reported

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72. OFFICIAL BANKR. FORM 7.

73. See *supra* Table 2.

74. OFFICIAL BANKR. FORM 6, Sched. I.

75. *Id.* (directing debtor to identify all income of a spouse in all joint cases and for all Chapter 12 or 13 cases regardless of whether the income is individual or joint).

business income (3.3%) on Schedule I as the number who checked the petition box to identify as a business filer (0.5%).<sup>76</sup> Even the court files themselves suggest that the AO data are missing many business filers.

Theoretically, the AO data from the business/nonbusiness checkbox might be consistent with the court records in our study, but this theory bumps up against the hard reality of the numbers described above. The petition checkbox asks about business debt, the Statement of Financial Affairs asks about business ownership, and Schedule I asks about business income. One could theorize that a debtor might own a business or have business income without necessarily having business debt, or vice versa. This theory seems implausible against the numbers. For the AO data to be consistent with other indicia of an underlying business in the same court records, only one of every six to nine filers with either business income or business ownership would have to be entering bankruptcy with predominantly business debts. The remaining persons with business income or business ownership would have to be entering bankruptcy with predominantly nonbusiness debts. Conversely, there would need to be people entering bankruptcy with predominantly business debts but who cannot report any business income or business ownership, even though the ownership question on the Statement of Financial Affairs reaches back six years. Certainly, these situations might occur, but it is highly unlikely they are occurring often—much less at the high levels necessary to make the AO data consistent with the court records. A more likely and simpler explanation is that the AO checkbox, and therefore the official AO reports on total business filings that rely on the checkbox, is an unreliable indicator of whether the bankruptcy involves a business.

In summary, our data have four places that can be used to indicate whether a debtor was an entrepreneur and to provide a point of comparison with the debtor's response with the petition checkbox. In the two official court records, 3.3% of the debtors reported on Schedule I current business income at the time of filing, and 4.9% of the debtors indicated on the Statement of Financial Affairs that they were either an officer or managing executive of a corporation or partnership, a sole proprietor, or a self-

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76. Of the 1771 cases in the full database, there also were six debtors who checked the box to identify as business owners, but who did not indicate business ownership on the Statement of Financial Affairs or business income on Schedule I. Of these six debtors, one reported self-employment on our questionnaire and in our interview.

The other five debtors had no indicia of self-employment anywhere in the court records, our questionnaire, or our interview, and they likely should have been classified as nonbusiness debtors. These five debtors constituted less than 0.3% of our sample. Looking at their records and answers to our questions, it appears the business characterization was a mistake, and these five persons likely should have indicated a nonbusiness filing in the petition checkbox. There was one additional debtor who said he or she was a business filer but indicated neither business ownership on the Statement of Financial Affairs nor business income on Schedule I, yet indicated in both the questionnaire and interview that he or she was self-employed at the time of bankruptcy.

employed professional. In our telephone interviews, 13.5% indicated self-employment at the time of filing or within the previous two years. Answering a similar inquiry on a written questionnaire, 17.4% of the debtors indicated self-employment. There were many overlaps, of course, with some debtors indicating in two, three, or all four places that they were self-employed. In total, 19.5% of the debtors had at least one of the four indicia for self-employment—compared with 0.5% of those whom the AO data would have classified as business debtors in the cases we sampled.

Our evidence suggests the AO figures vastly undercount the percentage of persons in bankruptcy with a failed business. In the AO's nomenclature, every debtor in our sample ended up in either the business or nonbusiness category. Despite evidence in our questionnaires and telephone interviews and in court files, 98.6% of the debtors in our sample who had some indicia of owning a business ended up in the AO data as nonbusiness cases.

### 3. *Who Are the Administrative Office's Business Filers?*

Because we have court records for every debtor in our study, we can look directly to discover whether the debtors in our study identified themselves as business filers in the cover-sheet checkbox. The AO reports district-level data for business filings every quarter, meaning we could compare the rate of debtors checking the box as business filers in our study against the rate the official AO figures report.

The petition checkbox reports for our data differ significantly from the official AO reports for the same districts and same time we studied. Of the 1771 debtors in our study, only nine checked the box to identify themselves as business debtors, yet the AO reported higher percentages of business debtors in the five judicial districts during the same period. It was the same checkbox, but we found far fewer debtors had checked it than would be expected based on a random sample if the AO data were accurate. The possibility that the differences between our checkbox data and the AO checkbox data are due to random chance is highly unlikely. Given the ratio of cases in the AO data that had checked the business filing box, the odds of our randomly selecting only nine such cases for our sample is less than one-thousandth of one percent.<sup>77</sup> To give some sense of comparison, we had approximately the same chance of having a coin toss come up heads twenty-two times in a row as we did of randomly drawing only nine business cases in our sample.

Rather, the difference between our sample and the AO data likely represents a real distinction between the two data sets, and an obvious dif-

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77. To be more precise, given the ratio of business cases in the overall population according to the AO, the approximate binomial probability of us finding only nine business filers in a random sample is 0.0003%.

ference presents itself as a candidate for the explanation. The Consumer Bankruptcy Project includes only individual debtors in the sample, while the AO data includes both individual and corporate debtors. The AO makes no distinction whether the debtor is a live human being, a partnership, a corporation, or other legal entity. Instead, the AO catalogs only whether the case is a business or nonbusiness filing.

These data suggest that the majority of business bankruptcies reported by the AO in Chapter 7 are in corporate or partnership form. During the same time, the AO reports that 3.3% of all Chapter 7 debtors in our five-district target group are business filers,<sup>78</sup> and our data show that only about 1.1% of the individuals in Chapter 7 check off the business filing box. As with the overall figures, it is again highly unlikely that the Chapter 7 figures occurred by chance, with less than a one-thousandth of one percent chance that the difference happened randomly. Rather, these data suggest that as much as the remaining 2.2% of the AO report is likely made up almost entirely of corporations, partnerships, or other legal entities that were excluded from our sample.

Another way to understand these data is to note that as many as two of every three Chapter 7 cases denominated by the AO as a business case is a corporation or partnership. If the five districts we studied can be extrapolated to the nationwide filing rate, this means that in 2001 up to 20,000 corporations, partnerships, and the like filed for Chapter 7 bankruptcies. These are not conversions from failed Chapter 11 filings, but initial filings in Chapter 7 by legal entities. This is particularly noteworthy because conventional wisdom holds that corporations have no reason to file for Chapter 7 because they are ineligible for discharges and can simply dissolve without further liability. These data suggest that small corporations and other business entities are somehow finding reasons to file for liquidation—reasons that escape the standard story of business failure.<sup>79</sup>

The software programs, with their built-in, default presumptions that individuals are nonbusiness filers and legal entities are business filers, help to obscure that trend. Recall that the software programs default to a consumer filing for individuals, but default to a business filing for corporations. Because the petition's checkbox appears to distinguish individual

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78. We compiled the AO data from its press release for the first quarter of 2001, which is available at U.S. Bankruptcy Courts, Business and Nonbusiness Bankruptcy Cases Commenced, by Chapter of the Bankruptcy Code, During the 3-Month Period Ending March 31, 2001, at [http://www.uscourts.gov/Press\\_Releases/301f2\\_3.xls](http://www.uscourts.gov/Press_Releases/301f2_3.xls) (last visited Mar. 23, 2005).

79. Thus, our findings reinforce the findings in Elizabeth Warren & Jay L. Westbrook, *Financial Characteristics of Businesses in Bankruptcy*, 73 AM. BANKR. L.J. 499, 532-33 (1999) (reporting significant numbers of corporate and other legal entities liquidating in Chapter 7). That study found 294 Chapter 7 cases involving corporations or other legal entities in a database that included individuals who filed for Chapter 7 either checking the box as a business filer or who filed with a "doing business as (d/b/a)" or similar designation, if the latter was a business style. *Id.* at 512. Even with such a broad sample selection, corporations still accounted for 25.9% of all the Chapter 7 filers. *Id.* at 533.

filers from legal entities rather than represent a real distinction between filers with primarily business or consumer debts, the filing preparation programs that are producing a sharp undercount of business bankruptcies seem to be also concealing a remarkable number of corporate Chapter 7 cases.

Of course, this effect should not occur in Chapter 13 cases because legal entities are not eligible for relief in that chapter.<sup>80</sup> For the districts we studied, the AO showed only a paltry 0.8% checked the box as business filers, but we found only 0.2% of our Chapter 13 debtors had checked that box. Frankly, we are at a loss why we should have found fewer Chapter 13 debtors checking the box than the AO data would indicate. Because we had 979 Chapter 13 debtors in our sample, the chance of this difference occurring randomly was actually quite small, around 2.8%. These are slightly worse odds than the chance of flipping heads five consecutive times on a coin (which is around 3.1%). Thus, although the difference does not approach a mathematical impossibility, it is still well within the conventional level of 5% for a statistically meaningful result. This difference in counts of the checkboxes between the AO data and apparently random samples merits further study.

### C. *How Many Business Bankruptcies?*

If the AO's official numbers are inaccurate, as we believe, how many cases in the bankruptcy system more appropriately should be classified as business debtors? To generalize from our data requires some assumptions about the national representativeness of the sample. The five court districts in our study vary widely in the percentage of people who report self-employment in the questionnaire or interviews or whose court records have indicia of business ownership or income. The official AO data also vary from district to district in the reported percentage of business filers around the country. On the other hand, the five districts in our study were selected for their representativeness of the nation as a whole, and taken together, the five districts approach the national average for the AO's official numbers on business filings.<sup>81</sup> Therefore, it is not unwarranted to generalize from our figures so long as it is done with caution and the understanding that it is only an approximation.

It is probably best to think about the actual number of business debtors as a range of estimates. The rigid and formal definition in the Statement of Financial Affairs, which by its own terms eliminates many failing small businesses,<sup>82</sup> produced 4.9% of debtors identifying as owning a business—

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80. See 11 U.S.C. § 109(e) (2000).

81. For more details on why these five districts were selected, see WARREN & TYAGI, *supra* note 61, at 182-83.

82. See *supra* note 72 and accompanying text.

still more than double the AO data for the same time period and same districts. The rigid and formal definition of business ownership in the Statement of Financial Affairs provides our most reliable low-end estimate of the percentage of business filers.

Our most reliable high-end estimate comes from the questionnaire, where 17.4% of debtors said they were self-employed at the time of filing or during the two years before.<sup>83</sup> Almost none of these debtors checked the box as business filers,<sup>84</sup> meaning the AO would not have recognized them as business bankruptcies. Applied to the national figures for 2003,<sup>85</sup> our questionnaire data would mean there were approximately 280,000 more bankruptcies that had a significant relationship to an underlying business than the AO reported.

Of course, in addition to these bankruptcies, there were the business filings that the AO already recognized. In 2003, that number was about 37,000 and includes the Chapter 11 and Chapter 12 filings that were not a part of our study because we chose to focus on the chapters studied in previous phases of the Consumer Bankruptcy Project. The AO counts all Chapter 12 cases as business filings. Although there is some evidence to suggest that the AO undercounts Chapter 11 business filings,<sup>86</sup> we will take the AO data at face value because that assumption will produce conservative estimates of the true number of business filings. Adding the numbers already reported by the AO as business filings to the data from our questionnaires results in perhaps as many as 315,000 bankruptcy filings involving a business in 2003. Putting the AO's business filings with our low- and high-end estimates would mean that of all 2003 bankruptcies, between 6.1% and 18.6% involved a business.

As with many things, the truth probably lies somewhere in between the extremes of the estimates from the Statement of Financial Affairs and the estimates from the questionnaires. In between these two estimates lies the 13.5% figure from our interviews. Again, virtually none of these debtors checked the cover-sheet checkbox to indicate they were business filers, so they would not have been included in the AO's count of business bank-

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83. We are not using the 3.3% of persons who reported business income on Schedule I because that number includes only persons who were receiving a business income at the time of filing bankruptcy and would exclude persons whose businesses shut down shortly before bankruptcy. Similarly, we are not using as a high-end estimate the 19.5% who had some indicia of self-employment anywhere in our data. That number likely overstates the number of self-employed, including, for example, persons who responded during the interview that they were self-employed but answered differently on the questionnaire.

84. See *supra* notes 74-76 and accompanying text.

85. Again, we are using data for the twelve-month period ending June 30 because it allows comparability with pre-1980 government data. See *supra* note 7.

86. See Fenning & Hart, *supra* note 48, at 126-27 (explaining that the data's accuracy remains entirely dependent upon self-reporting by the debtor or whoever fills out the form for the debtor); Frasier, *supra* note 30, at 352 (reporting accuracy rates for data on cover sheets).

ruptcies. For 2003, using the 13.5% figure would mean there were an additional 222,000 bankruptcies involving businesses than the AO data indicate. Added to the 37,000 filings the AO did recognize, there would have been 259,000 business bankruptcies, and bankruptcy filings would have been 15.7% of all filings instead of the 2.3% that the AO data reported. We consider this number to be our most reliable, conservative estimate of debtors who were in bankruptcy with debts from a failed business. This estimate is much closer to historical trends before approximately 1985-86, when we suspect the AO data began to lose touch with the underlying reality of what they purported to measure.<sup>87</sup>

It bears repeating that our estimate is only an approximation. Though the AO data undercount business bankruptcies by a huge margin, it is impossible to pinpoint the magnitude of the undercount. Moreover, the concept of a business bankruptcy can be quite elastic. Is a business bankruptcy one in which the debtor owns a business, has substantial income from a business, has debts from a business, or a combination of these and other factors? Regardless of where one draws the line between business and nonbusiness, the evidence points toward one inescapable conclusion: as both an absolute number and a percentage of total filers, there are many more people in bankruptcy with business problems than the AO data indicate.

### III

#### IMPLICATIONS AND FUTURE DIRECTIONS

Because the official data have marginalized entrepreneurs' participation in the bankruptcy system, the Conventional Story has diverged sharply from the real world of financial failure. Despite confident assumptions to the contrary, business filings remain a part of the bankruptcy system in roughly the same proportion as they have for decades. In this Part of the Article, we focus on what our findings might mean for our understanding of the business climate generally and for how the bankruptcy system treats businesses specifically.

The effects of inaccurate data are significant. Our findings undermine the narrative of the U.S. bankruptcy system as dealing with only two kinds of debtors: consumers and corporations. Entrepreneurs are in bankruptcy court in substantial numbers, even though the current classification system conceals most of them. The failure to consider the special needs of entrepreneurs echoes throughout the bankruptcy system and the specific bankruptcy reform proposals that have been introduced in recent years. Moreover, because the AO data provide the only available information on the number of business bankruptcies, government officials and academics

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87. See generally *supra* Table 1 and note 14 and accompanying text.

have relied on these data, gently seduced into painting a rosier picture of the business climate than is warranted.

A. *The Conventional Story as the Dominant Narrative*

As we noted in the Introduction, the dominant narrative about the rising bankruptcy filing rate is the overspending consumer.<sup>88</sup> Indeed, the need for bankruptcy reform is repeatedly justified because the rise in consumer bankruptcies accompanied by the decline in business bankruptcies supports a story of overconsumption.<sup>89</sup> If businesses are flourishing and only consumers are in trouble, the story goes, then it must be consumer misbehavior, not deteriorating economic conditions, that account for the rise in bankruptcy filings. Instead, our data show that consumer bankruptcies and business bankruptcies have risen together, and each continues to constitute roughly the same proportion of total bankruptcy filings as they have since at least World War II. If changes in consumer attitudes have driven the rising bankruptcy rate for nonbusiness,<sup>90</sup> then business bankruptcies must have risen for a different reason. For the story of the overspending consumer to make sense, there must be a different explanation for rising business filings that coincidentally led to a similar increase in filings. Alternatively, one must argue that we know what caused the increase in nonbusiness filings but mysteriously have no explanation for the increase in business filings. A simpler, more direct explanation is that the rising bankruptcy rates for both nonbusiness and businesses stem from underlying social phenomena that are common to both.

The overspending story does not make much sense in the context of the failure of small businesses. Businesses exist to make a profit, not to consume. Business owners may make errors in judgment about their ability to repay a debt, but businesses do not overspend for the sake of consumption. Rather than focusing on the demand for credit, as the overspending story does, a different explanation might focus on the supply of credit. The expansion of easy credit and a move from secured to unsecured lending have made more debt more available for more businesses and consumers alike.<sup>91</sup> Loans that would have been inaccessible in the past are now readily available as lenders have spent millions of dollars marketing loans so that they could increase their loan portfolios. Loaded down with more debt, both families and businesses are more vulnerable to economic dislocation.

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88. See *supra* notes 3-5 and accompanying text (citing academic articles, statements from members of Congress, and industry lobbyist claims that overspending consumers largely drive the bankruptcy filing rate).

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

90. See Buckley & Brinig, *supra* note 1; Jones & Zywicki, *supra* note 1.

91. See Mann, *supra* note 70, at 37-40 (presenting evidence that small business lending has shifted from secured to unsecured lending).

The explosion of debt held by both consumers and businesses would provide a common explanation for similarly rising bankruptcy filing rates.

In an absolute sense, nonbusiness filings have grown dramatically over the past twenty years, but the growth in nonbusiness filings has been matched by a similar growth in business filings. Instead of providing a business/nonbusiness distinction, however, the official AO categories increasingly have become a distinction between people and legal entities such as corporations and partnerships. Today, entrepreneurs and self-employed people have been swept up with wage earners, officially classified as nonbusiness filers even when the failure of a small business is at the heart of many of these bankruptcies. If the data had always reflected a person/corporate distinction, then the trend lines over time would be useful, but the changing classification of entrepreneurs from the business to the nonbusiness column has produced a startling distortion in any comparative trend lines for business and nonbusiness bankruptcies. This finding has obvious implications for those who use the difference in the purported trends between business and nonbusiness cases to indict consumers for their profligate ways.

The undercount of business bankruptcies also would mean that we know a lot less about the consumer bankruptcy system than we previously assumed. A number of scholarly studies relate macroeconomic data to the official statistics on nonbusiness bankruptcy filing rates.<sup>92</sup> To the extent these studies use data after the mid-1980s, when we suspect the undercount first began to appear, these studies rely on data that include substantial numbers of people who would have historically been counted as business filers. In other words, these studies may not tell us much about consumer bankruptcies at all.

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92. See, e.g., CONGRESSIONAL BUDGET OFFICE, PERSONAL BANKRUPTCY: A LITERATURE REVIEW 12-14 (2000), available at <ftp://ftp.cbo.gov/24xx/doc2421/Bankruptcy.pdf> (performing a literature review on studies about bankruptcy filing rates); Lawrence M. Ausubel, *Credit Card Defaults, Credit Card Profits, and Bankruptcy*, 71 AM. BANKR. L.J. 249 (1997) (examining links between credit card delinquencies and bankruptcy filing rates); Jagdeep S. Bhandari & Lawrence A. Weiss, *The Increasing Bankruptcy Filing Rate: An Historical Analysis*, 67 AM. BANKR. L.J. 1 (1993) (constructing econometric model to predict future filing rates based on past filing rates); Buckley & Brinig, *supra* note 1 (attributing run-up in bankruptcy filings to social change); Richard Thalheimer & Mukhtar M. Ali, *The Relationship of Pari-Mutuel Wagering and Casino Gaming to Personal Bankruptcy*, 22 CONTEMP. ECON. POL'Y 420 (2004) (finding no relationship between access to pari-mutuel or casino gaming and bankruptcy filing rates); Lawrence A. Weiss et al., *An Analysis of State-Wide Variation in Bankruptcy Rates in the United States*, 17 BANKR. DEV. J. 407 (2001) (finding economic variables explain state differences in filing rates); Todd Zywicki, *Why So Many Bankruptcies and What to Do About It: An Economic Analysis of Consumer Bankruptcy Law and Bankruptcy Reform*, (George Mason L. & Econ. Res. Paper No. 03-46), available at <http://www.law.gmu.edu/faculty/papers/docs/03-46.pdf> (last visited Mar. 23, 2005) (arguing that societal shifts explain rising bankruptcy rates); Lawless, *supra* note 10 (reconciling Federal Reserve data with bankruptcy filing rates).

Certainly, the macroeconomic reasons for rising bankruptcy filing rates are complex and varied. In this short space, we only can speculate—not establish—why bankruptcy rates have risen so dramatically. One thing is clear, however. The data presented here run counter to the Conventional Story of the overspending consumer. Whatever the reasons for rising bankruptcy rates, these reasons have affected business bankruptcies in the same way that they have affected nonbusiness bankruptcies. Any efforts to address the rising nonbusiness bankruptcy rate also will affect the many small businesses that have been invisible in the bankruptcy system. The next Section turns to whether recent efforts at discouraging bankruptcy filings adequately account for their effects on these businesses.

*B. Integrating the Struggling Entrepreneur into Bankruptcy Reform*

The data reported here provide a nuanced perspective on the role bankruptcy serves in the U.S. economy, but the current paradigms of bankruptcy generally portray only two types of debtors: individual consumers attempting to discharge debts incurred when spending and income fall out of balance and large corporations attempting to reorganize by ending unprofitable business activities and rewriting balance sheets. These paradigms leave no place for the struggling entrepreneur who has predominantly business debt but who also may have both personal liability on the business debt and some consumer debt as well. The data reported in this Article contradict a story of a dichotomous bankruptcy system, composed of corporations and individual consumers. Instead, these data tell a more complex story in which one in seven individuals in the bankruptcy system is a struggling entrepreneur.

Our data are consistent with the picture of entrepreneurs who are trying to cope with their own personal liability on business debts. Regardless of whether they are incorporated, these small businesses may have little or no value without the investment of their owners' human capital. These data are a reminder that the corporate form may protect large businesses, but in small businesses, incorporation may be largely irrelevant if lenders require the entrepreneur to agree to personal liability as a condition of lending.

Because the story now in vogue states that the bankruptcy system processes almost exclusively nonbusiness cases with declining business participation, proposed legislative changes generally treat the person who files for bankruptcy monolithically as a consumer debtor who has consumer problems. Such heated political debates about irresponsible consumers have little salience for an individual who is in bankruptcy court because her small business suffered financial setbacks. And yet about one in seven bankrupt filers who would be affected by changes in the law is someone trying to cope with the collapse of a small business.

As this Article goes to press, Congress is poised to pass substantial revisions to Chapters 7 and 13 that treat bankruptcy filers as if they are either entirely consumers or entirely businesses.<sup>93</sup> One proposed revision particularly demonstrates how rigidly, and consequently how nonsensically, the proposed bankruptcy revisions treat entrepreneurs. The legislation proposes a statutory definition of a small business debtor as “a person engaged in commercial or business activities.”<sup>94</sup> The definition excludes any case in which the U.S. Trustee has appointed a committee of unsecured creditors.<sup>95</sup> As any bankruptcy lawyer will quickly point out, it is only Chapter 11 where committees of unsecured creditors are appointed,<sup>96</sup> but the definition has consequences outside of Chapter 11. Specifically, any small business debtor would need to file a list of forms, reporting various financial information and profitability, regardless of whether the debtor filed in Chapter 7, Chapter 11, or Chapter 13.<sup>97</sup> Based on our data, this new statutory definition and reporting provision would apply not to the approximately 37,000 bankruptcies officially listed as business cases in 2003, but would cover upwards of 315,000 bankruptcies involving debtors engaged in commercial or business activities, most of which are in Chapter 7 or Chapter 13. Thus, although the bill uses a statutory definition of small business debtor keyed to Chapter 11, the vast majority of cases to which it might apply would be Chapter 7 or Chapter 13 cases.

How could this happen? The huge effect is evidently inadvertent, never mentioned in the legislative debates. We can only speculate, but the tenor of changes that apply to small business debtors presupposes a prototype business reorganizing under Chapter 11.<sup>98</sup> The official AO data reinforce this view, so that apparently little thought was given to the hundreds of thousands of additional cases to which the provision might apply.

Other provisions of the bankruptcy legislation target all individuals,

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93. Compare Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, S. 256, 109th Cong. tit. II (2005) (specifying consumer bankruptcy provisions), with *id.* tit. IV (specifying business bankruptcy provisions).

94. *Id.* § 432(a).

95. *Id.* (excluding also cases with more than \$2,000,000 in debt).

96. 11 U.S.C. § 1102(a) (2000). To be technically correct, we should note that a creditors committee also may be appointed in a Chapter 9 municipal bankruptcy, see *id.* § 901(a) (specifying that § 1102 applies in Chapter 9), but Chapter 9 cases are extremely uncommon.

97. See S. 256 § 434 (adding a new § 308 to the Bankruptcy Code); see also *id.* § 435 (authorizing the Judicial Conference of the United States to propose official bankruptcy forms on which the reporting must take place).

98. See *id.* § 436 (imposing new duties on Chapter 11 “small business cases”); *id.* § 437 (placing new time deadlines on filing of Chapter 11 plans in a “small business case”); *id.* § 438 (imposing plan confirmation deadlines in Chapter 11 cases in a “small business case”); *id.* § 439 (placing new duties on the United States Trustee in a Chapter 11 “small business case”); *id.* § 442 (expanding the grounds for dismissal in a Chapter 11 “small business case”); see also *id.* § 432(a) (creating a new distinction between the definition of “small business debtor,” which applies in all bankruptcy cases, and “small business cases,” which applies only in Chapter 11).

regardless of whether they are wage-earners or entrepreneurs and without reference to the reasons they are in bankruptcy court. Unlike the new statutory definition of a small business debtor, these provisions at least can be coherently applied within the existing statute, but they are overbroad to the extent that they would sweep in consumers and entrepreneurs alike. Before filing a bankruptcy petition, for example, any individual would have to submit to credit counseling.<sup>99</sup> Discharges in Chapters 7 and 13 would be denied to any debtor who did not complete a course in personal financial management.<sup>100</sup> The proponents of the amendments never explained why these steps are necessary for someone whose business operations have failed. Indeed, the proponents never mentioned debtors engaged in business at all, but the provisions would nonetheless require them to spend time and money for courses they do not need. Another provision would require the Director of the Executive Office of United States Trustees to issue schedules of the “reasonable and necessary administrative expenses of administering a Chapter 13 plan.”<sup>101</sup> Uniform fee schedules may work if the bankruptcy docket comprises principally routine consumer cases but not with the substantial percentage of bankruptcy cases involving failed businesses that are likely to present complex legal issues that cannot be captured by such routine approaches.

Overconsumption is the target of still other provisions, such as those expanding the debts presumed nondischargeable because they were incurred to purchase “luxury goods”<sup>102</sup> or limiting the types of “household goods” to which certain types of security interests do not apply.<sup>103</sup> Another example is the so-called means test, which conclusively presumes that a debtor’s pre-filing income would continue post-filing<sup>104</sup>—a circumstance that may be probable for wage-earners, but that is far less likely to be true for a debtor who operates a failing business. Because these provisions would apply to all individuals, whether they are self-employed or not, they needlessly penalize entrepreneurs who are in bankruptcy court not because overconsumption but because a failed business.

Laws designed to deal with consumer credit are not always well suited to the needs of small business owners, including the small business owners who turn to bankruptcy for relief. Nor are provisions designed for medium-sized corporations in Chapter 11 appropriate for tens of thousands of entre-

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99. *Id.* § 106(a) (adding a new § 109(h) to the Bankruptcy Code).

100. *Id.* § 106(b)-(c) (adding new §§ 727(a)(11) and 1328(g) to the Bankruptcy Code).

101. *Id.* § 107.

102. *Id.* § 310 (lowering the amount at which and extending the pre-filing time period during which purchases of luxury goods are presumed nondischargeable).

103. *Id.* § 313 (limiting the definition of household goods upon which nonpossessory, nonpurchase money security interests may be avoided).

104. *See id.* § 102(a) (extensively revising 11 U.S.C. § 707(b) to establish a “means test” to determine eligibility for Chapter 7 relief); *id.* § 102(b) (defining debtor’s current monthly income for purposes of the means test).

preneurs whose more modest operations have collapsed. But policy analysis in the bankruptcy field presupposes only two alternatives: the wage-earning consumer and the corporation. The changes to the Bankruptcy Code illustrate the mismatch between the assumed problems and those who would be affected. Some changes impose a statutory definition that would apply to hundreds of thousands of entrepreneurs who the drafters did not imagine were in the bankruptcy system to exist while other changes sweep too broadly to include entrepreneurs, and still other changes needlessly penalize entrepreneurs who file for bankruptcy.

No one has yet undertaken a systematic analysis of the current law to see how it may perpetuate similar divergences between intent and effect and how those divergences may affect entrepreneurs. The myth of the disappearing business bankruptcy holds the current law in thrall. The bankruptcy system and the major revisions on the way leave entrepreneurs at risk that the laws that govern their efforts to recover from a financial setback simply do not match the circumstances they face.

### C. *Bankruptcy Filing Data as an Indicator of Economic Performance*

Government agencies, policymakers, and scholars use the AO's bankruptcy statistics as a key indicator of business success and failure, but the data reported in this Article undermine the usefulness of the reported numbers. Instead, our data show that there is far more widespread distress in the American economy than agencies, policymakers, and scholars have been led to believe. For example, the Small Business Administration (SBA) has continually cited the declining business bankruptcy filing rate as an indication that the entrepreneurial system is strong and healthy. For a decade, the SBA's annual report to the President has taken note of the ostensibly declining business bankruptcy rate as the report comments on a strong business climate.<sup>105</sup> An SBA official touted the allegedly low corpo-

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105. See, e.g., 2004 OFF. OF ADVOCACY, SMALL BUS. ADMIN., THE SMALL BUSINESS ECONOMY: A REPORT TO THE PRESIDENT 1 (2004) ("The year 2003 was one of transition, as signs of economic recovery began to appear in mid-year. . . . The number of firms grew, and business bankruptcies declined."); 2002-2003 OFF. OF ADVOCACY, SMALL BUS. ADMIN., THE SMALL BUSINESS ECONOMY: A REPORT TO THE PRESIDENT 10 (2004) ("Small businesses also showed signs of a turnaround. The number of businesses that filed for bankruptcy decreased in 2002 to 38,155."); 2001 OFF. OF ADVOCACY, SMALL BUS. ADMIN., THE SMALL BUSINESS ECONOMY: A REPORT TO THE PRESIDENT 1 (2004) ("The number of businesses continued to increase in 2000, and bankruptcies declined for the third consecutive year."); 1998 OFF. OF ADVOCACY, SMALL BUS. ADMIN., THE STATE OF SMALL BUSINESS: A REPORT TO THE PRESIDENT 11 (1999) ("Nineteen-ninety-seven was an excellent year for the economy and for small business. . . . Business bankruptcies remained low for the fourth consecutive year."); 1997 OFF. OF ADVOCACY, SMALL BUS. ADMIN., THE STATE OF SMALL BUSINESS: A REPORT TO THE PRESIDENT 13 (1998) ("Nineteen-ninety-six was an excellent year for the economy and for small business. . . . Business failures and bankruptcies remained low for the fourth straight year."); 1996 OFF. OF ADVOCACY, SMALL BUS. ADMIN., THE STATE OF SMALL BUSINESS: A REPORT TO THE PRESIDENT 13 (1997) ("Nineteen-ninety-five was a good year for the U.S. economy and for small business. . . . The

rate bankruptcy filing rate as evidence that small business activity could pull the country out of recession:

The Bush administration is certainly hoping that small business, defined as companies with 500 or fewer workers, leads the charge, and soon. It's easy to see why. The Small Business Administration noted yesterday that corporate bankruptcies are low and that business owners' income, and corporate profits, rose last year, "giving owners the financial ability to expand their firms." "Small businesses are ready to lead America's economic recovery," says Thomas M. Sullivan, an SBA official.<sup>106</sup>

Testifying before Congress, the SBA Administrator used the declining business bankruptcy rate as evidence that the agency was doing its job and deserved an increase in its annual appropriation.<sup>107</sup> President Clinton referred to the declining business filing rate as evidence that small businesses had been successful under his watch.<sup>108</sup>

It is not only government agencies that have relied on the AO's flawed data. Academic studies have used the AO data and have drawn critical implications from it. Some well-respected scholars have suggested business bankruptcies have all but disappeared from the system. For example, Professors Douglas Baird and Robert Rasmussen claim to have seen a significant shift in the American bankruptcy system: "While the number of large businesses filing for Chapter 11 has increased, the total number of Chapter 11s is only half of what it was 20 years ago."<sup>109</sup> Our data suggest that rumors of the death of business bankruptcies have been greatly exaggerated.

The happy news of the downward trend in business bankruptcies is a myth, an artifact of inaccurate reporting rather than a twenty-year im-

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number of business bankruptcies and failures continued to decline: bankruptcies dropped from 50,845 in 1994 to 50,516 in 1995.").

106. Jeff Bailey, *Small Economic Engines May Not Be Enough: Hopes for Recovery in U.S. Are Pinned on Small Firms, But Can They Handle It?*, WALL ST. J., June 17, 2003, at B5.

107. See *President's FY98 Budget Request for the U.S. Small Business Administration: Hearing Before the Senate Comm. on Small Bus.*, 105th Cong. 11-66 (1997) (testimony of Aida Alvarez, Administrator, U.S. Small Business Administration) ("Small business is healthier today, with failures and bankruptcies declining every year since 1993."); *SBA's Budget for FY98: Hearing Before the House Comm. on Small Bus.*, 105th Cong. 43-62 (1997) (testimony of Aida Alvarez, Administrator, U.S. Small Business Administration) (same).

108. See Message to Congress Reporting on the State of Small Business, 32 WEEKLY COMP. PRES. DOC. 999 (June 5, 1996); Remarks to the White House Conference on Small Business, 31 WEEKLY COMP. PRES. DOC. 1037 (June 12, 1995).

109. Douglas G. Baird, *The New Face of Chapter 11*, 12 AM. BANKR. INST. L. REV. 69, 83 (2004). Professors Baird and Rasmussen have explored this issue primarily in the context of Chapter 11, but they discuss overall business filings. Douglas G. Baird & Robert K. Rasmussen, *The End of Bankruptcy*, 55 STAN. L. REV. 751, 752 (2002) ("For the vast majority of firms in financial trouble, the traditional corporate reorganization has become increasingly irrelevant."). While it is undeniable that there are fewer Chapter 11s than previously, our data indicate businesses still file for bankruptcy in large numbers, disguised as consumer bankruptcies.

provement in reality. The implications of this large error in the data filter through both government and academic reporting, touching on what we know about other aspects of our economy. These data suggest that much of the measurement of the small business economy is simply wrong and that error affects every assessment of the strength, number, and role of small businesses in the United States. From the SBA reports, to academic studies, to the pages of local newspapers,<sup>110</sup> erroneous data about declining business bankruptcies have fostered a faulty picture of the economy.

#### *D. Toward a New Research Agenda*

The data reported here are just a beginning. Their real effect will be felt as they are accounted for in studies and reports about small business and entrepreneurial activity across the United States. Any work that has relied on the relative changes in bankruptcy filing rates over the past two decades is now subject to substantial rethinking, but the potential impact of these data may reach even further.

Is it possible that these data signal a change in the composition of what constitutes a small business? Entrepreneurs can slip into the personal bankruptcy column, which raises the tantalizing question of whether the prototype small business may be changing from a small shop to a consultant. The small shop would have been widely regarded as a business separate from its owner, a discrete entity that might or might not have been incorporated. In contrast, the consultant who continues the same work that was once salaried and has now been outsourced is a very different kind of entrepreneur. Such a person is someone for whom there is no real separation between the business and the self. The personal nature of the bankruptcy is readily obvious. But this person is an entrepreneur nonetheless, dependent for income on the success of a small business, arranging for business loans, dealing with billing and bad debts, and at the mercy of a marketplace that may be slow or uneven. Repayment through Chapter 13, for example, is likely to involve quite different issues for such an entrepreneur than it would be for an employee with a steady income and a budget that involved only personal consumption.

The bankruptcy data reported here also raise the question of what an entrepreneur salvages following a bankruptcy. As more self-employed debtors migrate from the business to the nonbusiness column, it is possible that a growing fraction of small business bankruptcies aims to free up the human capital of the individual debtor instead of saving a separate business. Rather than redeploying the tangible assets of a large business, small business bankruptcy allows the individual debtor to redeploy her human capital in a new venture.

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110. See *supra* note 10 (citing newspaper articles).

The changes in the composition of small businesses in bankruptcy may also suggest an ever-tighter link between the failure of a small business and the failure of its owner. The debts to be dealt with may be largely personal debts, money borrowed to keep the debtor afloat when the income from the business began to falter. Unlike their counterparts with large, clearly separate businesses, small entrepreneurs who falter may have nothing to sell, nothing to offer as collateral, and nothing to cash out. That difference also means there may be nothing for the creditors as well. If there is no business other than the human capital of the debtor, then the creditors have little to liquidate to satisfy their debts. It is only the debtor's personal assets, such as the house, the car, the checking account, that are the target of creditor actions.

In addition, these data open the possibility that the much-praised corporate form may be failing a growing number of entrepreneurs. Once heralded for its ability to shield owners from personal liability, corporate form may be meaningless for someone who operates as a consultant. The debts are all personal debts.

If the business/personal distinction is dissolving for a growing number of small business owners, then other measures of the economy come into question. Is the consumer debt load really about consumption, or is it about entrepreneurs who are floating their micro-operations and their own survival during low-income periods? Is home mortgage debt about buying houses, or does a significant portion of home-mortgage debt represent refinancing activity supporting a struggling self-employed owner? Even data as basic as who is employed and who is unemployed are blurred in a world of out-sourced consultants with erratic incomes.

Other economic shifts in the American economy, such as declining rates of health insurance and increasing hours of work, may be reflected in these revised bankruptcy numbers as well. Small businesses are less likely to offer health insurance to their workers. The difference between being an employee and a consultant may be largely a difference between having health insurance and retirement benefits and having nothing but cash. Hours of work may stretch for the self-employed who must not only do the work as it comes in, but must also manage their own billing, supplies, equipment, taxes, and insurance.

The old boundaries between personal and business may be breaking down and reforming. Perhaps the AO should consider a different form of reporting that more closely mirrors this reality: people/legal entities along one scale, so that the number of humans and the number of corporations, partnerships, and the like can be accounted for and then a separate question to distinguish the wage-earners from the self-employed. Such a form would permit those who want to explore the circumstances of families and individuals in bankruptcy to measure the pool precisely. It would also serve to

highlight the substantial number of entrepreneurs in the bankruptcy system, offering a steady reminder that both bankruptcy policy and general business policy should be crafted with both groups in mind. Of course, any change in reporting would mean that the data from 1978 to the present would be useless for developing trend lines, but, as these data demonstrate, they are so misleading right now as to be largely useless anyway.

*E. A Cautionary Tale about Data Collection*

Finally, our findings tell a cautionary tale for empiricists of any stripe. The mistakes of the business bankruptcy data lie in a technological change that had far-reaching implications that government statisticians failed to detect. The story is simple. The proportion of business filers has dropped dramatically and steadily from the mid-1980s,<sup>111</sup> a drop that coincides with the rise in the automated preparation and filing of bankruptcy court documents. Computer software used by bankruptcy lawyers channeled potential filers into characterizing themselves as nonbusiness debtors, building a systematic bias into the bankruptcy data.<sup>112</sup> Increased reliance on this type of software for preparing bankruptcy filings, coupled with small changes in the wording and administration of an official bankruptcy form,<sup>113</sup> produced a shift in the official government data and gave birth to an erroneous Conventional Story about the basic operation of the bankruptcy system.

The larger message is chilling for researchers of all disciplines. As computers have expanded our ability to collect, transmit, and analyze data, researchers have enjoyed exponentially increasing access to information. But our findings suggest that the very tools that have made these information gains possible have also made it possible to build substantial and undetected distortions in the official data.

CONCLUSION

The evidence strongly supports the conclusion that the official government data on business bankruptcies have lost touch with the underlying reality they claim to measure. There are as many as nine times more bankruptcies involving a business than the current government data suggest. In the most recent year for which data are available, there were about a quarter of a million bankruptcies that historically would have appeared in the government figures as business filings but now are counted as nonbusiness filings. Perhaps one in every seven persons in a bankruptcy system designed for consumers actually needs a bankruptcy system that deals with business failure.

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111. See *supra* Part I.A.1.

112. See *supra* Part I.C.

113. See *supra* Part I.B.

We suspect that the source of the error was unintended, most likely a byproduct of the growing popularity of computer-assisted programs for the preparation of bankruptcy forms—programs that routinely classify all individual debtors as nonbusiness, regardless of conclusive evidence to the contrary. Although no one deliberately set out to undercount business debtors, the effects of the AO's practices have been pernicious. An entire class of debtors, those who turn to the bankruptcy system for help when their small businesses are failing, appears to have disappeared from the system, but they are still there.

Although there is no evidence that the AO set out to misstate bankruptcy filing data deliberately, the AO failed to consider whether its decades-old system for counting bankruptcy cases still captured meaningful data. Congress has charged the AO, through its director, with the task of compiling and reporting statistical data regarding the federal courts.<sup>114</sup> Surely, this charge includes the duty to ensure that its data are accurate. Indeed, if the AO will not ensure the integrity of its data, no one else can. Lynn LoPucki has identified the political barriers preventing meaningful academic access to federal court data.<sup>115</sup> Even the National Bankruptcy Review Commission, which Congress created in 1994 to make recommendations regarding bankruptcy reform,<sup>116</sup> lacked the political clout to turn its seemingly uncontroversial recommendations on data collection into reality.<sup>117</sup>

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114. See 28 U.S.C. § 604(a) (2000).

115. See Lynn M. LoPucki, *The Politics of Research Access to Federal Court Data*, 80 TEX. L. REV. 2161, 2171 (2002) (“By offering selective access to data, the courts have controlled legal scholars’ research agendas, encouraging research that focused on the social and economic implications of litigation and discouraging research that focused on the actions of judges and the impacts of those actions on both litigants and the public.”).

116. See Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 603, 108 Stat. 4106, 4147 (describing duties of the Commission).

117. The commission issued several recommendations on data collection, none of which have been implemented:

4.1.1 Establish as policy that all data held by bankruptcy clerks in electronic form, to the extent it reflects only public records as defined in Bankruptcy Code § 107, should be released in electronic form to the public, on demand.

4.1.2 Establish and fund a pilot project to aggregate the data from their various sources, particularly bankruptcy clerks, and make that data available to the public in electronic form, on demand.

4.1.3 Secure limited-duration appointment of a coordinator, who, with the head of the AO’s office and the head of EOUST, would be charged with the duty of:

- (1) making recommendations to increase the accuracy of the debtor’s petitions, schedules and statements;
- (2) setting the data-collection goals;
- (3) coordinating the bankruptcy data-collection efforts of the central reporting agencies; and
- (4) reporting on an annual basis to the Congress, the Chief Justice, and the President.

4.1.4 Establish a bankruptcy data system in which (1) a single set of data definitions and forms are used to collect data nationwide and (2) all data for any particular case are aggregated in the same electronic record.

We are not the first to question the AO data. Others have suggested the government's data might undercount business filings, calling the government's data "problematic"<sup>118</sup> or suggesting an undercount of perhaps 9% in Chapter 11 cases.<sup>119</sup> The undercount is not small. The true number of bankruptcies with a connection to an underlying business is six to nine times more than the AO data suggest. To call these data problematic is generous. Indeed, another scholar characterized the official data as "fraught with errors, meaning that they are *not* reliable."<sup>120</sup>

We would go even further. The data on business filings are affirmatively misleading. The consequences for policymakers, academics, and pundits are stark: our findings undercut what everyone was sure they already knew. If these misleading data continue to motivate policy and scholarship—if the Conventional Story remains conventional wisdom—the consequences of this drastic undercount for financially hard-pressed entrepreneurs could be catastrophic.

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4.1.5 Maximize the number of documents filed electronically and maximize open-to-the-public remote electronic access to all data for free, or at the lowest possible cost.

1 NAT'L BANKR. REV. COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS 921-41 (2000) (stating specific recommendations and elaborating on need for more bankruptcy data collection).

118. See GROSS, *supra* note 10, at 71-72.

119. See Fenning & Hart, *supra* note 48, at 132 (noting an undercount of 7% with true relative difference of 9%).

120. See Frasier, *supra* note 30, at 340 (emphasis in original).