

# Structured Finance Newsletter

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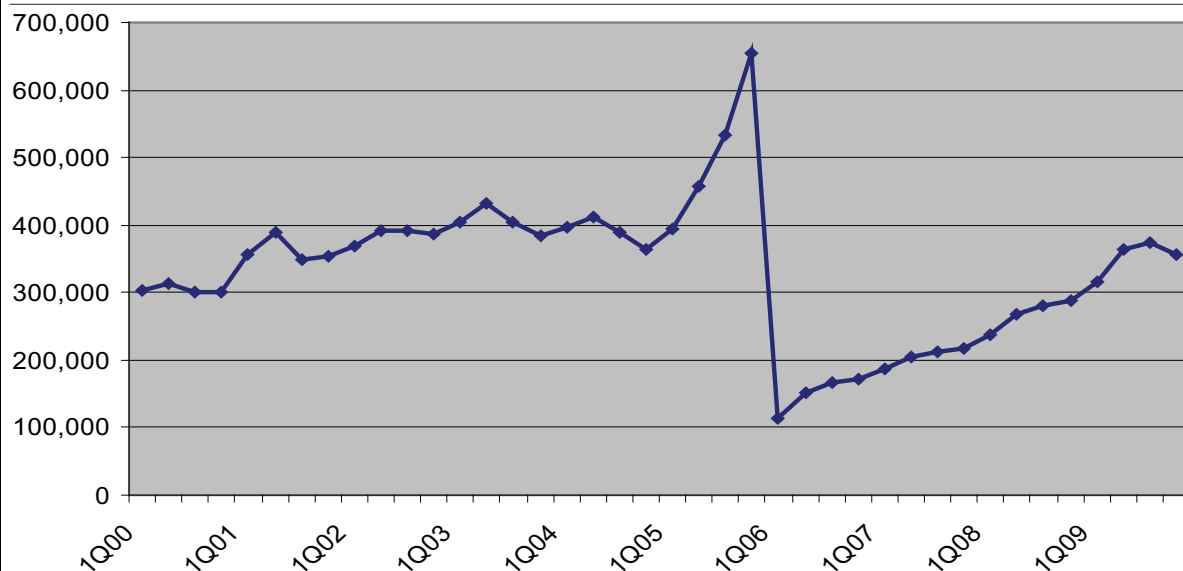
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## PERSONAL BANKRUPTCY TRENDS: ECONOMIC AND LEGISLATIVE IMPACT

U.S. personal bankruptcy levels declined 3% to 144,490 in April 2010 from the prior month, which registered the highest levels since the bankruptcy law changes<sup>1</sup> in 2005. During the first four months of 2010, bankruptcy filings have been 17% higher than the same period of 2009. While the decline in bankruptcy filings in April 2010 is viewed as a positive sign, the overall increase in bankruptcy levels in the first four months of 2010 is concerning.

The graph below summarizes the personal (non-business) bankruptcy statistics on a quarterly level from 2000 to the end of 2009:

Quarterly Bankruptcy Filings



Source: American Bankruptcy Institute

Bankruptcy levels increased dramatically prior to the change in the bankruptcy system in 2005 as the changes to the bankruptcy laws made it more difficult for consumers to file for bankruptcy. Following this change, bankruptcies dropped to levels which were well below those experienced historically.

The bankruptcy statistics from 2009 show that Chapter 7 bankruptcy filings are rising faster than Chapter 13 filings. Chapter 7 bankruptcies allow a borrower to eliminate all debts through bankruptcy while Chapter 13 usually is used for borrowers seeking to save their homes from foreclosure. Chapter 7 filings accounted for approximately 71% of all bankruptcy filings in 2009 compared with approximately 60% in 2006 and 2007. This may be an indication that more homeowners, who may be underwater in their mortgages, may be walking away from their homes.

The Federal Reserve Bank of St. Louis has recently issued a working paper on personal bankruptcy cycles. This paper examines the causes of personal bankruptcies and timing of bankruptcies in relation to recessionary periods. This paper concludes that bankruptcy rates are significantly higher than normal during recessions and rise as recessions persist. This may be particularly true in the current recession as the level of unemployment has continued to remain high. It also concludes that high bankruptcy rates may begin to fall but remain above normal for several quarters after a recession has ended. However, the longer the recession, the faster the return to normalcy.

In addition to the economic factors at play, there are legislative proposals which have been introduced which may impact the dischargeability of student loans in bankruptcy. There have recently been two bills introduced, one in the House and one in the Senate that would allow for borrowers of student loans to retroactively seek to discharge their private student loan debt when in bankruptcy. The difference in the two bills is that the House bill would make only student loans issued by for-profit entities dischargeable in

bankruptcy while loans made by non-profit entities would remain non-dischargeable (except for undue hardship). The Senate bill would make all private student loans dischargeable in bankruptcy. The impact could be both an increase in bankruptcy filings as well as a decline in recoveries on defaults related to bankruptcies.

DBRS will continue to closely monitor these economic and legislative factors and their impact on individual credits and sectors.

For questions or comments, please contact Rosemary Kelley at [rkelley@dbrs.com](mailto:rkelley@dbrs.com).

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1. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

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