

SENATE SMALL BUSINESS COMMITTEE

MINUTES

MARCH 6, 1981

The Senate Small Business Committee met on Friday, March 6, 1981, at 10:00 a.m. The Chairman, Senator R. P. "Bo" Thomas, presided.

The following members were present: Senators Thomas, Creech, Allred, Baker, Boger, Cavanagh, Duncan, Frye, Marvin, Marion, Noble, Smith, and Walker. Members absent, Senator Lawing.

The Chairman recognized Senator Creech for an explanation of Senate Bill 156, An Act to Make the Federal Bankruptcy Exemptions Unavailable to North Carolina Debtors.

Senator Creech stated that the bill does exactly what it states, that several states have already opted out, and he felt that the Federal law encouraged businesses to declare bankruptcy. He noted that the North Carolina statutes on bankruptcy have not been changed, except for very minor revisions, since 1868. Senator Creech asked Mr. William C. Rustin, Jr., Executive Vice President of the North Carolina Merchants Association, Inc. to speak on the bill. (See Attachment No. 1 for Mr. Rustin's remarks.)

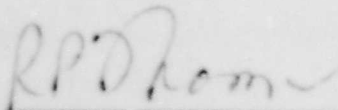
Senator Creech then recognized Mr. Hugh Wesley Williams, Executive Director of the Raleigh Merchants Bureau, who spoke briefly for this bill.

The Chairman recognized Mr. William C. Lawton, a Raleigh attorney, to state his position on this legislation. (See letter from Mr. Lawton, dated March 2, 1981, summarizing his position--Attachment No. 2.)

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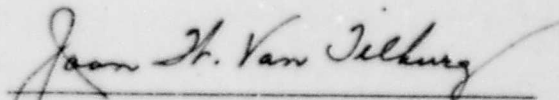
The Chairman announced to the Committee that he wanted this proposed legislation to be fully heard, therefore, discussion on Senate Bill 156 would be continued at future meetings.

The meeting adjourned at 10:30 a.m.



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R. P. "Bo" Thomas  
Chairman



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Joan W. Van Tilburg  
Committee Clerk

## NC MERCHANTS ASSOCIATION - BANKRUPTCY TESTIMONY

Thank you for this opportunity to address the problems brought on by the overly liberal exemptions in the federal bankruptcy law. Perhaps the worst harm is due to the change in attitude of our people; to illustrate, in a specific example:

"A customer made a purchase of \$900.00 on a Monday; on Wednesday, he filed Chapter XIII. This customer's financial condition did not change in three days."

"Another customer filed in August of 1979, and I have not received a payment to this date." (February 10, 1980.)

Rather than protecting those individuals who have true cases of hardship, the federal law has apparently spread the fever of "getting something for nothing," and this is the attitude that runs contrary to the true pride of the American people.

Let's see how this attitude has affected businesses:

(1) The increase in bankruptcies in the 44-county Eastern District of North Carolina has been 64% from 1979 to 1980 (Raleigh News and Observer, March 4, 1981).

(2) In the Western District of North Carolina, it was 149%; and

(3) Nationwide, personal bankruptcies rose 82% during the first full year under the federal law, to an enormous quantity of over 380,000 individual personal bankruptcy filings (Charlotte Observer, March 1, 1981).

(4) Using Sears' stated figures in the February 6 issue of the Washington Post, they wrote off \$40,500,000 in 1980 alone, over some 80,000 accounts, which reflects an average of over \$500 per filing. That converts to an estimated loss of over 200 million dollars in 1980.

(5) Small businesses do not have as many accounts as Sears, but they have a like percentage of filings--and their ability to absorb these losses is much less. Good, longtime customers are falling by the wayside daily--just as are a lot of small businesses who see their accounts receivables evaporate into thin air.

(6) If the businesses are able to absorb these losses, then they have no option but to pass these increases in operating cost to their other customers--the ones who do pay for the goods and services they purchase, but at a necessarily higher price to cover the losses caused by others--and this is not fair to the good consumers!

Perhaps, this change in attitude from "hardship case" to get "something for nothing" is okay in today's society--but as of February 15th, the legislatures of 16 other states have felt it to be against the grain of American pride.

Alabama	Kansas	Oklahoma
Arizona	Kentucky	South Dakota
Florida	Louisiana	Tennessee
Georgia	Nebraska	Virginia
Illinois	Ohio	Wyoming
Indiana	(and South Carolina is very close)	

*William C. Lawton*

ATTORNEY AT LAW

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March 2, 1981

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AREA CODE 919

Senator R. P. Thomas  
General Assembly of North Carolina  
Legislature Building  
Raleigh, North Carolina 27611

Re: Senate DRS 7527-LJ entitled Federal Bankruptcy  
Exemption Unavailable

Dear Senator Thomas:

I am an attorney practicing law in Raleigh. I do a substantial amount of federal bankruptcy work. Although I am all too aware that the federal bankruptcy law does give the individual states the right to opt out of the federal bankruptcy exemptions, I feel that there are certain circumstances surrounding the present proposed legislation that warrant its defeat in the General Assembly this session.

Although I do a substantial amount of debtor work, I am not unmindful of the objections and the needs of creditors. While it may be that the present federal exemptions are arguably unfair to creditors, a complete opt out as proposed by this legislation is completely unfair to debtors and goes overboard to assist creditors.

The primary objections to the federal exemptions are two-fold. First, the allocation of the real property exemption, \$7,500 per individual, to personal property, where there is no real property held by the debtors, is viewed by creditors to be unfair. Second, the exemption of household goods as individual items where they are valued at \$200 or less is likewise deemed unfair. While they may, in fact, be unfair in their present form because, subject to abuse, I believe a more realistic approach to the federal exemptions would be to adopt state exemptions along the same lines as the federal exemption with specific amendments addressing the above two primary objections. For instance, there is not much doubt that most of the federal exemptions are very reasonable, with the exception of these two exemptions. To overcome the first objection, it would be entirely within the province of the General Assembly to provide the same \$7,500



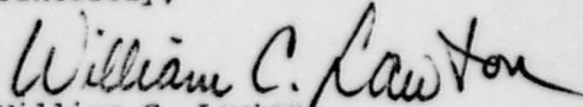
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exemption per individual to real property while at the same time providing that if there is no real property owned by that individual, the \$7,500 may not be applied to other personal property. The second objection can be addressed balancing the interests of debtors and creditors by allowing a maximum dollar figure, for example, \$5,000 as the total allowable household and consumer goods exemption. This would prevent the exemption of \$15,000 or \$20,000 worth of household and consumer goods simply because no individual item exceeded \$200 in value.

I would very much like to speak to this bill before your Committee. Would you please notify my office of an appropriate time to address the Committee when this legislation is being considered.

With kindest personal regards, I am

Sincerely,

  
William C. Lawton

WCL:ssc

SENATE SMALL BUSINESS COMMITTEE

MINUTES

MARCH 13, 1981

The Senate Small Business Committee met on Friday, March 13, 1981, at 9:30 a.m. The Chairman, Senator R. P. Thomas, presided.

Members present: Senators Thomas, Creech, Allred, Baker, Boger, Cavanagh, Duncan, Frye, Lawing, Marvin, and Smith. Members absent: Senators Marion, Noble, and Walker.

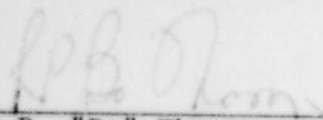
The Chairman recognized The Honorable Thomas M. Moore, United States Bankruptcy Judge of the Eastern District of North Carolina. Judge Moore appeared before the Committee at the request of the Chairman.

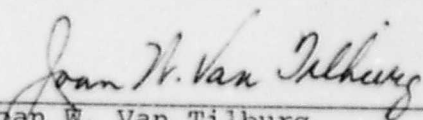
Judge Moore introduced Ms. Peggy Deans, Clerk of the United States Bankruptcy Court of the Eastern District, who presented statistics on the number of filings before the federal Bankruptcy Reform Act of 1978 and afterward. (See Attachment No. 1.)

Judge Moore then made a detailed presentation regarding bankruptcy but prefaced his remarks with the statement that he was not making a stand for or against the proposed legislation, but was there to present the facts. (See Attachment No. 2.)

The Chairman recognized Mr. Robert H. Gage, an attorney from Morganton, North Carolina, with the Catawba Valley Legal Services, Inc., who made brief remarks concerning his position that the increase in bankruptcy cases were simply a coincidence with inflationary times.

The meeting adjourned at 10:30 a.m.

  
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R. P. "Bo" Thomas  
Chairman

  
\_\_\_\_\_  
Joan W. Van Tilburg  
Committee Clerk

Our first permanent bankruptcy law was enacted in 1898. Major changes were made in the law in 1938 as a result of the enactment of the Chandler Act. Again, forty years later, the bankruptcy laws of this Country were rewritten and major changes in procedure, substantive law and the court system were accomplished. The most recent legislation on this subject is known as the Bankruptcy Reform Act of 1978. The provisions of the Act which I will be discussing with you are contained in Title 11 of the United States Code, referred to as The Bankruptcy Code.

The provisions of the Code which are the principal concern of this Committee are contained in Section 522 of Title 11 - Exemptions. Before commenting on this section, however, perhaps I should make it clear that my duties as Bankruptcy Judge require me to interpret and apply the law to factual situations presented to me in Court or in Chambers. My personal views as to the morality of the law or as to society's need for the law are quite immaterial. I must confess, however, that it would be difficult to perform my duties and responsibilities if I did not respect the law in our Country as well as the legislators who enact such laws. I believe the Bankruptcy Reform Act of 1978 to be a well-designed act and one that serves a very worthwhile purpose. I might also point out that the U.S. Congress studied the bankruptcy law extensively from 1972 to 1978 when the new law was enacted. It was not hastily drafted or enacted. It represents the collective effort of the United States Congress.

Before discussing Section 522, let me review the North Carolina exemptions which were in effect prior to October 1, 1979. There were three major exemptions:



1. Article X, Section 1, N. C. Const. - Personal Property Exemption - \$500.00 (without deduction for liens).

2. Article X, Section 2, N. C. Const. - Homestead Exemption: homestead and dwelling of a value of \$1,000.00 (limited to use of property for life of persons in being).

3. Article X, Section 5, N. C. Const. - Insurance Exemption. Life insurance payable to wife or children. A. N. C. Supreme Court decision has determined that this exemption includes the cash surrender value of the insurance policy as well as the face value of the policy upon death.

These exemptions were enacted in 1868 - One Hundred and Thirteen Years Ago. I believe it can be safely stated without fear of debate or prejudice, that such exemptions, if adequate in 1868, were totally inadequate and outdated in 1978, when the Bankruptcy Reform Act was enacted.

In addition to the exemptions previously mentioned you should be aware of the fact that under the Bankruptcy Law prior to October 1, 1979, real estate owned by a man and his wife as tenants by the entirety, did not become a part of the debtors' estate and hence this property was not administered by the Court.

Under the pre-October, 1979, bankruptcy law, it was quite possible for an individual to file bankruptcy and obtain a discharge and yet retain an unlimited amount of property in the form of real property owned as tenants by the entirety and cash surrender value of life insurance. On occasions, I had cases where the debtor retained property with values in excess of \$100,000.00. The business community understood and accented this as the law. Keep in mind, however, that only the affluent owned property of this nature. It was not the lot of the average consumer-wage earner to own substantial real property or have life insurance policies with a substantial cash value.

Perhaps it should also be pointed out that future earnings, social security, alimony, child support, welfare payments, retirement benefits such as state employees retirement, military retirement, civil service retirement or other benefits which could not be recovered except upon retirement or termination of employment were not considered assets to be administered in a bankrupt's estate. Under the old law, also, a wrongful death or personal injury award were not property of a debtor's estate.

The point I am attempting to make, at this time, is simply that, even under the old law, it was quite possible for a debtor to retain a very sizeable estate after filing a petition in bankruptcy. These situations did not occur frequently and as a result, there was no public debate over such horror stories.

Now, let's look at the Federal exemptions authorized by Section 522 of the Bankruptcy Code.

1. Interest in real or personal property used as residence up to \$7,500.00 (this is 7 1/2 times the N. C. Homestead Exemption); but entireties property is not exempt.
2. \$1,200.00 in value in one automobile (equity). It isn't easy to accumulate \$1,200.00 equity in an automobile if you are a salaried employee or wage earner who buys an automobile financed over the 48-month time frame.
3. \$200.00 in value in any item of household goods, clothing, books, animals, crops or musical instruments. It is quite conceivable that this exemption could be used to permit the debtor to retain an "excessive" value of household goods, clothing, etc. However, from a purely practical point of view, most every consumer debtor is buying on credit and his household goods are usually encumbered by "retail installment contracts", purchase money

security agreements and financing statements. The fact is that while Congress has increased the exemptions for household goods. "Congress" has not enabled the debtors to create any more equity in such property than they had before the new Bankruptcy Code. For example, a debtor can now exempt \$200.00 equity in an unlimited number of items; however, if he has no equity in any of the household goods, the exemption does not provide him any benefit whatsoever.

4. \$500.00 in jewelry. This is a new exemption - but in over 20 years, I can only recall 3 instances where personal jewelry has been liquidated by a trustee. Once it was a Rolex watch; twice diamonds.

5. \$400.00 in any property - new exemption.

6. \$750.00 in books, implements & tools - new exemption

7. Any unmaturred life insurance policv - nothing new.

8. \$4,000.00 in interest, dividends or loan value in life insurance - this is less than under State exemptions.

9. Health aids - new but very rarely used - never sold any in 20 years.

10. Debtor's rights to:

Social Security

VA benefits

Disability income

Alimony and support (with limitations) - reasonably necessary

Bonus & pension plans

11. Debtor's rights to:

Wrongful death

Personal iniurv (\$7,500.00) - less than old Act

Loss of earnings.

#### CONCLUSION:

The contrast between the old exemptions and the new is not as great as many would have you believe, so examine the specifics closely before you act on this matter. Also, consider that debtors are not oranzed and have

no organization such as the lending institutions and merchants have representing them.

The exemptions per se have not been the stimulus for increased filings. The federal exemptions are not imposing any real hardship on the credit community. However, 522(f), the lien avoidance provision, is impacting upon the small loan or finance company. Section 522(f) is a major factor contributing to the uproar in the credit community. This will not be affected if you opt out of the federal exemptions.

The high percentage of increase in filings which many special interest groups would have you believe is the direct result of the federal exemptions are, in fact, attributal to other factors. The other factors which are responsible for the increased filings are (1) the general economic conditions in the country, (2) the easy credit and hard-sell policies of the business community, (3) increased public awareness of the relief provided by the Bankruptcy Code and (4) a more favorable treatment for a debtor under the new Bankruptcy Code.

The increased filings have provided stimulus for attack on the federal exemptions. However, it really has little, if any, relationship to the federal exemptions. As the statistics have shown, there has been an approximate 125% increase in filings in the Eastern District of North Carolina during the period October 1, 1979, through September 30, 1980, as compared with the period October 1, 1978, through September 30, 1979. However, there has been no increase in the percentage of straight bankruptcy cases filed as a percentage of the total case filings. For example, 43% of the cases filed before October 1, 1979, were straight bankruptcy cases and 43% of the cases filed after October 1, 1979, have been straight bankruptcy cases. Only 1,000 more straight bankruptcy petitions were filed in the 12-month period ending September 30, 1980, than were

filed in the 12-month period ending September 30, 1979. Compare the percentage increase in filings for the years 79-80/78-79 with the years 74-75/73-74.

$$\frac{79-80/78-79}{4,100} = 125\%$$

$$\frac{74-75/73-74}{1,058} = 192\%$$

There were no new federal exemptions which could be blamed for the increased filings in 1974-75. It was principally economics and easy credit.

Let me thank you for the opportunity to meet with you and provide you factual information which I have which may in some way assist you in your legislative responsibilities.



FILINGS FROM 10/1/79 through 9/30/80

<u>TOTAL CASES</u>	<u>ESTATES</u>	<u>CHAPTER 7</u>	<u>CHAPTER 11</u>	<u>CHAPTER 13</u>
2,606	4,102	1,104	62	1,440

FILINGS FROM 10/1/78 through 9/30/79

<u>TOTAL CASES</u>	<u>ESTATES</u>	<u>CHAPTER VII</u>	<u>CHAPTERS X, XI, XII</u>	<u>CHAPTER XIII</u>
1,795	----	764	35	996

	<u>CHAPTER 7</u>	<u>CHAPTER 13</u>	<u>CHAPTER 11</u>
% filings prior to Code	43%	55%	2%
% filings since Code	43%	55%	2%

ASSET CASES filed 10/1/79 through 9/30/80 - 124 (11%)

Number of converted Chapter 13 cases that are now asset cases - 2

SAMPLING OF 25 CASES (43 estates) re: EXEMPTIONS:

CHAPTER 13

Total Property That Could Be Claimed  
 REAL \$3,582.66 per individual  
 PERSONAL \$1,557.00 per individual

All claiming Federal exemptions

CHAPTER 7

Total Property Claimed  
 REAL \$3,920.45 per individual  
 PERSONAL \$3,574.41 per individual

SAMPLING OF CHAPTER 13 PLANS CONFIRMED WITHIN LAST 30 DAYS - 29 cases

70% dividend to unsecured creditors

*Exemptions  
 Claimed without regard to  
 the liens against the property.*

*194-15 192%*