



Business

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The who, why and how of bankruptcy filings

By Janice Brunson
staff writer

Charge accounts are maxed out, and the house payment is three months past due. Utility services are about to be disconnected, the car is in repossession and daily phone calls from creditors send the blood pressure soaring.

Earnings simply do not provide income enough to keep up. They seek bills, especially now that overtime pay has been cut in the face of a faltering economy.

A gloomy picture but one that is all too familiar to trustees for the U.S. Bankruptcy Court, Eastern District of Michigan, in Detroit. During the first four months of 1991, bankruptcies are up significantly over the same period last year, from 4,597 filings in 1990 to 6,021.

Of the total number filed, more than 80 percent are personal or consumer filings, people whose financial lives are out of control. They seek relief in bankruptcy court under one of two options — complete liquidation

under Chapter 7 or debt repayment under Chapter 13. The majority file Chapter 7.

Southfield attorney Stuart Gold, one of a dozen trustees who oversees proceedings in metropolitan Detroit for the U.S. court, describes today's typical debtor.

"UNDER 45 years old. Married with a combined income of \$30,000. One or two children. Anywhere from \$10,000 to \$20,000 of unsecured liabilities, most likely credit card charges and medical obligations.

"Cause of the calamity — one or the other (husband or wife) has been laid off or unemployed for a period of time or there has been a drop in overtime pay. We're seeing more and more of that."

Gold cites the case of a 45-year-old, unmarried professional employee by a major area corporation. He earns \$60,000 a year and is \$58,000 in debt.

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who have no home equity are permitted an additional \$3,750 in miscellaneous deductions.

If exemptions exceed assets, all debts are discharged. If assets exceed debts, excess assets are liquidated and creditors are paid with the proceeds.

Based on the formula, 80 percent of all people who file Chapter 7 have no assets, according to Marion Mack, assistant U.S. trustee for eastern Michigan. But others are capable of at least some repayment of outstanding bills but file Chapter 7 to avoid all payment.

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provide debtors with a "fresh start, not a head start," according to Mack, who said the substantial abuse provision was enacted into the bankruptcy code in the 1980s to toughen earlier laws that tended to favor the debtor.

"Abuse is like pornography. You know it when you see it. It jumps off the page. It shocks the conscience," Mack said, adding that court challenges for substantial abuse under Chapter 7 have steadily increased in the past six months. The disposition of such challenges are settled in court.

The case of the \$60,000-a-year professional is telling. As required by law, he submitted verification of income and a monthly budget of living expenses to Gold, trustee in the case. Allowances for such budgeted items as telephone, clothing, recreation and church contributions were considered exorbitant, and the court dismissed the petition.

While there are no hard and fast formulas to determine substantial abuse, Mack said "it is a good faith issue. Should creditors be forced to subsidize recreation, or clothing or dry cleaning? Maybe a person has to tone down lifestyle."

Under Chapter 13, debtors attempt to pay outstanding bills, agreeing to repayment schedules of three to five years. Those filing 13 are normally employed or have a regular source of income.

"The classic 13," according to West Bloomfield attorney David Ruskin who is also a bankruptcy trustee, are homeowners facing imminent foreclosure because of default in house payments. "It allows time to catch up."

UNDER 13, assets aren't liquidated, permitting the homeowner with a large equity the opportunity to salvage the investment.

Other factors also prompt 13, according to trustee Earle Erman, a Bloomfield Township attorney. They are personal ethics, legal guidance and the willingness of creditors to accept repayment plans.

In certain regions of the country, such factors appear to weigh heavily. In Tennessee, for example, there is a disproportionately high incidence of Chapter 13 filings, said U.S. trustee Mack.

Court costs for filing Chapter 7 or 13 proceedings are the same for each, \$120. But Chapter 13 proceedings are more complicated and last longer because of repayment schedules of up to five years. Chapter 7 filings are normally completed within 90 days.

Many times, 7 or 13 is equally appropriate, according to Erman. In such instances, "we favor the chapter that gives the client the most all-around benefit."

In either case, bankruptcy almost always has a negative impact on credit ratings and makes little allowance for those who attempt repayment.

"I advocate that the distinction should be noted by credit agencies," Mack said, favoring those who "try and pay their bills to the best of their ability."

Otherwise, Ruskin adds, "What's the incentive for attempting repayment? The credit community wants it both ways, (repayment but no distinction on credit reports). They're shooting themselves in the foot by not offering this extra incentive."

Under Chapter 7, bankruptcy is noted on consumer credit reports for 10 years and under 13, for seven years, according to Pat Young of TRW Information Services in Southfield. The firm is one of the nation's largest credit reporting agencies.



Seek portfolio growth, cut expenses, couple advised

By Dan Boyce
and Alan Ferrara
special writers

Local financial planning experts reviewed the data of the family profiled here and made general recommendations based on the participants' resources and goals. The information is for educational purposes only; references are not intended as discrimination or endorsements by Observer & Eccentric Newspapers or the advisers.

To receive a free financial planning brochure or to obtain a questionnaire to participate in this column, contact the Center of Financial Planning, Dept. 100, 2621 Central Park Blvd., Suite 604, Southfield 48076 or call 948-7900. Names of participants are withheld upon request, and submitted financial data is confidential.

Our profiled couple this month is facing some major changes in their lives and wondering how best to cope with them.

Ira and Joan Cremins have lived almost all of their married life in Plymouth. Ira, who will turn 62 next month, was laid off last year from his job as a materials handler for an auto supplier. Joan, 59, worked as a sales clerk until she was laid off in 1988. Partly because of Ira's past health problems, they decided to opt for an earlier than planned retirement rather than actively seek stop-gap jobs.

Their main goal is to maintain their standard of living in retirement, which they estimate will require an income of \$2,500 per month or \$30,000 annually. The only major expense looming on the horizon is replacement of their 1984 car within the next two years. They estimate a new car will cost them \$15,000-\$20,000.

One of their major financial assets is their home, which they value at \$195,000 and which is owned free and clear. They are contemplating a move to a smaller home. With their children grown, they do not need the amount of space in their current home, and they would like to reduce their property taxes.

A move to a less expensive residence not only would lower their property taxes but would also probably free up some of the equity locked in their current home — allowing for a greater investment cushion. We believe that such a move early in retirement is well-advised. It might help keep them from perhaps becoming "house poor" later in life.

We would suggest that they buy the new car at the time they sell their current home. If possible, a portion of the home equity could be used for the car. We would also suggest that they at least consider a recent model, low-mileage used car. This could shave thousands of dollars off the cost of a new auto.

We believe that their inclination to pay cash for the car, as well as any other retirement purchases is good strategy. We have found that those retired individuals who have kept their debts to a minimum are the most financially secure in retirement. This is especially true regarding consumer debt, which is both very costly and is not tax-deductible. A low debt position decreases the amount of required monthly expend-

Financial Position	
ASSETS	
Invested Assets:	
Checking and Cash	\$10,000
C. D.'s	76,000
EE Savings Bonds	15,000
Lifo Insurance Cash Value	19,000
Stocks	6,500
I. R. A.'s	\$1,700
Total Investments	\$178,200
Non-Investment Assets:	
Residence	\$195,000
Automobiles	4,000
Other Personal Assets	20,000
Total Non-Investment	\$219,000
Total Assets	\$397,200
LIABILITIES	
Insurance Loans @ 5%	\$7,000
Total Liabilities	\$7,000
NET WORTH	\$390,200

The Bottom Line	
Financial Strengths:	
✓ Owns home free and clear	
✓ No consumer debt	
✓ Asset egg has been accumulated	
✓ Potential for tying up equity in home if move occurs	
✓ Good auto and homeowners coverage	
✓ I. R. A.'s	
Financial Weaknesses:	
✓ Layoff forced early retirement	
✓ Low retirement income	
✓ Little protection against future inflation	
✓ Health insurance needed until age 65	
✓ No estate plan	



FAMILY FINANCES

itures. As a result, a retiree on a fixed income can survive and thrive at much lower income levels.

THE CREMINS' future income includes a fixed pension of \$400 per month for Ira. He also expects to receive \$900 from Social Security, and Joan will receive approximately half of that three years from now when she turns age 62. The remainder of their income must come from their own savings and investments.

It appears that they will be able to meet their income needs during the next few years. With income of \$1,200 per month from pension and Social Security, they need an additional \$1,200 per month from investments to meet their \$2,500 per month income goal. If they earn an average of 8 percent on their \$178,000 of investment assets, they would be able to generate the \$1,200 per month needed. Eight percent can be obtained right now in long-term U.S. government treasury bonds or with shorter term deferred investment annuity contracts.

A major concern of ours is the probability of future inflation eroding their purchasing power. At an average 5 percent rate of inflation, their purchasing power would be cut in half over 15 years, and the cost of living would quadruple over Joan's 30-year life expectancy. If they put their entire savings into long-term government bonds, they would be virtually assured of a lower standard of living in the future.

They can expect only minor increases in their future income from the addition of Joan's Social Security in three years and from the investment of any sales proceeds from their home. We would offer two suggestions to help them deal with significant problem of inflation.

FIRST, IRA and Joan need to take a close look at their expenditures. They should track their expenses over a period of several months and determine whether there are some expenditures that are really unnecessary for their quality of life. Even small long-term reductions in their expenditure rate is a real plus for them.

the total investment assets increase somewhat to offset future inflationary pressures. This can be done either through reinvestment of income or from growth in the value of their investments. Currently, they have only one small growth investment — a stock holding.

This observation leads to the second suggestion, to consider some growth and income investments in their portfolio rather than committing to pure income-oriented investments. Utility stocks, convertible bonds, and quality blue chip issues are all appropriate assets for a part of their portfolio — perhaps 30 percent of it. Although returns are not guaranteed, they should be able to achieve higher average rates of return over the long haul. They might want to use mutual funds to achieve adequate diversification and to gain professional management expertise.

If they are able to successfully reduce expenditures and increase average investment return, they will not need as large an investment cushion in retirement. This in turn may give them greater flexibility in their choice of a retirement residence.

Another issue they must address is the need for health insurance during the early years of retirement until both are age 65 and eligible for Medicare. They may want to contact a specialist in the insurance area to investigate alternatives. But they should first look into continuing the group coverage from Ira's old employer. By law, they must be offered such coverage under the group medical plan for two years from the date of Ira's layoff although the premium would be paid by Ira and Joan. Some companies also offer the ability to convert this group coverage to personal coverage until age 65.

Ira and Joan need to put a basic estate plan in place. They currently have no wills, trusts or other documents. All property is held jointly, except for their IRAs and annuities. They should realize that in the case of a common accident, their property would be probated and distributed according to inflexible state rules call the intestacy statutes.

SOMETIMES THE BEST WAY TO WRITE A CHECK IS NOT TO WRITE ONE



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