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EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

November 8, 1999
(Senate)

STATEMENT OF ADMINISTRATION POLICY

(THIS STATEMENT HAS BEEN COORDINATED BY OMB WITH THE CONCERNED AGENCIES.)

S. 625 - Bankruptcy Reform Act of 1999

(Grassley (R) Iowa and eight cosponsors)

The President supports bankruptcy reform that is balanced, would reduce abuses of the bankruptcy system, and would require debtors and creditors alike to act responsibly. Last year, the Senate produced such a balanced bill with overwhelming bipartisan support. The President is disappointed that, this year, the House failed to produce legislation that he could support. S. 625 reflects some improvements over H.R. 833 as passed by the House. The Administration, however, continues to have serious reservations about S. 625 and strongly opposes some of its provisions. For example, we are deeply concerned about a provision of the manager's amendment that adds an important "safe harbor" that protects low-income debtors from motions to deny them access to Chapter 7 under the means test, but also eliminates an essential "safe harbor" that would protect low-income debtors from coercive creditor motions that might be brought under a under a vague "totality of the circumstances" test more appropriately enforced by bankruptcy trustees and courts. The latter protection eliminated by the managers' amendment was included in the reported version of the Senate bill, the House-passed bill, and last year's conference report. The Administration's other objections to this bill are explained in detail in the Attachment.

Most of the Administration's concerns would be addressed by relevant amendments that the Administration understands will be offered on the Senate floor. The Administration's views on the anticipated amendments are also contained in the Attachment. The Administration remains hopeful that bipartisan cooperation will result in responsible bankruptcy legislation that the President can enthusiastically sign.

Finally, the Administration understands that certain non-relevant amendments will be offered as well. On November 4, 1999, in a letter to the Majority Leader, the President made clear that he strongly supports an increase in the minimum wage of $1 over the next two years; however, if Congress sends him a bill delaying the increase, repealing overtime protections for certain workers, adding costly and unnecessary tax cuts that threaten fiscal discipline and direct benefits away from working families, and thwarting ongoing efforts to enforce pension law, he will veto it.

In addition, the Administration strongly opposes the inclusion of an unrelated education amendment, a version of the Teacher Empowerment Act. When similar legislation passed the House this summer, the President indicated that he would veto it. The Administration's position on this legislation has not changed. The amendment would eviscerate the class size reduction program passed on a bipartisan basis last year and replace it with a block grant that fails to guarantee that any funds will be used to support the crucial work of reducing class sizes in the early grades. In addition, the block grant does not target funds toward the neediest students and does not include important provisions to improve teacher quality. If this amendment is attached to S. 625, the President will veto the bill.

The Administration opposes the drug-related amendment because it would reduce the current disparity between crack and powder cocaine sentences solely by increasing powder cocaine penalties dramatically instead of addressing both crack and powder cocaine penalties. Decreasing the threshold amount of powder cocaine necessary to obtain 5- and 10-year mandatory minimum sentences may be counterproductive because it could significantly redirect Federal law enforcement resources from the highest level offenders. In addition, this amendment would actually exacerbate the disproportionate impact of cocaine sentencing on minorities because, according to U.S. Sentencing Commission statistics, approximately 31% of defendants sentenced at the Federal level for powder cocaine offenses in 1998 were African American, 48% were Hispanic, and only 19% were white.

* * * * * * *

Attachment

Detailed Administration Views on S. 625 and Anticipated Floor Amendments

Access to Chapter 7. Any means test used in bankruptcy proceedings should deny access to Chapter 7 bankruptcy procedures only to those debtors who genuinely have the capacity to repay a portion of their debts successfully under a Chapter 13 repayment plan. Debtors who may be denied a discharge of their debts must be given a meaningful opportunity to have their specific circumstances considered by bankruptcy courts with the authority to determine whether they genuinely have the capacity to repay a portion of their debts. In its current form, S. 625 would use a relatively inflexible and arbitrary means test to limit access to Chapter 7. The Administration strongly opposes this provision.

As reported, S. 625 would apply rough guidelines, developed by the Internal Revenue Service (IRS) for tax repayment plans, as standards for determining debtors' ability to repay, with exceptions only for expenses that are both "reasonable and necessary." While some expense standards should be used to guide the determination of ability to repay, they should be tailored for bankruptcy. We should not simply import standards that were developed for a different purpose -- tax collection – and which are applied for that purpose with far more discretion than S. 625 would allow for bankruptcy. We note that the Congress has criticized the IRS for inadequate flexibility in using these standards for tax collection, yet this bill would use them far more rigidly for bankruptcy purposes. The Administration believes that the IRS expense formulas can be used as a starting point for developing appropriate bankruptcy guidelines, but that each system would be best served by its own appropriate standards. As House Judiciary Committee Chairman Henry Hyde has said, the use of IRS guidelines without flexibility "depriv[es] debtors and their families of the means to pay for their basic needs." As Chairman Hyde noted on the House floor, "The cost of food in Omaha, Nebraska, or Boise, Idaho, is different than in downtown Manhattan. So what is realistic about an inflexible standard?"

The Senate bill creates a largely self-executing mechanism under which elaborate debtor filings will be reviewed by United States trustees, who, based on the filings, will file a motion to deny access to Chapter 7, if the debtor has the capacity to repay or her use of Chapter 7 is abusive. As modified by the managers' amendment, the bill also gives creditors the ability to file motions to challenge the debtors' use of Chapter 7 as abusive under a vague "totality of the circumstances" test. Creditor motions alleging abuse could be used by creditors against low and moderate income debtors – who have few resources for legal advice -- to coerce or threaten them to forgo their rights. The bill should provide below-median-income debtors with a "safe harbor" from general abuse motions by creditors, as well as with the "means-test safe harbor" that the managers' amendment provides. Both are essential.

Finally, since the bill as amended by the managers' amendment precludes any party from filing a 707(b) motion alleging that a below-median income debtor has the capacity to repay under the means test, there is no justification for requiring that these debtors fulfill the elaborate means test paperwork requirements. The courts will bear unnecessary costs for collection and storage of these useless filings and they impose an unnecessary cost (and increased legal fees) on the debtor as well. These debtors should be required to provide only the information sufficient to verify their income eligibility for the "safe harbor." Similarly, a more streamlined system could screen out those with no capacity to repay before additional paperwork requirements are imposed. All parties should be able to agree that any means test should be implemented efficiently. Burdensome filing and hearing requirements that lead to little or no additional debt repayment are not in the interest of debtors, creditors, or taxpayers.

The Administration understands that a series of amendments will be offered to improve the fairness and efficiency of the means test. The Administration strongly supports these amendments, including:

- An amendment by **Senator Feingold** to clarify that the long-term care expenses of a debtor caring for a non-dependent parent or relative are necessary expenses under the means test;
- A similar amendment by **Senator Leahy** to clarify that certain expenses for victims of domestic abuse are necessary expenses under the means test;
- A similar amendment by **Senator Schumer** to clarify that retraining expenses of displaced or unemployed workers are necessary expenses under the means test;
- An amendment by **Senator Dodd** to address special concerns of children and families, which includes a provision to clarify that the expenses associated with adopting a child are necessary expenses under the means test;
- An amendment by **Senators Schumer and Durbin** to provide an appropriate safe harbor from all types of creditor motions and unnecessary paperwork requirements for below-median-income debtors;
- An amendment by **Senator Durbin** to reduce unnecessary costs and inefficiency in the reformed bankruptcy system by streamlining application of the means test and reducing costly paperwork collections without affecting debt repayment under the system;
- An amendment by **Senator Schumer** to authorize the Treasury Department, in consultation with the Executive Office for United States Trustees, to modify certain of the IRS guidelines for use in bankruptcy to account for variations in the cost of living; and

- An amendment by **Senator Schumer** to improve the accuracy of the means test calculation by counting all required Chapter 13 expenses (administrative costs, reasonable attorneys fees, and arrearages on other debt) in calculating capacity to repay under the means test.

Abusive Creditor Reaffirmation Practices. Much evidence shows that debtors often reaffirm unsecured debt and low-value secured debt on unfavorable terms even though they do not have the means to meet their own necessary expenses and make more important debt payments, placing such priority debts as child support and alimony obligations at risk. Such reaffirmations frequently are the result of insufficient or misleading information or threats from creditors. S. 625 as reported does little to address these abuses. If we are to provide substantial new opportunities for creditors to challenge debtors' use of the bankruptcy system under Chapter 7 of the Bankruptcy Code, we must limit abusive creditor practices such as coercive reaffirmations and violations of the automatic stay against collection actions. We understand Senator Sessions may offer an amendment to provide some protections against abusive reaffirmations. However, we believe the amendment has significant loopholes, allowing debtors to reaffirm debts they cannot afford and failing to provide creditors with all the information that bankruptcy judges deem necessary and which many are already requiring be provided in their courts. The Administration strongly supports:

- An amendment by **Senator Reed**, that protects debtors by giving them adequate information for decisions about significant reaffirmations of unsecured and low-value secured debt.

We understand, however, that Senators Reed and Sessions continue to discuss ways to reconcile their two amendments in a way that might address our concerns.

Credit Card Information and Protection. The Administration continues to believe that reform must address the factor that is most strongly correlated with the rise in personal bankruptcy: rising levels of consumer debt. Americans now receive more than 3.5 billion credit card solicitations per year, many of which are marketed to encourage consumers to carry high balances and incur large interest charges. One of the most effective ways to reduce the number of bankruptcies in this new financial era is to give consumers the information they need to manage their credit card debts effectively, recognizing the creditors' superior information and bargaining ability. Consumers must be given clear information on the terms of their credit and the financial implications of not paying off their credit card balances. The Administration supports:

- An amendment by **Senators Grassley, Torricelli, Biden, and Johnson** addressing some abusive credit practices, such as failure to disclose "teaser" rates clearly, and requiring limited generic disclosure of the impact of making only the minimum payment on credit cards. While the Grassley-Torrecelli amendment is an improvement over H.R. 833, much more should be done. The amendment creates a system that is unnecessarily burdensome for consumers who may be reluctant to call their credit card company if they are worried about their finances or are pressed for time. The Administration strongly supports:

- An amendment by **Senator Schumer** to expand coverage of the teaser rate disclosures provided under the amendment by Senator Grassley and Torrecelli to apply to applications or solicitations available to the public in catalogs, magazines, and restaurants; and

- An amendment by **Senator Dodd** to require additional information specific to the individual consumer to allow them to better understand the impact of making only the minimum payment.

Cramdowns. S. 625 also changes the lien stripping or "cramdown" provisions in current law governing a Chapter 13 bankruptcy, under which the lien underlying a secured debt is reduced to its value at the time of bankruptcy. The Administration agrees that lien stripping should be limited to automobile loans incurred in the period preceding bankruptcy to prevent abuses, but believes that the provisions in the Senate bill are excessive. While the Administration strongly prefers the Senate provisions to the extreme prohibitions in H.R. 833, the five-year prohibition on lien stripping on automobile debts in the current bill will do little more to deter bankruptcy abuses than a more reasonable time limit. Instead, the prohibition will significantly reduce repayment of priority, unsecured debts like child support and taxes. The Administration strongly supports:

- An amendment by **Senator Kohl** that would ban cramdowns of secured goods with purchase money security interests incurred within six months of the bankruptcy filing.

Nondischargeable Debts. The Bankruptcy Code makes debts nondischargeable only where there is an overriding public purpose, as with debts for child support and alimony payments, educational loans, tax obligations, or debts incurred by fraud. In an attempt to deal with the possibility of abuse, the bill makes nondischargeable debt incurred on the eve of bankruptcy and certain debts incurred to pay nondischargeable debts. Unfortunately, the amendment will catch those who innocently incur debts as well. Moreover, the additional credit card and other nonpriority debts made nondischargeable by these provisions will compete in some cases after bankruptcy with child support, alimony, taxes, and other societal priorities like educational loans and taxes. The Administration strongly prefers the provisions in S. 625, which offer some protection for child support and alimony, to those in H.R. 833. However, the Administration also strongly supports:

- An amendment by **Senator Moynihan** that would preserve the current nondischargeability rules for lower income debtors, those least likely to incur debts on the eve of bankruptcy for abusive purposes; and

- An amendment by **Senator Dodd** to address special concerns of children and families, which includes a provision to alter the bill's nondischargeability provisions to make it less likely that debts legitimately incurred to support a family will be made nondischargeable; and

- An amendment by **Senator Schumer** that would make court-ordered fines and debts resulting from abortion clinic violence nondischargeable. As the Justice Department noted in a May 14, 1999 letter to Senator Schumer, the Administration generally opposes the expansion of nondischargeable debt unless there is an overriding public policy objective and no other way to achieve that objective, but believes this amendment is a necessary tool in current efforts to end clinic violence and intimidation.

Loopholes for the Wealthy. The Administration supports closing loopholes in bankruptcy law, such as unlimited homestead exemptions, that allow many wealthy debtors to avoid their responsibility to repay a significant portion of their debt. Bankruptcy reform should not place a greater responsibility for debt repayment on moderate- and low-income debtors than it does on high-income debtors. The Administration strongly supports:

- An amendment by **Senator Kohl** to place a reasonable limit on homestead exemptions.

Barriers to Entry to the Bankruptcy System. Finally, the bill appears to place unnecessary barriers to entry into the bankruptcy system that will not prevent abuse, but will create burdens on those with a genuine need for speedy bankruptcy protection. The Administration strongly supports:

- An amendment by **Senator Leahy** to save the taxpayers an estimated $24 million over five years by eliminating the requirement that every debtor file three years of tax returns and instead permit any party in interest to demand the copies when needed to verify the debtor's assets and income, thus reducing filing and storage costs and unnecessary paperwork burdens; and

- An amendment by **Senator Durbin** to allow certain mandatory credit counseling to be provided over the phone.

HILLNEWS

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will to do so. "When the boys and girls decide they're through playing and really want to finish their work," he said, "we'll get through just like that."

Problems remained on all of the unsigned bills, but a fight over how much flexibility to allow local education officials to spend money the Clinton administration wants earmarked for hiring new teachers was the most visible dispute.

Republicans complained that White House budget director Jack Lew opened negotiations on Labor-HHS-Education spending on Sunday by saying the teacher hiring issue was non-negotiable.

Sen. Arlen Specter, R-Pa., who chairs the Senate Appropriations subcommittee that deals with the bill, has been just as firm in his position. "We are not going to concede on teachers," Specter said Tuesday.

The subcommittee chairman said he was prepared to move a Labor-HHS-Education bill on Wednesday that would require school districts to give first priority to hiring more teachers.

Minimum Wage Hike This Year Unlikely After Senate Vote

EMPLOYMENT & LABOR

The Senate's adoption Tuesday of a Republican minimum wage increase plan did little to bolster chances for final action on the politically charged issue this year.

House floor action on the minimum wage before adjournment remains uncertain, and prospects for passage of legislation acceptable to the Clinton administration are even more unlikely.

Disagreements remain over how soon a $1 increase in the $5.15 minimum wage should take full effect, and over how much tax relief should be provided for businesses as compensation for higher payroll costs.

The Senate GOP plan, adopted 54-44 as an amendment to a bankruptcy overhaul measure (S 625), would increase the minimum wage over three years and provide $18.4 billion in tax cuts over five years. The Republican plan would also grant employers more flexibility in awarding performance bonuses without regard to laws governing overtime pay.

Senate Democrats drew four moderate Republicans to their cause, but saw their proposed $1-an-hour increase over two years and $9.5 billion in tax cuts tabled on a 50-48 tally. Republicans Lincoln Chafee, R.I., James M. Jeffords, Vt., Olympia J. Snowe, Maine, and Arlen Specter, Pa., joined Democrats in opposing the tabling motion.

Majority Leader Trent Lott, R-Miss., has predicted that no minimum wage increase will be enacted this year, and Democrats called the GOP proposal unacceptable.

Senate Democratic leaders said Tuesday they will try again next year and will make the minimum wage an election-year [illegible] issue.

Clinton Threatens a Veto

Minority Leader Tom Daschle, D-S.D., said he was encouraged by the narrowness of the vote on tabling the amendment offered by Massachusetts Democrat Edward M. Kennedy.

Kennedy called the GOP package "a real [illegible] Republican turkey with three right wings," composed of a watered-down wage increase, a poison pill that would undermine overtime payments to hourly employees, and other tax provisions.

Pete V. Domenici, R-N.M., who offered the GOP minimum wage amendment, said Democrats are trying to [illegible] passed, and added: "For all the talk, the Republicans have come forth with a very good bill."

Domenici's amendment would provide full deductibility of health insurance premiums paid by the self-employed, a permanent extension of the work opportunity credit, expansion of pension programs, an increase in the amount of equipment expenses businesses can claim, repeal of a rule on [illegible] installment [illegible], and an increase for small businesses from 50 percent to 80 percent in the deductibility of business meal expenses.

President Clinton threatened a veto, saying three years is too long a phase-in for the wage increase and criticizing what he called "special-interest tax breaks."

Clinton could also have been speaking of the minimum wage package approved, 23-14, on Tuesday by the House Ways and Means Committee. That measure's $30 billion worth of tax relief, which accompanies a $1 minimum wage hike over three years, was altered by panel Chairman Bill Archer, R-Texas, to remove three key provisions: a tax credit for independent film producers, a tax break for inner-city bus operators and a deduction for those who receive educational assistance from their employers.

The House bill includes many of the provisions of the Senate measure, as well as about $16 billion in estate tax relief.

House leaders insist they will not bring the minimum wage legislation (HR 3081) to the floor unless its supporters show that they have the votes for passage. While that seemed unlikely last week, Tuesday's markup and the likelihood that the first session of the 106th Congress will extend into next week gave backers new hope.

"If we're here long enough, there's a good chance we'll get to it," said Roy Blunt, R-Mo., the chief deputy whip who has done much of the vote counting on the Republican side.

Business Meal Deduction in Dispute

The business meal deduction sparked a lengthy debate in Ways and Means on Tuesday. The House bill would increase the deduction to 60 percent. Archer's proposal, adopted Tuesday, removed a provision limiting the increased deduction to small businesses.

"I'm sort of piqued at this insistence to increase the meal deduction," said Gerald D. Kleczka, D-Wis. "It escapes logic in my mind."

But Mark Foley, R-Fla., responded, "The meal tax deductibility serves an important purpose in our society. It literally spurs economic opportunity."

The panel rejected, [illegible], an amendment offered by ranking Democrat Charles B. Rangel, D-N.Y., that would have reduced the cost of the tax relief package to about [illegible] billion. The plan would have increased the meal deduction to [illegible] for small businesses and would have permitted deduction of entertainment expenses.

The rejected Democratic package also included full deductibility of health insurance premiums paid by the self-employed, an increase in the amount of equipment expenses businesses can claim to [illegible], an exclusion for the value of employer-provided educational assistance and extension and expansion of the Qualified School Academy Bond Program that aids school construction in low-income areas.

Russ Freyman

Wednesday, November 10, 1999

CQ DAILY MONITOR

The Morning News Briefing, Updated Continuously on www.CQ.com/news

With Little Settled, Budget Negotiators Settle In

Wednesday adjournment up in smoke as unresolved problems persist; Movement made on Labor-HHS bill, but teacher dispute still a sticking point

One thing became clear during Tuesday's budget negotiations. The standoff — and the first session of the 106th Congress — will last at least until next week.

HILL NEWS

Congressional and White House negotiators were aiming to reach agreements on the five unsigned fiscal 2000 spending bills by Wednesday night, but gave up for the day Tuesday without having "closed" any of them.

The House on Tuesday evening formally ended any hope that Congress would meet its goal of adjourning before Veterans Day by passing on a voice vote a fifth continuing resolution (H J Res 78) to keep the government in full operation through next Wednesday. The Senate is expected to concur Wednesday.

With neither chamber expected to return until next Monday or Tuesday after Wednesday's business is complete, House Appropriations Chairman C.W. Bill Young, R-Fla., said the latest plan is for appropriators to work through the holiday and weekend to have the bills ready to move by next Tuesday.

Despite the lack of progress this week, Senate Majority Leader Trent Lott, Miss., continued to insist that the remaining problems can be resolved once there is a

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***NOTE TO READERS:** Due to the Veterans Day holiday, the next issue of the CQ Daily Monitor will be published Friday, Nov. 12.*

TODAY AT A GLANCE

House Floor: On the schedule is legislation (HR 3073) that would set up a new grant program aimed at helping the poor and promoting responsible parenting through educational, economic and employment initiatives. Under suspension of the rules, lawmakers will take up seven measures, including a bill (HR 1869) that would expand the criminal definition of stalking to include use of the telephone, mail or the Internet. *(Convenes at 10 a.m.; votes possible throughout the day.)*

Senate Floor: Consideration resumes on amendments to legislation (S 625) that would tighten criteria for consumers filing for bankruptcy. Four hours of debate and a vote have been set for a GOP amendment that would increase criminal penalties for manufacturing or trafficking in amphetamines. Also scheduled are roll call votes on two nominees and a vote on the fifth continuing resolution (H J Res 78) to keep the government operating. *(Convenes at 9:30 a.m.; first vote possible at 1:30 p.m.)*

Asset Forfeiture: Senate Judiciary has six bills on its schedule, including a compromise measure that addresses revisions in civil assets forfeiture laws.

Land Acquisition: House Resources will mark up a bill (HR 701) that aims to set aside revenues from offshore oil and gas drilling operations for government purchases of environmentally sensitive lands.

State Programs: House Government Reform will mark up a measure (HR 2376) that would enable states to modify or change federal programs to meet their residents' needs.

(The complete Daybook begins on p. 13)

Senate's Centrists Organize To Stem Partisan Rancor

Bipartisan group of more than Two dozen senators attend Session to set future goals

THE PULSE OF CONGRESS

A year of acid partisanship in the Senate and the death of one of its most esteemed moderates has led to the revival of the Centrist Coalition, a band of senators from both parties hoping to forge bipartisan deals on major legislation in the years ahead.

John B. Breaux, D-La., and Olympia J. Snowe, R-Maine, have taken the lead in reviving the group, sending a letter to 35 colleagues inviting them to a meeting Nov. 3. Breaux said the death of Rhode Island Republican John H. Chafee had a sobering impact on the chamber and left many members searching for a way to soften the partisanship that has essentially defined this year.

Last week's meeting drew 15 Democrats and 11 Republicans, the biggest turnout yet for the coalition, which had not met since a poorly attended session in Chafee's office in the spring.

"The consensus was that we should continue this effort," said Breaux, adding that the key to the group's success will be consistency. Long gaps between meetings this [illegible]

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CENTER ON BUDGET AND POLICY PRIORITIES

November 8, 1999

Nickles Minimum Wage Bill Includes Costly Tax Cuts That Could Harm Lower-Wage Workers

by Iris J. Lav

Legislation Senator Don Nickles has put forth on behalf of the Republican leadership to increase the minimum wage by one dollar over three years, which is expected to be taken up on the floor this week, includes a set of tax breaks that not only would largely benefit higher-income individuals but that also are likely to lead to *reductions* in employer-provided pension and health benefits currently available to lower-wage workers.

- The bill features a series of changes in tax laws related to pensions that would make pension tax breaks considerably more lucrative for highly paid executives and other highly compensated individuals. Some of these pension provisions would allow smaller employers to retain or increase coverage for the owners and higher-paid employees while reducing coverage for more moderately-paid workers.
- A costly new "above-the-line" deduction for health insurance premiums paid by individuals who purchase their own insurance — or whose employers subsidize less than 50 percent of the cost of health insurance premiums — also is included. This provision is likely to do little to make health insurance affordable for most of the nation's uninsured, 93 percent of whom either owe no federal income taxes or are in the 15 percent bracket and thus would at most receive a subsidy of 15 cents for every dollar spent on health insurance. Moreover, because the deduction would provide a far deeper percentage subsidy for purchasing health insurance to higher-paid business owners and executives than to lower-wage earners, it could even encourage small business owners to drop group coverage (or not to institute it in the first place) and to rely on the deduction for their own coverage. To the extent this occurs, the ranks of the uninsured among lower-wage workers could increase.
- The net cost of the tax provisions in the Nickles minimum wage bill would be $18 billion over the next five years, and $76 billion over ten years. By the tenth year, the annual cost would be more than $16 billion.
- This cost is not paid for; it is simply assumed to be covered by the non-Social Security surplus. That surplus, however, has yet to materialize; projections of a sizeable non-Social Security surplus rest on the assumption that Congress will make substantial cuts in discretionary spending, an assumption that action on the current appropriations bills belies. Whether a non-Social Security surplus of any magnitude will materialize remains to be seen. Furthermore, this bill would make its inadequately designed and targeted tax cuts the first claim on such a surplus, ahead of needs in Social Security, Medicare, other emerging needs, and paying down more of the debt.

The argument usually advanced for including tax measures as an accompaniment to a minimum wage increase is that small businesses need to be compensated for the increased wages they would have to pay under a higher minimum wage. This argument is not well-founded; the evidence does not indicate that modest minimum wage increases have significantly negative effects on small businesses. For example, recent research that examined whether minimum wage increases contribute to the failure rate of businesses found "...there seems to be no discernible correlation between minimum wage increases and a rise in business failures, either in the year the increase occurred or in the following year." (1) But whatever the merits of compensating small businesses, the tax cuts in the Nickles bill go far beyond any reasonable bounds for what might be justified as measures to cushion the effects of a higher minimum wage on small businesses. In addition to providing costly tax breaks to high-income taxpayers, most of whom do not work in small businesses, the tax cuts have the potential to hurt the very workers minimum wage legislation is intended to help.

Pension Provisions Are Poorly Targeted

The Nickles minimum wage legislation includes the pension tax provisions of the tax bill Congress passed and the President vetoed this summer. These provisions have at most a tenuous connection to any problems that small businesses are said to experience as a result of a minimum wage hike.

The proposed pension changes would relax various provisions of current law that limit the contributions that highly paid individuals may make to pension plans, as well as the amount of the pension payments that such high-income individuals may receive when they retire. For example, the bill would increase the maximum tax-favored contribution that an employed individual is permitted to make to a 401(k) plan from $10,000 to $15,000. This change would primarily benefit the fewer-than-five-percent of individuals covered by a 401(k) plan who make the maximum $10,000 contribution today; this is a group that receives average pay of $130,000. The bill also would increase the maximum benefit that a retiree can receive under a defined benefit pension plan from $130,000 a year to $160,000. That change would benefit only those at the very top of the income distribution whose salaries are so large that they would be able to qualify for annual pension payments of more than $130,000 when they retire.

These and the other pension-related tax breaks in this bill have little to do with assisting small businesses. Most small businesses, in fact, do not even offer pension plans. In 1993, only 13 percent of full-time workers in firms with fewer than 10 employees — and 25 percent of workers in firms with between 10 and 24 employees — enjoyed pension coverage. It is unlikely that many small businesses with large minimum-wage workforces would be affected by these expansions in pension tax breaks.

By contrast, 73 percent of workers in firms with 1,000 or more employees have pension coverage.(2) Most of the benefit of the pension provisions in the Nickles bill would accrue to highly-salaried executives of large corporations that already offer generous pension coverage.

An analysis by the Institute on Taxation and Economic Policy finds that 91 percent of the tax benefits from the pension provisions in the vetoed tax bill would go to the 10 percent of Americans with the highest incomes. By contrast, *the bottom 60 percent of Americans would receive less than one percent of these tax benefits.* The effect of these provisions would be a significant increase in the tax-preferred benefits of high-income individuals, with little expansion for the moderate- and low-income workers — many of whom work for small businesses — who most need to build savings for retirement.

In fact, some of the pension provisions could lead to *reduced* coverage for some low- and middle-income workers. For example, the bill would raise the amount of salary on which pension contributions may be made from $160,000 to $200,000. This would enable small business owners and highly-paid executives to maintain contributions for their own pension plans while reducing the firm's contributions for other employees. Consider, for instance, the case of a small business owner with compensation of $250,000 who wants to have the business contribute $10,000 a year to his pension. Under current law, the owner would have to set the firm's pension contribution rate at 6.25 percent of pay (6.25 percent of the $160,000 limit is $10,000). Both the owner and the employees would receive contributions equal to 6.25 percent of their compensation. Under the higher $200,000 limit the Nickles bill would set, however, the business owner could reduce the firm's contribution rate for its employees to five percent and still have the firm contribute $10,000 to his own pension. The employer contribution for an employee earning $40,000 would drop from $2,500 (6.25 percent of $40,000) to $2,000 (5 percent of $40,000).(3)

Provisions in the Nickles bill also would relax pension anti-discrimination rules and other rules barring firms from treating highly compensated employees more generously than average workers. These provisions could induce further erosion in coverage among low- and moderate-paid workers.

In a November 1 letter to House Ways and Means Chairman Bill Archer commenting on the identical pension provisions in the minimum wage legislation the House is considering (H.R. 3081), Treasury Secretary Lawrence Summers and Labor Secretary Alexis Herman raise concerns about the provisions in the bill that "...raise the maximum retirement plan contribution and considered compensation for business owners and executives and weaken the pension anti-discrimination and top-heavy protections for moderate- and lower-income workers." The letter emphasizes that the "...provisions are regressive, would not significantly increase plan coverage or national savings, and could lead to reductions in retirement benefits for moderate- and lower-income workers."

Health Insurance Deductions Little Help to Uninsured

Another provision of the vetoed tax bill that is included in the Nickles minimum wage legislation would create a new tax deduction for the purchase of health insurance by taxpayers who pay at least 50 percent of the cost of their health insurance premiums. At first glance, such a deduction may seem an attractive idea if it could help the uninsured obtain coverage or help small businesses cover their employees. Closer examination indicates, however, that this deduction — which would cost upwards of $8 billion a year when fully in effect — would provide little help to most of those lacking insurance and would not significantly reduce the ranks of the uninsured. Moreover, because the deduction provides a far deeper percentage subsidy for the purchase of insurance to higher-income business owners and executives than to lower-income wage earners, it could encourage small business owners to drop group coverage and rely on the deduction to help defray the cost of their own coverage. To the extent this occurs, the ranks of the uninsured could increase.

The deduction would provide little subsidy to lower-income wage earners, including most workers who currently are uninsured and those for whom employers pay inadequate shares of premiums to make insurance affordable.(4) Some 93 percent of all uninsured individuals either have incomes too low to incur income tax liability or pay income tax at the 15 percent marginal rate. These individuals would at most get a subsidy of 15 percent of the cost of purchasing health insurance. Rather than the uninsured or the workers who today cannot afford the premiums required to obtain adequate health coverage, those who would receive the largest benefits from such a deduction are, by and large, individuals in higher tax brackets who already purchase individual insurance.

- For low- and moderate-income families and individuals without employer-sponsored coverage, a 15 percent subsidy that leaves them with the other 85 percent of the premium cost is much too small a subsidy to make insurance affordable.

  For a family earning $35,000 whose employer does not offer insurance, the proposed deduction would reduce the out-of-pocket cost of a typical family health insurance policy that carries a $1,000 deductible from $6,700 to $5,860 — or from 19 percent of income to 17 percent of income.(5) An Urban Institute study shows that more than three-quarters of low- and moderate-income uninsured individuals will not purchase insurance that consumes more than *five* percent of their income.(6) Few families that have forgone health coverage because they cannot afford to spend 19 percent of income on it would find coverage affordable because a deduction had lowered its cost to 17 percent of income. (It is of note that the child health block grant established in 1997 set a limit on the premiums and co-payments that can be charged under programs receiving block grant funds, with the limit being *five* percent of income for families above 150 percent of the poverty line and smaller amounts for poorer families.)

- This provision might be of modest help to some moderate-income families whose employer pays half or nearly half of the premium costs since the deduction would be in addition to the employer subsidy. But even families whose employers pay 50 percent of the premium would receive only very modest help from the deduction. The deduction would reduce the proportion of the premium these families have to pay only from 50 percent of the premium to 42.5 percent. While that might help some families afford insurance, the number of such families likely would be small.

- Moreover, the deduction could induce some employers currently paying more than 50 percent of premium costs to scale back their contribution to 50 percent or less or even to drop coverage.

- The group that would appear to benefit most from this deduction would be higher-income taxpayers who purchase insurance as individuals. A health insurance deduction is worth more than twice as much to affluent individuals in the 31 percent, 36 percent, and 39.6 percent brackets than to moderate- and middle-income families in the 15 percent bracket.

- The proposed new health insurance deduction would allow small business owners or more highly-paid employees to purchase insurance for themselves, using the more generous subsidy the deduction provides, without the necessity of providing coverage for lower-paid employees. As a result, the deduction could provide an incentive for some small business employers to drop group coverage, or for some owners newly launching small businesses to decide to decline to provide such coverage. To the extent this occurs, it would adversely affect some of the same workers the minimum wage legislation is supposed to help.

Other Provisions

Two other provisions in the Nickles minimum wage bill are poorly targeted. These are the deduction for the purchase of long-term care insurance and the increase in the deduction permitted for business meals.

Deduction for Long-term Care Insurance

The bill includes a provision that would allow a new deduction for 100 percent of the premiums paid to purchase long-term care insurance. This provision would cost approximately $2 billion a year when fully in effect.

There are major problems relating to access to long-term care that need to be addressed. This proposal for a deduction for long-term care insurance premiums, however, would not help most middle-income people and could exacerbate the inequities in access and affordability that currently exist.

Three-quarters of all taxpayers, including most moderate- and middle-income taxpayers, pay federal income taxes at no higher than the 15 percent marginal tax rate. For this three-quarters of all taxpayers, a deduction would provide at most a subsidy of 15 percent of the cost of purchasing long-term care insurance. Long-term care insurance premiums are relatively expensive, and a 15 percent subsidy is unlikely to make long-term care insurance fit into the budgets of many middle-income families.(7)

The primary beneficiaries of the proposed deduction are likely to be higher-income taxpayers who currently carry long-term care insurance, and taxpayers in the higher tax brackets for whom a 36 percent or 39.6 percent subsidy makes purchase of long-term care insurance an attractive option. But these are likely to be the same taxpayers for whom long-term care access is not a major problem.

Business Meals Deduction

The bill also includes a provision to increase the proportion of business meals that small businesses (businesses with receipts below $7.5 million a year) may deduct. Currently, businesses may deduct 50 percent of business meals and drinks. This limitation on the "three-martini lunch" is intended to prevent excessively luxurious dining and drinking at taxpayer expense. The Nickles bill includes a provision that would raise to 80 percent the proportion of business meals and drinks that can be deducted, at a cost to the Treasury of about $2.5 billion a year when fully in effect. (Note that this goes beyond the vetoed tax bill, which would have raised the deductible portion to 60 percent.)

End Notes:

1. Jerold Waltman, Allan McBridge, and Nicole Camhout, "Minimum Wage Increases and the Business Failure Rate," *Journal of Economic Issues*, March 1998.

2. U.S. Department of Labor, Social Security Administration, Small Business Administration, and Pension Benefit Guarantee Corporation, *Pension and Health Benefits for American Workers,* 1994.

3. The pension tax provisions in the vetoed tax bill, all of which are included in the Nickles minimum wage legislation, are explained more fully in the Center report, *Exacerbating Inequities in Pension Benefits: An Analysis of the Pension Provisions in the Tax Bill*, by Peter Orszag, Iris Lav, and Robert Greenstein, October 8, 1999. The vetoed tax bill also included provisions that would make Individual Retirement Account tax breaks more generous; these IRA changes are not included in the Nickles

minimum wage bill. (The distribution data cited above on the tax benefits that the Nickles bill pension provisions would provide thus do not cover the IRA expansions of the vetoed bill. Data on the distributional effects of the full package of retirement tax benefits contained in the vetoed bill, including the IRA expansions, are provided in *Exacerbating Inequities in Pension Benefits.*)

4. Census data show that at least 93 percent of uninsured individuals either pay no income tax or are in the 15 percent income tax bracket. Some 18 million uninsured individuals — 43 percent of all of the non-elderly uninsured — owe no income tax; their earnings are too low for them to incur an income tax liability. These uninsured individuals would receive no benefit from a tax deduction; a deduction would do nothing to make health insurance more affordable for them. Another 20 million uninsured individuals — 50 percent of the non-elderly people without health insurance — pay income tax at a 15 percent marginal tax rate. A deduction would provide these taxpayers with a subsidy equal to 15 percent of the cost of insurance not covered by an employer. General Accounting Office, Letter to The Honorable Daniel Patrick Moynihan, June 10, 1998, GAO/HEHS-98-190R, Enclosure II. The analysis is based on the 1996 Current Population Survey.

5. A General Accounting Office study found that in 1996, the middle of the range of premium costs was $5,700 for a family-coverage policy that included a $1,000 deductible. The proposed tax deduction would provide a subsidy of $840 for the purchase of a policy with a $5,700 premium ($840 equals 15 percent of $5,700). This means the family would have to pay the remaining $4,860, or 14 percent of its income, to purchase the health insurance policy. Since this premium is for a policy with a $1,000 deductible, another three percent of income would have to be expended before any benefits would be available. The family's net expenditure for health coverage — the premium plus the deductible — would total $5,860, or 17 percent of the family's income. Without the proposed tax deduction, the full cost of the policy plus the $1,000 deductible is equal to 19 percent of the family's income.

6. Leighton Ku, Teresa Coughlin, *The Use of Sliding Scale Premiums in Subsidized Insurance Programs*, Urban Institute, March 1997.

7. Long-term care premiums vary by the age at which the policy is purchased and the type and amount of long-term care expenses the policy will reimburse. A 1997 study by Consumers Union found premiums at age 55 ranged from $588 to $1,474 a year, while premiums at age 65 ranged from $1,042 to $3,100 a year. These policies cover individuals, so the costs for a couple would generally be double those amounts. *Consumer Reports*, October 1997.

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November 8, 1999
(Senate)

STATEMENT OF ADMINISTRATION POLICY

(THIS STATEMENT HAS BEEN COORDINATED BY OMB WITH THE CONCERNED AGENCIES.)

S. 625 - Bankruptcy Reform Act of 1999

(Grassley (R) Iowa and eight cosponsors)

The President supports bankruptcy reform that is balanced, would reduce abuses of the bankruptcy system, and would require debtors and creditors alike to act responsibly. Last year, the Senate produced such a balanced bill with overwhelming bipartisan support. The President is disappointed that, this year, the House failed to produce legislation that he could support. S. 625 reflects some improvements over H.R. 833 as passed by the House. The Administration, however, continues to have serious reservations about S. 625 and strongly opposes some of its provisions. For example, we are deeply concerned about a provision of the manager's amendment that adds an important "safe harbor" that protects low-income debtors from motions to deny them access to Chapter 7 under the means test, but also eliminates an essential "safe harbor" that would protect low-income debtors from coercive creditor motions that might be brought under a under a vague "totality of the circumstances" test more appropriately enforced by bankruptcy trustees and courts. The latter protection eliminated by the managers' amendment was included in the reported version of the Senate bill, the House-passed bill, and last year's conference report. The Administration's other objections to this bill are explained in detail in the Attachment.

Most of the Administration's concerns would be addressed by relevant amendments that the Administration understands will be offered on the Senate floor. The Administration's views on the anticipated amendments are also contained in the Attachment. The Administration remains hopeful that bipartisan cooperation will result in responsible bankruptcy legislation that the President can enthusiastically sign.

Finally, the Administration understands that certain non-relevant amendments will be offered as well. On November 4, 1999, in a letter to the Majority Leader, the President made clear that he strongly supports an increase in the minimum wage of $1 over the next two years; however, if Congress sends him a bill delaying the increase, repealing overtime protections for certain workers, adding costly and unnecessary tax cuts that threaten fiscal discipline and direct benefits away from working families, and thwarting ongoing efforts to enforce pension law, he will veto it.

In addition, the Administration strongly opposes the inclusion of an unrelated education amendment, a version of the Teacher Empowerment Act. When similar legislation passed the House this summer, the President indicated that he would veto it. The Administration's position on this legislation has not changed. The amendment would eviscerate the class size reduction program passed on a bipartisan basis last year and replace it with a block grant that fails to guarantee that any funds will be used to support the crucial work of reducing class sizes in the early grades. In addition, the block grant does not target funds toward the neediest students and does not include important provisions to improve teacher quality. If this amendment is attached to S. 625, the President will veto the bill.

The Administration opposes the drug-related amendment because it would reduce the current disparity between crack and powder cocaine sentences solely by increasing powder cocaine penalties dramatically instead of addressing both crack and powder cocaine penalties. Decreasing the threshold amount of powder cocaine necessary to obtain 5- and 10-year mandatory minimum sentences may be counterproductive because it could significantly redirect Federal law enforcement resources from the highest level offenders. In addition, this amendment would actually exacerbate the disproportionate impact of cocaine sentencing on minorities because, according to U.S. Sentencing Commission statistics, approximately 31% of defendants sentenced at the Federal level for powder cocaine offenses in 1998 were African American, 48% were Hispanic, and only 19% were white.

* * * * * * *

Attachment

Detailed Administration Views on S. 625 and Anticipated Floor Amendments

Access to Chapter 7. Any means test used in bankruptcy proceedings should deny access to Chapter 7 bankruptcy procedures only to those debtors who genuinely have the capacity to repay a portion of their debts successfully under a Chapter 13 repayment plan. Debtors who may be denied a discharge of their debts must be given a meaningful opportunity to have their specific circumstances considered by bankruptcy courts with the authority to determine whether they genuinely have the capacity to repay a portion of their debts. In its current form, S. 625 would use a relatively inflexible and arbitrary means test to limit access to Chapter 7. The Administration strongly opposes this provision.

As reported, S. 625 would apply rough guidelines, developed by the Internal Revenue Service (IRS) for tax repayment plans, as standards for determining debtors' ability to repay, with exceptions only for expenses that are both "reasonable and necessary." While some expense standards should be used to guide the determination of ability to repay, they should be tailored for bankruptcy. We should not simply import standards that were developed for a different purpose -- tax collection – and which are applied for that purpose with far more discretion than S. 625 would allow for bankruptcy. We note that the Congress has criticized the IRS for inadequate flexibility in using these standards for tax collection, yet this bill would use them far more rigidly for bankruptcy purposes. The Administration believes that the IRS expense formulas can be used as a starting point for developing appropriate bankruptcy guidelines, but that each system would be best served by its own appropriate standards. As House Judiciary Committee Chairman Henry Hyde has said, the use of IRS guidelines without flexibility "depriv[es] debtors and their families of the means to pay for their basic needs." As Chairman Hyde noted on the House floor, "The cost of food in Omaha, Nebraska, or Boise, Idaho, is different than in downtown Manhattan. So what is realistic about an inflexible standard?"

The Senate bill creates a largely self-executing mechanism under which elaborate debtor filings will be reviewed by United States trustees, who, based on the filings, will file a motion to deny access to Chapter 7, if the debtor has the capacity to repay or her use of Chapter 7 is abusive. As modified by the managers' amendment, the bill also gives creditors the ability to file motions to challenge the debtors' use of Chapter 7 as abusive under a vague "totality of the circumstances" test. Creditor motions alleging abuse could be used by creditors against low and moderate income debtors – who have few resources for legal advice -- to coerce or threaten them to forgo their rights. The bill should provide below-median-income debtors with a "safe harbor" from general abuse motions by creditors, as well as with the "means-test safe harbor" that the managers' amendment provides. Both are essential.

Finally, since the bill as amended by the managers' amendment precludes any party from filing a 707(b) motion alleging that a below-median income debtor has the capacity to repay under the means test, there is no justification for requiring that these debtors fulfill the elaborate means test paperwork requirements. The courts will bear unnecessary costs for collection and storage of these useless filings and they impose an unnecessary cost (and increased legal fees) on the debtor as well. These debtors should be required to provide only the information sufficient to verify their income eligibility for the "safe harbor." Similarly, a more streamlined system could screen out those with no capacity to repay before additional paperwork requirements are imposed. All parties should be able to agree that any means test should be implemented efficiently. Burdensome filing and hearing requirements that lead to little or no additional debt repayment are not in the interest of debtors, creditors, or taxpayers.

The Administration understands that a series of amendments will be offered to improve the fairness and efficiency of the means test. The Administration strongly supports these amendments, including:

- An amendment by **Senator Feingold** to clarify that the <u>long-term care expenses</u> of a debtor caring for a non-dependent parent or relative are necessary expenses under the means test;
- A similar amendment by **Senator Leahy** to clarify that certain expenses for <u>victims of domestic abuse</u> are necessary expenses under the means test;
- A similar amendment by **Senator Schumer** to clarify that <u>retraining expenses of displaced or unemployed workers</u> are necessary expenses under the means test;
- An amendment by **Senator Dodd** to address special concerns of children and families, which includes a provision to clarify that the expenses associated <u>with adopting a child</u> are necessary expenses under the means test;
- An amendment by **Senators Schumer and Durbin** to provide an appropriate <u>safe harbor</u> from all types of creditor motions and unnecessary paperwork requirements for below-median-income debtors;
- An amendment by **Senator Durbin** to <u>reduce unnecessary costs and inefficiency</u> in the reformed bankruptcy system by streamlining application of the means test and reducing costly paperwork collections without affecting debt repayment under the system;
- An amendment by **Senator Schumer** to authorize the Treasury Department, in consultation with the Executive Office for United States Trustees, <u>to modify certain of the IRS guidelines for use in bankruptcy</u> to account for variations in the cost of living; and

- An amendment by **Senator Schumer** to improve the accuracy of the means test calculation by counting all required Chapter 13 expenses (administrative costs, reasonable attorneys fees, and arrearages on other debt) in calculating capacity to repay under the means test.

Abusive Creditor Reaffirmation Practices. Much evidence shows that debtors often reaffirm unsecured debt and low-value secured debt on unfavorable terms even though they do not have the means to meet their own necessary expenses and make more important debt payments, placing such priority debts as child support and alimony obligations at risk. Such reaffirmations frequently are the result of insufficient or misleading information or threats from creditors. S. 625 as reported does little to address these abuses. If we are to provide substantial new opportunities for creditors to challenge debtors' use of the bankruptcy system under Chapter 7 of the Bankruptcy Code, we must limit abusive creditor practices such as coercive reaffirmations and violations of the automatic stay against collection actions. We understand Senator Sessions may offer an amendment to provide some protections against abusive reaffirmations. However, we believe the amendment has significant loopholes, allowing debtors to reaffirm debts they cannot afford and failing to provide creditors with all the information that bankruptcy judges deem necessary and which many are already requiring be provided in their courts. The Administration strongly supports:

- An amendment by **Senator Reed,** that protects debtors by giving them adequate information for decisions about significant reaffirmations of unsecured and low-value secured debt.

We understand, however, that Senators Reed and Sessions continue to discuss ways to reconcile their two amendments in a way that might address our concerns.

Credit Card Information and Protection. The Administration continues to believe that reform must address the factor that is most strongly correlated with the rise in personal bankruptcy: rising levels of consumer debt. Americans now receive more than 3.5 billion credit card solicitations per year, many of which are marketed to encourage consumers to carry high balances and incur large interest charges. One of the most effective ways to reduce the number of bankruptcies in this new financial era is to give consumers the information they need to manage their credit card debts effectively, recognizing the creditors' superior information and bargaining ability. Consumers must be given clear information on the terms of their credit and the financial implications of not paying off their credit card balances. The Administration supports:

- An amendment by **Senators Grassley, Torricelli, Biden, and Johnson** addressing some abusive credit practices, such as failure to disclose "teaser" rates clearly, and requiring limited generic disclosure of the impact of making only the minimum payment on credit cards. While the Grassley-Torrecelli amendment is an improvement over H.R. 833, much more should be done. The amendment creates a system that is unnecessarily burdensome for consumers who may be reluctant to call their credit card company if they are worried about their finances or are pressed for time. The Administration strongly supports:

- An amendment by **Senator Schumer** to expand coverage of the teaser rate disclosures provided under the amendment by Senator Grassley and Torrecelli to apply to applications or solicitations available to the public in catalogs, magazines, and restaurants; and

- An amendment by **Senator Dodd** to require additional information specific to the individual consumer to allow them to better understand the impact of making only the minimum payment.

Cramdowns. S. 625 also changes the lien stripping or "cramdown" provisions in current law governing a Chapter 13 bankruptcy, under which the lien underlying a secured debt is reduced to its value at the time of bankruptcy. The Administration agrees that lien stripping should be limited to automobile loans incurred in the period preceding bankruptcy to prevent abuses, but believes that the provisions in the Senate bill are excessive. While the Administration strongly prefers the Senate provisions to the extreme prohibitions in H.R. 833, the five-year prohibition on lien stripping on automobile debts in the current bill will do little more to deter bankruptcy abuses than a more reasonable time limit. Instead, the prohibition will significantly reduce repayment of priority, unsecured debts like child support and taxes. The Administration strongly supports:

- An amendment by **Senator Kohl** that would ban cramdowns of secured goods with purchase money security interests incurred within six months of the bankruptcy filing.

Nondischargeable Debts. The Bankruptcy Code makes debts nondischargeable only where there is an overriding public purpose, as with debts for child support and alimony payments, educational loans, tax obligations, or debts incurred by fraud. In an attempt to deal with the possibility of abuse, the bill makes nondischargeable debt incurred on the eve of bankruptcy and certain debts incurred to pay nondischargeable debts. Unfortunately, the amendment will catch those who innocently incur debts as well. Moreover, the additional credit card and other nonpriority debts made nondischargeable by these provisions will compete in some cases after bankruptcy with child support, alimony, taxes, and other societal priorities like educational loans and taxes. The Administration strongly prefers the provisions in S. 625, which offer some protection for child support and alimony, to those in H.R. 833. However, the Administration also strongly supports:

- An amendment by **Senator Moynihan** that would preserve the current nondischargeability rules for lower income debtors, those least likely to incur debts on the eve of bankruptcy for abusive purposes; and

- An amendment by **Senator Dodd** to address special concerns of children and families, which includes a provision to alter the bill's nondischargeability provisions to make it less likely that debts legitimately incurred to support a family will be made nondischargeable; and

- An amendment by **Senator Schumer** that would make court-ordered fines and debts resulting from abortion clinic violence nondischargeable. As the Justice Department noted in a May 14, 1999 letter to Senator Schumer, the Administration generally opposes the expansion of nondischargeable debt unless there is an overriding public policy objective and no other way to achieve that objective, but believes this amendment is a necessary tool in current efforts to end clinic violence and intimidation.

<u>Loopholes for the Wealthy</u>. The Administration supports closing loopholes in bankruptcy law, such as unlimited homestead exemptions, that allow many wealthy debtors to avoid their responsibility to repay a significant portion of their debt. Bankruptcy reform should not place a greater responsibility for debt repayment on moderate- and low-income debtors than it does on high-income debtors. The Administration strongly supports:

- An amendment by **Senator Kohl** to place <u>a reasonable limit on homestead exemptions</u>.

<u>Barriers to Entry to the Bankruptcy System.</u> Finally, the bill appears to place unnecessary barriers to entry into the bankruptcy system that will not prevent abuse, but will create burdens on those with a genuine need for speedy bankruptcy protection. The Administration strongly supports:

- An amendment by **Senator Leahy** to save the taxpayers an estimated $24 million over five years by eliminating the requirement that every debtor file three years of tax returns and instead permit any party in interest to demand the copies when needed to verify the debtor's assets and income, thus reducing filing and storage costs and unnecessary paperwork burdens; and
- An amendment by **Senator Durbin** to allow certain mandatory credit counseling to be provided over the phone.

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November 8, 1999
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STATEMENT OF ADMINISTRATION POLICY

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S. 625 - Bankruptcy Reform Act of 1999

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In addition, the Administration strongly opposes the inclusion of an unrelated education amendment, a version of the Teacher Empowerment Act. When similar legislation passed the House this summer, the President indicated that he would veto it. The Administration's position on this legislation has not changed. The amendment would eviscerate the class size reduction program passed on a bipartisan basis last year and replace it with a block grant that fails to guarantee that any funds will be used to support the crucial work of reducing class sizes in the early grades. In addition, the block grant does not target funds toward the neediest students and does not include important provisions to improve teacher quality. If this amendment is attached to S. 625, the President will veto the bill.

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- An amendment by **Senator Schumer** to authorize the Treasury Department, in consultation with the Executive Office for United States Trustees, <u>to modify certain of the IRS guidelines for use in bankruptcy</u> to account for variations in the cost of living; and

- An amendment by **Senator Schumer** to improve the accuracy of the means test calculation by counting all required Chapter 13 expenses (administrative costs, reasonable attorneys fees, and arrearages on other debt) in calculating capacity to repay under the means test.

Abusive Creditor Reaffirmation Practices. Much evidence shows that debtors often reaffirm unsecured debt and low-value secured debt on unfavorable terms even though they do not have the means to meet their own necessary expenses and make more important debt payments, placing such priority debts as child support and alimony obligations at risk. Such reaffirmations frequently are the result of insufficient or misleading information or threats from creditors. S. 625 as reported does little to address these abuses. If we are to provide substantial new opportunities for creditors to challenge debtors' use of the bankruptcy system under Chapter 7 of the Bankruptcy Code, we must limit abusive creditor practices such as coercive reaffirmations and violations of the automatic stay against collection actions. We understand Senator Sessions may offer an amendment to provide some protections against abusive reaffirmations. However, we believe the amendment has significant loopholes, allowing debtors to reaffirm debts they cannot afford and failing to provide creditors with all the information that bankruptcy judges deem necessary and which many are already requiring be provided in their courts. The Administration strongly supports:

- An amendment by **Senator Reed**, that protects debtors by giving them adequate information for decisions about significant reaffirmations of unsecured and low-value secured debt.

We understand, however, that Senators Reed and Sessions continue to discuss ways to reconcile their two amendments in a way that might address our concerns.

Credit Card Information and Protection. The Administration continues to believe that reform must address the factor that is most strongly correlated with the rise in personal bankruptcy: rising levels of consumer debt. Americans now receive more than 3.5 billion credit card solicitations per year, many of which are marketed to encourage consumers to carry high balances and incur large interest charges. One of the most effective ways to reduce the number of bankruptcies in this new financial era is to give consumers the information they need to manage their credit card debts effectively, recognizing the creditors' superior information and bargaining ability. Consumers must be given clear information on the terms of their credit and the financial implications of not paying off their credit card balances. The Administration supports:

- An amendment by **Senators Grassley, Torricelli, Biden, and Johnson** addressing some abusive credit practices, such as failure to disclose "teaser" rates clearly, and requiring limited generic disclosure of the impact of making only the minimum payment on credit cards. While the Grassley-Torrecelli amendment is an improvement over H.R. 833, much more should be done. The amendment creates a system that is unnecessarily burdensome for consumers who may be reluctant to call their credit card company if they are worried about their finances or are pressed for time. The Administration strongly supports:

- An amendment by **Senator Schumer** to expand coverage of the teaser rate disclosures provided under the amendment by Senator Grassley and Torrecelli to apply to applications or solicitations available to the public in catalogs, magazines, and restaurants; and
- An amendment by **Senator Dodd** to require additional information specific to the individual consumer to allow them to better understand the impact of making only the minimum payment.

Cramdowns. S. 625 also changes the lien stripping or "cramdown" provisions in current law governing a Chapter 13 bankruptcy, under which the lien underlying a secured debt is reduced to its value at the time of bankruptcy. The Administration agrees that lien stripping should be limited to automobile loans incurred in the period preceding bankruptcy to prevent abuses, but believes that the provisions in the Senate bill are excessive. While the Administration strongly prefers the Senate provisions to the extreme prohibitions in H.R. 833, the five-year prohibition on lien stripping on automobile debts in the current bill will do little more to deter bankruptcy abuses than a more reasonable time limit. Instead, the prohibition will significantly reduce repayment of priority, unsecured debts like child support and taxes. The Administration strongly supports:

- An amendment by **Senator Kohl** that would ban cramdowns of secured goods with purchase money security interests incurred within six months of the bankruptcy filing.

Nondischargeable Debts. The Bankruptcy Code makes debts nondischargeable only where there is an overriding public purpose, as with debts for child support and alimony payments, educational loans, tax obligations, or debts incurred by fraud. In an attempt to deal with the possibility of abuse, the bill makes nondischargeable debt incurred on the eve of bankruptcy and certain debts incurred to pay nondischargeable debts. Unfortunately, the amendment will catch those who innocently incur debts as well. Moreover, the additional credit card and other nonpriority debts made nondischargeable by these provisions will compete in some cases after bankruptcy with child support, alimony, taxes, and other societal priorities like educational loans and taxes. The Administration strongly prefers the provisions in S. 625, which offer some protection for child support and alimony, to those in H.R. 833. However, the Administration also strongly supports:

- An amendment by **Senator Moynihan** that would preserve the current nondischargeability rules for lower income debtors, those least likely to incur debts on the eve of bankruptcy for abusive purposes; and
- An amendment by **Senator Dodd** to address special concerns of children and families, which includes a provision to alter the bill's nondischargeability provisions to make it less likely that debts legitimately incurred to support a family will be made nondischargeable; and

- An amendment by **Senator Schumer** that would make court-ordered fines and debts resulting from abortion clinic violence nondischargeable. As the Justice Department noted in a May 14, 1999 letter to Senator Schumer, the Administration generally opposes the expansion of nondischargeable debt unless there is an overriding public policy objective and no other way to achieve that objective, but believes this amendment is a necessary tool in current efforts to end clinic violence and intimidation.

<u>Loopholes for the Wealthy</u>. The Administration supports closing loopholes in bankruptcy law, such as unlimited homestead exemptions, that allow many wealthy debtors to avoid their responsibility to repay a significant portion of their debt. Bankruptcy reform should not place a greater responsibility for debt repayment on moderate- and low-income debtors than it does on high-income debtors. The Administration strongly supports:

- An amendment by **Senator Kohl** to place <u>a reasonable limit on homestead exemptions</u>.

<u>Barriers to Entry to the Bankruptcy System.</u> Finally, the bill appears to place unnecessary barriers to entry into the bankruptcy system that will not prevent abuse, but will create burdens on those with a genuine need for speedy bankruptcy protection. The Administration strongly supports:

- An amendment by **Senator Leahy** to save the taxpayers an estimated $24 million over five years by eliminating the requirement that every debtor file three years of tax returns and instead permit any party in interest to demand the copies when needed to verify the debtor's assets and income, thus reducing filing and storage costs and unnecessary paperwork burdens; and
- An amendment by **Senator Durbin** to allow certain mandatory credit counseling to be provided over the phone.