

The Transformation of Bankruptcy in the United States

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The large body of empirical and theoretical literature on bankruptcy in the United States has overlooked the transformation of bankruptcy from a business-to-business collection tool to a tool used mainly by insolvent households. Occupational data on bankruptcy show that the transformation of bankruptcy occurred during the interwar years. The transformation of bankruptcy does not appear to be a business cycle phenomenon, but appears to be attributable to long run, structural changes in the economy such as an increase in the supply of consumer credit and a decline in the rate of new business formation.

By the late 1990s, Americans filed over one million bankruptcy petitions a year. More than 95 percent of these petitions were classified as non-business bankruptcy cases, and more than 99 percent were filed voluntarily by debtors. But modern bankruptcy law in the United States originated to solve an entirely different problem—business bankruptcy. In the first two decades of the twentieth century the majority of bankruptcy cases were business bankruptcy cases and over 25 percent of cases were filed involuntarily by creditors. Between the two World Wars the role of bankruptcy in the United States changed dramatically. By 1940, more than 75 percent of all bankruptcy cases were non-business cases, and creditors filed less than five percent of cases.

Previous studies of bankruptcy between the two World Wars have focused on the relationship between bankruptcy and the business cycle and have given little attention to the long run trends or to the differences between business and non-business bankruptcy.¹ The focus on the cyclical aspects of bankruptcy has diverted attention away from the transformation of bankruptcy in the U.S. economy. An occupational breakdown of bankruptcy cases shows that business and non-business bankruptcy cases followed divergent paths during the interwar period. Non-business bankruptcy cases increased rapidly during the 1920s and 1930s while the number of business bankruptcy cases plunged during the 1930s and remained low during and after World War II.

The story of the transformation of bankruptcy serves as a cautionary tale for economists concerned with the analysis of institutions, particularly legal rules. Economists have devoted considerable attention to analyzing the

effects of changes in legal rules, including bankruptcy laws, but the transformation in bankruptcy was driven by long term trends in economic organization, which in turn changed in the way people used bankruptcy law. Changes in the law itself had little impact in the long run. The rise in non-business bankruptcy began in the 1920s despite amendments intended to make bankruptcy less attractive. The decline in business bankruptcy took place in the 1930s despite amendments intended to provide more options for bankrupt businesses.

A Brief History of Bankruptcy Law in the United States

The term *bankruptcy* is often used to refer to financial failure generally, but bankruptcy has a specific legal meaning in the United States. Bankruptcy is federal law. The Constitution empowers Congress to enact “uniform laws on the subject of bankruptcy” and restricts the ability of states to provide a discharge or collect assets that are not in the state.² In addition to being federal law, modern bankruptcy law has several other defining characteristics. Bankruptcy is a collective proceeding—all of a debtor’s creditors are involved. It provides a pro rata distribution of an insolvent debtor’s assets among like creditors, and it provides a discharge to qualified debtors.

A variety of other laws regulating debtors and creditors exist in the common law and state statutes. Under these debt collection laws, when a person does not pay his or her debts, each creditor attempts to lay claim to as much of a debtor’s assets or income as is necessary to pay the debt owed him. The priority of claims is first-come, first-served rather than pro rata, leading some to refer to the laws as “grab laws.” Bankruptcy law supplements, but does not replace, grab laws. When a bankruptcy law is in effect, a creditor may still attempt to collect debts through such remedies as garnishment, but the debtor or another creditor may override the proceedings by filing a bankruptcy request.

Congress first exercised its power to enact a uniform law on bankruptcy in 1800. The debates in the *Annals of Congress* are brief but suggest that the demand for the law arose from individuals who were in financial distress.³ The law was modeled after the English bankruptcy law of the time. The law applied only to traders. A creditor could file a bankruptcy petition against a debtor, the debtor's assets would be divided on a pro rata basis among all of his creditors, and the debtor would receive a discharge. Although a debtor could not file a voluntary bankruptcy petition, it was generally believed that many debtors asked a friendly creditor to petition them into the bankruptcy court so that they could obtain a discharge. The law was intended to remain in effect for five years. Complaints that

the law was expensive to administer, that it was difficult and costly to travel to federal courts, and that the law provided opportunities for fraud led to its repeal after only two years. Similar complaints were to follow the passage of subsequent bankruptcy laws.

Bankruptcy law largely disappeared from national politics from 1802 until the Panic of 1839. The Panic of 1839 and the recession that followed it brought forward a flood of petitions and memorials for bankruptcy legislation. Memorials typically declared that many business people had been brought to ruin by economic conditions that were beyond their control, and not through any fault of their own. In the wake of the Panic, Whigs made the passage of bankruptcy relief a central part of their platform. After gaining control of Congress and the Presidency, the Whigs pushed through the 1841 Bankruptcy Act.⁴ The law went into effect on February 2, 1842.

The Bankruptcy Act of 1841 included two innovations. First was the introduction of voluntary bankruptcy, in which the debtor initiates bankruptcy proceedings. Second was the expansion of the number occupations that fell under the law. Under the 1800 Act only traders could become bankrupts. Under the 1841 Act traders, bankers, brokers, factors, underwriters, and marine insurers could be made involuntary bankrupts and any business owner could petition for voluntary bankruptcy.

Like the 1800 Act, the Bankruptcy Act of 1841 was short-lived. The 1841 Act was repealed March 3, 1843. The rapid about-face on bankruptcy was the result of the collapse of a bargain between Northern and Southern Whigs. A majority of Southern Whigs voted for passage, but they reversed their votes the next year. After repeal of the Bankruptcy Act of 1841, the subject of bankruptcy again disappeared from congressional consideration until the Panic of 1857, when appeals for a bankruptcy law resurfaced. Though demands for a bankruptcy law persisted throughout the Civil War, considerable opposition also existed to passing a law before the war was over. In the first Congress after the end of the war, the Bankruptcy Act of 1867 was enacted.⁵ The 1867 Act was amended several times and lasted longer than its predecessors, but again, complaints of excessive fees and expenses led to the repeal of the Bankruptcy Act in 1878.

Almost immediately following the repeal of the 1867 Bankruptcy Act, a well-organized movement to obtain a new bankruptcy law emerged. A national campaign by merchants and manufacturers to obtain a bankruptcy law began in 1881 when The New York Board of Trade and Transportation organized a National Convention of Boards of Trade.⁶ After failing to obtain passage of a bankruptcy law, associations of merchants and manufacturers met again

in 1889. Under the name of The National Convention of Representatives of Commercial Bodies they held meetings in St. Louis and Minneapolis.⁷ The president of the Convention, a lawyer and businessman named Jay Torrey, drafted a bill for which the Convention lobbied throughout the 1890s.

The merchants and manufacturers who lobbied for bankruptcy law provided credit to their customers whenever they delivered goods in advance of payment. The trade credit provided by merchants and manufacturers was often the primary source of credit for retailers.⁸ This trade credit was generally unsecured, and formal contracting was kept to a minimum.⁹ Informal trade credit worked well in spite of high levels of business failure.¹⁰ However, sometimes debtors failed to pay. Without a federal bankruptcy law, collection proceeded under state law. Creditors were troubled by three features of state law. First, the details of collection laws varied from state to state, forcing creditors to learn the laws in all the states in which they wished to sell goods. Second, many state laws discriminated against creditors who were not citizens of the state. Third, many of the state laws provided for a first-come, first-served distribution of assets rather than a pro rata division.

The first-come, first-served rule of collection created incentives for creditors to race to be the first to file a claim. The effect of this rule was described by Jay Torrey: "If a creditor suspects his debtor is in financial trouble, he usually commences an attachment suit, and as a result the debtor is thrown into liquidation irrespective of whether he is solvent or insolvent. This course is ordinarily imperative because if he does not pursue that course some other creditor will."¹¹ Thus collection law could actually precipitate business failures. In contrast, a successful bankruptcy law should reduce business failures and bankruptcy by giving debtors more time to meet creditor demands and by encouraging out-of-court settlements.

As early as 1884, the Republican Party supported the bankruptcy bills put forward by the merchants and manufacturers. It took nearly twenty years to enact bankruptcy legislation because the Democratic Party supported bills that were purely voluntary (creditors could not initiate proceedings) and temporary (the law would only remain in effect for a few years). The requirement that the law be temporary was crucial to Democrats because a vote for a permanent bankruptcy law would have been a vote for the expansion of federal power and against states' rights, a central component of Democratic policy.¹² Throughout the 1880s and 1890s, votes on bankruptcy split strictly along party lines. Because control of Congress was split between the two parties for most of the last quarter of the nineteenth century, neither side could force through their version of bankruptcy law. This period of divided

government ended with the 55th Congress, in which the Bankruptcy Act of 1898 was passed.

The 1898 Act allowed individuals and businesses to file voluntary bankruptcy petitions. It allowed creditors to file involuntary petitions against most businesses, but prohibited involuntary petitions against farmers or wage earners. The Act provided for the liquidation of a debtor's non-exempt assets and a discharge of the remaining debts. Creditors were grouped into different classes based on the priority of their claims, and all creditors of a similar class received a pro rata distribution of the proceeds of liquidation. The Act also included a provision for composition, or voluntary agreements about the payoff of debt, but a composition had to be approved by a group of creditors who constituted a majority in both number and claims.¹³ In a compromise with advocates of states' rights, the 1898 Act allowed exemptions to be determined by the states.

Numerous small amendments were made to the Bankruptcy Act in the first decades of the twentieth century.¹⁴ Most of these amendments were intended to make it more difficult to obtain a discharge. In the late 1920s, concerns about rising rates of bankruptcy and corruption in bankruptcy administration led to two major government investigations.¹⁵ In the 1930s, Congress passed significant amendments to the Bankruptcy Act.¹⁶ The original 1898 Bankruptcy Act was almost solely directed at liquidation; amendments passed in 1933, 1934, and 1938 introduced alternatives to liquidation: wage earner workouts, business arrangements, and corporate reorganization. In contrast to the late nineteenth century, when business associations played a leading role in shaping bankruptcy legislation, bankruptcy lawyers and judges took the lead in shaping the amendments of the 1930s.¹⁷

A steady increase in bankruptcy filings in the 1960s prompted Congress to form a committee to investigate bankruptcy in 1970. The committee presented its report in 1973, and in 1978 Congress passed the Bankruptcy Reform Act. Bankruptcy scholars typically refer to the 1898 law as the Bankruptcy Act and the 1978 law as the Bankruptcy Code, or simply the Code. Although the Code retained the functional features and organization of the Bankruptcy Act, the Code completely replaced the Act. In particular, the Code changed the law regarding personal bankruptcy to make it possible for the debtor to retain more property and to make it easier for a debtor to obtain a discharge. Unlike the intense political conflicts of the late nineteenth century, the 1978 law generated little political heat.¹⁸

In the 1980s and 1990s creditors again lobbied intensely for bankruptcy legislation. In contrast to the 1880s and 1890s, creditors focused their attention on personal bankruptcy rather than business bankruptcy.¹⁹ The changes in lobbying efforts over the century reflect the transformation of bankruptcy in the U.S. economy .

The Transformation of Bankruptcy Described

Previous research on bankruptcy before World War II has focused on the relationship between bankruptcy and business cycles.²⁰ Ben Bernanke argues that bankruptcy, like bank failures, played an important role in lengthening the Great Depression. As the Great Depression began, both nominal incomes and prices fell, resulting in an “erosion of borrowers’ collateral relative to debt burdens.”²¹ Lenders could continue to use simple non-contingent contracts and face a higher risk of default, or they could write more elaborate contracts. Either way, the cost of credit intermediation increased and the equilibrium quantity of lending decreased. The threat of bankruptcy may have inhibited recovery. Bernanke does not directly examine data on bankruptcy cases, but instead uses the liabilities of commercial failures because Dun and Bradstreet published information on commercial failures monthly while information on bankruptcy was only published annually. He finds that including the liabilities of commercial failures adds to the explanatory power of a model in which un-anticipated monetary and price shocks influence the level of industrial output. Daniel Schiffman finds support for Bernanke’s approach in the behavior of railroads during the Depression.²²

Bernanke focuses on commercial bankruptcy; Martha Olney builds a similar argument regarding consumer default.²³ Olney shows that in the late 1920s and early 1930s the laws governing installment contracts were particularly harsh on defaulting debtors. As household income fell during the Great Depression, people drastically reduced their consumption expenditures in an attempt to avoid defaulting on installment payments. Again, the threat of bankruptcy may have inhibited recovery.

Alexander Field criticizes Bernanke’s approach to bankruptcy.²⁴ Field argues that the downturns in income and increases in household debt explain nearly all of the increases in bankruptcy, and that increases in bankruptcy are unlikely to have further depressed income, but Field’s analysis is problematic.

Field offers ordinary least squares regressions of the determinants of bankruptcy filings to support his argument that personal income and debt levels drove changes in bankruptcy filings. The independent variables are personal income, debt (loans of all U.S. banks, 1919 to 1941, and loans of commercial and mutual savings banks, 1942 to 1946), and bankruptcy filings lagged one year. He does not control for the wars or for any of the amendments to the law in 1922, 1926, 1933, 1934 and 1938. The dependent variables are statistically significant at the five percent

level and the variation in the independent variables explain more than 90 percent of the variation in the dependent variable. He concludes from his regressions that “over the critical quarter century explored one can demonstrate a stable relationship between income, debt and bankruptcy...”²⁵

The apparent stability of the relationship, however, arises from a failure to distinguish between business and non-business bankruptcy. Field’s failure to distinguish between business and non-business cases may stem from a misreading of the available data. He states that, “For 1940 onward, data on the number of cases filed and concluded remains available on a disaggregated basis, but information on liabilities and occupations is not.”²⁶ This statement is incorrect. As the Appendix 1 describes, responsibility for reporting on bankruptcy shifted in 1940 from the Attorney General to the Administrative Office of the U.S. Courts, but the Administrative Office continued to use the same occupational categories as the reports of the Attorney General.²⁷ It is also possible that Field has missed clues about the importance of business bankruptcy in recent research. Recent studies have emphasized the importance of business bankruptcy to advocates of bankruptcy legislation in the nineteenth century.²⁸ Field’s interpretation of the history of bankruptcy legislation, however, is based solely on classic works by Charles Warren and Harold Remington and does not cite any of the research published in the last fifty years.²⁹

Separating business and non-business bankruptcy cases results in a picture of bankruptcy during the inter-war period that is very different from the one that Field paints. Figure 1 shows business (merchant, manufacturer, and farmer) and non-business (wage earner) bankruptcy cases from 1899 to 1970. During the 1920s and 1930s business and non-business bankruptcy cases moved in opposite directions. The decline that Field finds in bankruptcy filings in the late 1930s was driven solely by the decline in business bankruptcy. Non-business bankruptcy cases continued to rise until 1941, and even in 1942 numbered twice what they had been in 1930. Non-business bankruptcy resumed its rapid ascent again after the war. Business bankruptcy, on the other hand remained well below its prewar levels for the next quarter of a century.

The Rise of Non-Business Bankruptcy

Non-business bankruptcy is primarily wage earner bankruptcy. Wage earner bankruptcy cases account for at least 89 percent of all non-business bankruptcy cases every year from 1936 to 1970. Bankruptcy law prohibits involuntary bankruptcy petitions against wage earners. Wage earners choose to file bankruptcy petitions.³⁰ The

immediate force behind that choice is usually the desire to head off debt collection efforts, such as garnishment. Case studies of personal bankrupts in the 1920s revealed that personal bankruptcy petitions were usually filed to prevent garnishment.³¹ One bankruptcy referee estimated that 85 percent of the cases he handled were due to garnishment.³² In Texas, where there was no law for garnishment at the time, only 5 percent of all cases were wage earner cases.³³ Garnishment was widely regarded as a threat to employment. In his study of bankruptcy in Chicago, John Cover concluded that, “Many firms resent the responsibility imposed by such court judgments and regard critically the employee who finds himself in this predicament.”³⁴ Collection efforts still tend to be the immediate precipitant of non-business bankruptcy petitions today.³⁵

Because of a rapid increase in bankruptcy petitions in the 1980s and 1990s, economists and other social scientists have devoted a good deal of attention to the factors that influence the decision to choose bankruptcy. Attempts to explain why more people chose bankruptcy in the last two decades of the twentieth century tend to fall into two groups. One group emphasizes changes in the law or social norms that lowered the cost of choosing bankruptcy. The other group emphasizes changes in the availability of credit or the instability of household income that made people more likely to become insolvent.

In the early 1980s, several studies concluded that the Code (a.k.a. the Bankruptcy Reform Act of 1978) made personal bankruptcy relatively more attractive.³⁶ Doubts were raised about this explanation when the rate of filings continued to increase even after the implementation of 1984 amendments that were intended to make the law less debtor-friendly. Rapid increases in personal bankruptcy in a number of other countries also raised doubts about explanations that emphasize legal changes within the United States.³⁷ Subsequent studies challenged the initial findings on the importance of the legal changes and attempted to provide alternative explanations of the increase in bankruptcy filings. Ian Domowitz and Thomas Eovaldi downplay the impact of the legal changes and emphasize the downturn in the economy in the early 1980s.³⁸

But as the economy recovered from the downturn of the early 1980s, personal bankruptcy did not fall, which raises more doubts about the significance of the business cycle as an explanation of growth in bankruptcy. Frank Buckley and Margaret Brinig argue that the stigma associated with default has diminished. They argue that households are both more willing to take on debt and more willing to declare bankruptcy because the cost of bankruptcy, in terms of social stigma, has decreased.³⁹ Scott Fay, Erik Hurst and Michelle White add that as more

people have declared bankruptcy, information about bankruptcy has become more readily available to others, making it easier for them to choose bankruptcy.⁴⁰ Using data on credit card holders, David Gross and Nicholas Souleles find evidence that, holding other factors constant, the likelihood of personal default increased in the 1990s.⁴¹

Bhandhari and Weiss used time series analysis of bankruptcy filings to argue that changes in the law were relatively unimportant and that the increase in bankruptcy can largely be explained by the increase in debt to income ratios.⁴² Moss and Johnson find that debt loads increased, and that the proportion of debt held by low income households increased. They argue that the Supreme Court's decision in 1978 that usury limits on credit cards would be those of the state the card was issued from rather than the state of the cardholder led to the deregulation of interest rates.⁴³ Credit card issuers moved to states with no usury laws and some states reacted by eliminating their usury laws.⁴⁴ Low-income households that had been unable to obtain credit cards when usury laws were in effect were able to obtain high interest credit cards. Moreover, low-income households were more likely to experience decreases in incomes leading them to default. Teresa Sullivan, Elizabeth Warren and Jay Westbrook conclude from an examination of a survey of bankrupts that increased instability of incomes is the primary force behind the increase in bankruptcy.⁴⁵ In short, disagreements about the cause of increases in bankruptcy tend to revolve around the question: Is a person more likely to go bankrupt because she has more debt, or does a person have more debt because she is more likely to go bankrupt?

Experts asked the same questions about personal indebtedness as they observed increases in personal bankruptcy in the 1920s. Contemporaries wondered about innovations in credit markets, changes in the law and declining social stigma in the 1920s.⁴⁶ For instance, Rolf Nugent believed that the decline of stigma toward indebtedness led to increased consumer debt loads and that, "The indifference to debt has produced more consumer bankruptcies."⁴⁷ A government investigation of bankruptcy published in 1932 suggested that the ease with which one might obtain a discharge contributed to the increase in bankruptcy cases.⁴⁸ In contrast, some legal scholars believed that the rapid increase in personal bankruptcy cases was attributable to changes in the supply of credit, rather than changes in the law or changes in attitudes toward debt.⁴⁹ The majority of evidence from the 1920s tends to support an emphasis on credit supply innovations, rather than legal or cultural changes, as the primary determinants of bankruptcy rates. The driving force behind the rise in bankruptcy was not an increase in the likelihood that a household with debt would default. The driving force was the increase in the number of households

with debt.

The general drift of bankruptcy legislation through the 1920s was to make the Bankruptcy Act less friendly, rather than more friendly, to debtors. In 1903, the law was amended to make it more difficult for a debtor to receive a discharge and to make it easier for creditors to obtain information from bankrupts.⁵⁰ An amendment made in 1910 went on to further toughen the law. Joseph Sherley, the sponsor of the amendment in the House, declared that, "It is generally admitted that the law as originally passed was weak in so far as it tended to prevent the discharge of dishonest debtors. It was much strengthened by the amendments of 1903. It should be still more strengthened."⁵¹ Amendments of the law in 1926 increased the number of causes for which a discharge might be denied and "increased the number of criminal acts and the punishments of those directly or indirectly associated with any fraud with going into and through bankruptcy."⁵² Critics of the law argued that the attempts to make a discharge more difficult to obtain were ineffective. Even after the 1926 Amendments less than one percent of discharges were denied.⁵³ While the amendments to the law may not have had their desired impact, it is clear that changes in the law did not make it easier to obtain a discharge.

Evidence on consumer default rates also weighs against a decline in social stigma as a cause of the increase in bankruptcy cases. If people felt less compelled to repay their debts because of declining social stigma, one would expect to see evidence of increases in the default rate. The available evidence indicates that the rate of default on consumer credit remained low throughout the 1920s. The loss ratio for General Motors Acceptance Corporation never reached one percent. Moreover, the loss ratio fell over the course of the decade. Alfred P. Sloan reported the loss ratio in 1919 and 1920 as 0.502 percent and 0.918 percent. By 1922 and 1923 the loss ratio had fallen to less than 0.1. Sloan reported that even at the lowest point of the Depression in 1933, the loss ratio only rose to 0.83.⁵⁴ GMAC was not unique. The rate of repossession for new cars did not rise above 3 percent throughout the second half of the 1920s.⁵⁵ The personal loan industry reported extremely low rates of loan losses. Clark Evans declared that, "Almost universal experience shows a loss ratio of less than one per cent of the total loans or credit advanced and only in the rarest cases do such organizations show as high a ratio as two per cent."⁵⁶ A study of small loan agencies in Massachusetts in 1928 reported that total losses were 0.4, and that 58 percent of the agencies reported no losses.⁵⁷ Research by Martha Olney indicates that households desperately tried to avoid default during the 1920s, even in the face of large decreases in income.⁵⁸

How does one reconcile low and stable default rates with rapidly rising non-business bankruptcy? The answer lies in the increased supply of consumer credit.⁵⁹ Although the likelihood that a particular debtor would default did not increase during the 1920s, the number of households with significant consumer debt did increase. An increase in the number of households with debt will result in an increase in the number of defaults even if the probability of default among debtors remains constant. Figure 2 shows the relationship between the ratio of consumer debt to personal income and the number of non-business bankruptcy cases from 1919 to 1946. Non-business bankruptcy cases follow movements in the debt to income ratio almost perfectly. Using just non-business bankruptcy cases also fits Field's basic story about the influence of debt and income on bankruptcy better than the total filings that he used. The debt to income ratio peaks in the early 1940s when wage earner bankruptcy cases peak rather than in the mid-1930s when total filings peak. The evidence does not, however, fit a simple business cycle story. The number of non-business bankruptcy cases rose in both contraction and expansion.

The increase in the debt-to-income ratio was not just a matter of the same households taking on more debt, but an expansion in the number of indebted households. Increased household indebtedness was driven by innovations in credit supply.⁶⁰ Finance companies were created to finance inventories of retailers, and buying on installment became ubiquitous.⁶¹ For instance, the percentage of households that purchased automobiles on installments increased from 4.9 percent in 1919 to 15.2 percent in 1929.⁶² In 1925 10 percent of households had radios; by 1930 46 percent had radios. E. R. A. Seligman estimated that, as of 1927, 75 percent of radios were bought on time.⁶³

Installment credit was not the only area where innovation took place. The adoption by the states of the Uniform Small Loan Law served much the same role in the 1920s that deregulation of credit card interest rates did in the 1980s and 1990s. A coalition of small lenders and the Russell Sage foundation drafted a Uniform Small Loan Law that many states enacted. The law provided for licensing of small lenders and allowed them to charge higher interest rates than most usury laws had allowed. It may seem that a usury law that sets maximum interest rates should benefit the poor, but because the costs of lending to the poor are high relative to the amounts borrowed, conventional lenders typically do not find small debts profitable. In the absence of a legal small debt market, poor borrowers have to turn to unregulated lenders. The Uniform Small Loan Law raised legal interest rates on small debts, but made it possible to obtain these debts from legitimate businesses.⁶⁴ Lenders also developed new methods for securitization

of commercial and residential mortgages.⁶⁵

The rise of non-business bankruptcy affected the performance of the bankruptcy system. Creditors had virtually no interest in participating in most wage earner bankruptcy cases. The number of “no asset” cases rose in step with wage earner bankruptcy. The Boston study of personal bankrupts found that in 85 percent of wage earner cases the debtor had no assets, and in an additional 9.4 percent of cases the debtor had less than \$100 in assets. Among farmers and professionals, debtors had no assets in 65 percent of cases.⁶⁶

The rapid increase in personal bankruptcy led the authors of the Department of Commerce’s 1929 to 1930 study of business failures in New Jersey to question, “whether the law is being put to the use that it was intended, and whether the law and its administration are particularly suitable for changed economic and social conditions.”⁶⁷ Judge Thacher’s report on bankruptcy argued that the 1898 Bankruptcy Act had been grounded on the assumption of creditor participation. Creditors were expected to play an active role in the examination of bankrupts, insuring honesty and the highest possible dividends. His report declared that the 1898 Act had been “carefully drawn and thoroughly considered,” but concluded that, “under the stress of greatly changed social and economic conditions it has had quite unforeseen consequences, the most serious of which have resulted from a failure of the theory that creditors can be relied upon to take charge of the management and enforcement of the act.”⁶⁸ In the majority of cases creditors had no incentive to take charge of the management and enforcement of the 1898 Act.

The Decline of Business Bankruptcy

The rapid rise of voluntary wage earner bankruptcy cases would have been enough to transform the bankruptcy system, but it was compounded by an equally dramatic decline in business bankruptcy cases. Business bankruptcy cases numbered over 20,000 a year in the mid 1920s and rose to 25,353 in 1933. They fell to a low of 697 in 1946, and by 1970 still numbered only 5,929. The decline in business bankruptcy was also associated with a decline in involuntary bankruptcy. Involuntary petitions numbered over 5,000 a year from 1921 to 1932, and went as high as 9,286 in 1922. By 1940, involuntary petitions had fallen to 1,752 and never again rose above 2,000. Given the importance of bankruptcy law to turn-of-the-century merchants and manufacturers, why did bankruptcy law as a tool for collecting debts from other merchants and manufacturers virtually disappear?

For some entrepreneurs, bankruptcy court is the end of a journey that began with great hopes.

Entrepreneurs enter a market when they think there is a profitable opportunity.⁶⁹ Many of them are mistaken. They earn negative economic profits and eventually exit the market. Most of these entrepreneurs are able to pay off their debts as they exit, but some default on their debts. Some of the entrepreneurs who default end up in bankruptcy court. A decline in the number of business bankruptcy cases must be the result of either a decline in the number of businesses that default, a decline in the number of defaulting business that end up in bankruptcy, or a decline in both. As with the rise in non-business bankruptcy, changes in the law do not provide an explanation for the decline in business bankruptcy. The amendments to the bankruptcy law for businesses in the 1930s added options for corporate reorganization and business arrangements. The amendments of 1933 and 1934 introduced corporate reorganization into bankruptcy law. In 1933, Congress added section 74 (arrangements of unsecured debts of unincorporated business), section 75 (adjustments for farmers) and section 77 (railroad reorganization). In 1934, Congress added section 77b (which made it possible for any corporation to attempt reorganization). In 1938, Congress passed the Chandler Act, extensively amending the Bankruptcy Act. The Chandler Act created Chapter XI (arrangements for small businesses), Chapter X (corporate reorganization), and Chapter XIII (wage earner workouts).

All of the options incorporated into bankruptcy law in the 1930s originally evolved outside of bankruptcy court as alternatives to liquidation. Corporate reorganization evolved in the nineteenth century to deal with railroad failures.⁷⁰ Judges used receiverships to facilitate financial reorganization of insolvent railroads. Although receivership enabled railroads to avoid liquidation, lawyers for insolvent railroads complained that receivership was a cumbersome procedure for reorganization. A separate receivership had to be established in each jurisdiction in which the railroad operated and dissenting creditors could create a holdup problem by demanding that they be paid in full rather than participate in a reorganization plan.⁷¹ Lawyers and investors in non-railroad corporations also complained because courts would not use receiverships to facilitate reorganizations for them. Receivership for the purpose of reorganization was restricted to corporations in which there was deemed to be a strong public interest, such as railroads.⁷² Business arrangements became common in the years after the Bankruptcy Act was passed. By 1920, adjustment bureaus sponsored by the National Association of Credit Men operated throughout the country.⁷³ The Thacher report on bankruptcy devoted a great deal of attention to these alternatives to liquidation and argued that they should be incorporated in to the bankruptcy law.⁷⁴

Adding options for arrangement or reorganization would seem to make bankruptcy more attractive. It is

possible, however, to argue that adding these options to bankruptcy law would encourage private arrangements instead of bankruptcy. Albert Chapin argued in his text on credit and collections that “creditors can now negotiate with a debtor openly and unhurriedly before any action is instituted for they need not fear a nuisance minority which, prior to the [Chandler] Act, could always disrupt negotiations by throwing a debtor into bankruptcy.” He concluded that “there should be possible the effectuation of many an honest adjustment without resorting to court procedure at all.”⁷⁵ Late nineteenth century proponents of bankruptcy legislation had argued that bankruptcy law would facilitate out-of-court settlements; Chapin and others extended this argument to the incorporation of reorganization procedures into bankruptcy law.

If the amendments to the bankruptcy law facilitated private arrangements, then the gap between the number of businesses that defaulted and the number of businesses that ended up in bankruptcy court should have widened. Just the opposite occurred. Dun and Bradstreet, and their predecessor firms, published estimates of the number of business that defaulted beginning in the 1870s. The estimates are based on firms listed in Dun and Bradstreet’s Reference Book, which includes firms that seek commercial credit. The majority of the firms included are merchants and manufacturers. Certain types of firms, such as railroads, financial firms, and farms are explicitly excluded. Although Dun and Bradstreet refer to them as business failures, business default is a more apt term, since they are defined as “concerns involved in court procedures or voluntary actions, probably ending in a loss to creditors.”⁷⁶ Business failures include firms that are involved in bankruptcy proceedings, and also firms that are involved in private arrangements and firms that are involved in legal proceedings under state or common law. Dun and Bradstreet referred to firms that ceased to exist as discontinuances. Figure 3 shows the number of merchants that defaulted, as estimated by Dun and Bradstreet, and the number of merchants that went through bankruptcy proceedings.⁷⁷ Figure 4 shows the number of manufacturers that defaulted and the number of manufacturers that went through bankruptcy proceedings. Both figures make clear that the decline in business bankruptcy in the 1930s was part of a decline in the total number of business defaults rather than a movement away from bankruptcy.

Manufacturers appear to have been somewhat more likely to use bankruptcy after corporate reorganization and business arrangements were added. Bankrupt manufacturers were also much more likely to have been organized as corporations. Between 1933 and 1939 the Attorney General published information on the form of organization of bankrupt businesses. The percentage of manufacturers organized as corporations was never less than 60 percent,

while the percentage of merchants organized as corporations was never as high as 20 percent.⁷⁸

The decline in business default and in business bankruptcy correspond to a decline in the rate of new business formation. Figure 5 shows new business formation, business discontinuances, and business bankruptcies from 1900 to 1941. When new business formation increases, business discontinuances and business bankruptcy cases rise. When new business formation decreases, business discontinuances and business bankruptcy cases fall.⁷⁹ Sarah Lane and Martha Schary arrived at a similar conclusion regarding the number of businesses that defaulted between 1946 and 1986. Using Dun and Bradstreet data, they found that a firm's age was "the largest determinant of its probability of failure."⁸⁰ Consequently, they concluded that "periods with rapid rates of firm formation should lead to periods of high failure rates since more young firms will exist in the economy."⁸¹ Unfortunately, the Dun and Bradstreet series on new business formation and discontinuance does not extend past 1941, but the shift from business bankruptcy to wage earner bankruptcy is also consistent with well known changes in labor markets. As the rate of self-employment declined during the twentieth century, business bankruptcies declined and wage earner bankruptcies increased.⁸²

As with non-business bankruptcy, the available evidence indicates that the number of business bankruptcy cases was not strongly influenced by legal changes or short run business cycle movements. Instead, both business and non-business bankruptcy were primarily determined by long run changes in the economy.

Conclusion

Long run changes in the economy in the 1920s and 1930s transformed the role of bankruptcy in the United States. An increase in the supply of credit to households led to a rise in wage earner bankruptcy cases in the 1920s and 1930s. A decline in new business formation that began in the 1930s led to a decline in business bankruptcy. By the beginning of World War II bankruptcy law was no longer the business-to-business collection tool that it had been through World War I.

The transformation of bankruptcy in the interwar period suggests the value of taking a long-term perspective in analyzing bankruptcy. At any given time the number of business or non-business bankruptcy cases was determined more by the long term movements than by short term fluctuations. To a great extent, trends in bankruptcy appear to have been little influenced by legal changes as well. The attempts to make the law stricter that

took place on a regular basis until the 1930s did little to stem the rising tide of wage earner bankruptcy cases. Similarly, the primary effect of the 1930s amendments seems to have been on the percentage of defaulting manufacturers who ended up in bankruptcy court.

The small effect of the legal changes should caution economists about the ability of particular institutions to influence people's choices in the face of countervailing economic forces. The transformation of bankruptcy also suggests that economists should be cautious in their predictions about the effects of different legal rules. During the first two decades of the twentieth century the 1898 Bankruptcy Act seemed to be very much the law its proponents had intended. Over the next two decades the Bankruptcy Act of 1898 produced very different results as the economy evolved. When the percentage of non-business cases increased so did the percentage of no-asset cases. As critics at the time observed, no-asset cases tended to undermine the principle of creditor participation that the Act had been built around. While the primary features of the Bankruptcy Act remained unchanged, its function had been almost completely transformed.

Appendix 1

The 1898 Bankruptcy Act required the Attorney General to report on the administration of bankruptcy law in the United States. The reports of the Attorney General provide information on the number of cases filed at the national level and in each state, and whether the cases filed were voluntary or involuntary. The reports of the Attorney General also provide information on the number of cases closed (as opposed to cases filed) that fell into particular occupational categories. Through 1932, the categories of occupations listed were merchant, manufacturer, wage earner, farmer, professional, and miscellaneous. From 1933 to 1939, professionals were lumped with wage earners rather than listed separately, and miscellaneous cases were divided into business and non-business categories rather than a single category.

In 1940, the Administrative Office of the U.S. Courts took over responsibility for reporting on bankruptcy administration. The reports of the Administrative Office continue to provide state-by-state filings as well as an occupational breakdown of cases. The Administrative Office adopts the categories used by the Attorney General as of 1933: merchant, manufacturer, farmer, wage earner, professional, miscellaneous in business, and miscellaneous not in business. The Administrative Office, however, reports occupations for cases filed rather than cases closed.⁸³

To compensate for inconsistencies in the occupational categories reported, our business bankruptcy series in Figure 1 includes only merchants, manufacturers and farmers; the non-business bankruptcy series includes only wage earner cases. Professionals are excluded because they are lumped with wage earners from 1934 to 1939 and miscellaneous cases are excluded because it is not possible to tell how many were business and how many were non-business prior to 1936. There are three potential problems with our classification of cases: (1) the switch in 1940 to reporting cases filed rather than cases closed, (2) the inclusion of professionals with wage earners from 1933 to 1939, and (3) the exclusion of miscellaneous cases from our data. None of these problems is capable of altering the overall conclusion that bankruptcy shifted away from business bankruptcy and toward non-business bankruptcy during the inter-war period.

The switch from cases filed to cases closed causes little distortion in the series. The correlation coefficient of the cases closed and cases filed is .977 for the years from 1899 to 1939. The series track each other closely throughout the period, suggesting that changes in the number of cases closed is likely to be a good proxy for changes in cases filed, particularly since we are concerned with long term trends rather than short term fluctuations.

The inclusion of professionals in the wage earner category tends to bias the number of non-business cases upward from 1934 to 1939, but the bias is relatively small. In 1933, there were 27,262 wage earner cases and 2,025 professional cases. In 1940, there were 36,846 wage earner cases and 799 professional cases.

Excluding miscellaneous cases from our series leads us to understate the shift from business bankruptcy to non-business bankruptcy. Miscellaneous cases account for between 10 and 20 percent of all cases in every year. In the late 1930s, between 55 and 62 percent of all miscellaneous cases are classified as business by the Attorney General. In the 1960s, the percentage of miscellaneous cases that are classified as business is never over 45 percent and after 1963 does not rise above 38 percent. The business portion of miscellaneous cases becomes smaller over time, while the business portion of all bankruptcy cases was declining as well.

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Table A.1

Bankruptcy Cases by Occupation, 1899 to 1970

Year	Farmers	Wage		Mfgs.	Professionals ^a		Misc. ^b	Total
		Earners ^a	Merchants		Professionals ^a	Misc. ^b		
1899	1,926	5,317	5,894	506	579	5,569	19,791	
1900	2,064	7,580	5,286	563	518	4,781	20,792	
1901	1,464	7,164	3,313	304	426	1,799	14,470	
1902	1,327	6,923	3,125	322	539	1,922	14,158	
1903	977	4,654	3,956	459	490	2,173	12,709	
1904	884	5,414	4,257	407	211	1,150	12,323	
1905	832	5,645	4,562	502	143	1,001	12,685	
1906	844	3,188	2,865	608	465	2,722	10,692	
1907	1,065	3,380	4,512	953	272	2,047	12,229	
1908	835	3,510	4,179	615	250	2,437	11,826	
1909	797	3,534	4,568	662	223	2,058	11,842	
1910	849	4,376	5,277	926	356	3,011	14,795	
1911	679	4,185	4,971	789	314	3,212	14,150	
1912	837	4,646	5,338	841	422	3,505	15,589	
1913	942	4,895	6,652	848	333	4,034	17,704	
1914	1,045	5,798	6,302	894	418	4,284	18,741	
1915	1,246	6,659	7,482	1,208	395	4,243	21,233	
1916	1,658	6,458	9,086	1,228	551	4,950	23,931	
1917	1,906	7,817	8,657	1,202	584	5,099	25,265	
1918	1,632	8,246	7,054	966	559	5,005	23,462	
1919	1,207	6,779	5,599	842	528	4,346	19,301	
1920	997	5,634	3,873	673	507	3,899	15,583	
1921	1,363	5,920	3,740	580	299	3,260	15,162	

1922	3,236	7,552	6,469	811	350	4,044	22,462
1923	5,490	10,237	10,740	1,319	491	5,509	33,786
1924	7,772	13,102	12,045	1,525	662	6,418	41,524
1925	7,872	14,429	11,455	1,478	764	8,238	44,236
1926	7,769	16,806	11,734	1,435	1,018	8,287	47,049
1927	6,296	18,500	12,044	1,394	1,214	8,618	48,066
1928	5,679	21,590	13,804	1,372	1,322	9,677	53,444
1929	4,939	25,503	13,965	1,446	1,353	9,691	56,897
1930	4,464	28,989	13,479	1,383	1,378	10,662	60,355
1931	4,023	29,693	13,459	1,336	1,292	10,302	60,105
1932	4,849	29,655	15,606	1,466	1,506	10,197	63,279
1933	5,924	27,436	17,944	1,577	2,026	12,124	67,031
1934	4,719	28,911	11,442	1,765	---	12,233	59,070
1935	4,315	31,677	7,891	1,288	---	11,312	56,483
1936	3,646	32,907	5,485	938	---	9,353	52,329
1937	2,482	37,837	4,887	811	---	9,095	55,112
1938	1,800	35,166	2,575	2,095	---	7,970	49,606
1939	1,426	30,789	3,838	796	---	6,684	43,533
1940 ^c	2,678	36,846	4,651	921	799	6,424	52,319
1941	2,367	42,348	4,378	766	744	5,829	56,432
1942	2,048	40,180	3,386	507	581	5,407	52,109
1943	1,151	27,020	1,775	286	395	4,084	34,711
1944	512	15,460	554	181	211	2,615	19,533
1945	305	10,010	287	153	152	1,955	12,862
1946	260	7,618	236	201	112	1,769	10,196
1947	183	9,396	631	596	111	2,253	13,170
1948	167	12,456	1,338	808	114	3,537	18,420

1949	232	17,772	1,969	853	159	3,828	24,813
1950	290	22,933	2,565	803	126	6,675	33,392
1951	205	25,984	2,360	522	125	5,995	35,191
1952	196	26,527	2,319	532	137	5,162	34,873
1953	214	31,253	2,402	518	140	5,560	40,087
1954	322	40,889	3,191	745	151	7,871	53,169
1955	386	46,163	3,317	750	217	8,571	59,404
1956	400	48,784	3,155	730	212	8,805	62,086
1957	403	59,053	3,160	665	204	10,276	73,761
1958	332	73,379	3,504	758	284	13,411	91,668
1959	408	81,516	3,400	634	430	14,284	100,672
1960	453	89,639	3,157	624	497	15,666	110,036
1961	546	119,117	4,244	790	623	21,323	146,643
1962	548	120,742	4,295	735	771	20,689	147,780
1963	554	127,156	4,271	859	753	21,137	154,730
1964	565	141,550	5,064	819	785	22,282	171,065
1965	589	148,965	4,856	852	780	23,628	179,670
1966	624	160,299	4,683	747	632	24,871	191,856
1967	443	174,025	4,929	729	704	26,652	207,482
1968	567	162,866	4,567	749	1,087	27,469	197,305
1969	606	150,235	3,969	680	1,301	28,139	184,930
1970	658	156,397	4,413	858	1,304	30,769	194,399

^a Professional subsumed in wage earner data for 1934-1939.

^b Miscellaneous includes both "in business" and "not in business" cases.

^c Data are for cases closed from 1940-1970.

Sources: U.S. D.O.J., *Report*, 1899-1939; Administrative Office of the U.S. Courts, *Tables*, 1940-1970.

Figure 1

Business and Non-Business Bankruptcy Cases, 1899 to 1970 (Log Scale)

Sources: U.S. D.O.J., *Report*; Administrative Office of the U.S. Courts, *Tables*.

Figure 2

Non-Business Bankruptcy Cases and the Debt-to-Income Ratio, 1919 to 1970

Sources: U.S. D.O.J., *Report*; Administrative Office of the U.S. Courts, *Tables*; *Historical Statistics*, Series X409 and F8.

Figure 3

Merchant Bankruptcy Cases and Merchant Business Failures, 1899 to 1970

Sources: U.S. D.O.J., *Report*; Administrative Office of the U.S. Courts, *Tables*; U.S. Bureau of the Census, *Statistical Abstract*.

Figure 4

Manufacturing Bankruptcy Cases and Manufacturing Business Failures, 1899 to 1970

Sources: U.S. D.O.J., *Report*; Administrative Office of the U.S. Courts, *Tables*; U.S. Census Bureau, *Statistical Abstract*.

Figure 5

Business Formation, Business Discontinuance, and Business Bankruptcies, 1900 to 1941

Sources: U.S. D.O.J., *Report*; Administrative Office of the U.S. Courts, *Tables*; U.S. Census Bureau, *Statistical Abstract*.

NOTES

¹ Field, “Bankruptcy”; Bernanke, “Bankruptcy” and “Non-monetary Effects.”

² On the history of legal decisions regarding state insolvency laws see Newmeyer, *Supreme Court*, pp. 79-80, 85-86; Zainaldin, *Law*, pp. 39-40; and Bailey, “Assignment” and “Discharge.”

³ *Debates and Proceedings in the Congress of the United States*, January 1799, pp. 2667-68. On the politics of the Bankruptcy Act of 1800 see Mann, *Republic of Debtors*, pp. 166-220.

⁴ Balleisen, *Navigating Failure*, pp. 101-33, gives a detailed historical account of the 1841 Act. Skeel, *Debt’s Dominion*, pp. 28-34, provides a public choice interpretation of the passage and repeal. Berglof and Rosenthal, “Political Economy,” analyzes roll call votes on the bill and its repeal.

⁵ The most detailed account of the 1867 Bankruptcy Act is Sandage, “Deadbeats,” pp. 84-266.

⁶ Hansen, “Commercial Associations,” examines the role of commercial associations in drafting and lobbying for the 1898 Bankruptcy Act.

⁷ U.S. Senate, *Memorial*; and *Congressional Record*, 55-2 (1898), p. 1905, list all petitioners for the Torrey Bill.

⁸ Nystrom, *Economics*, p. 405; U.S. D.O.J., *Causes*, p. 20.

⁹ James Beach, a late nineteenth century dry goods wholesaler claimed that, “The aggregate transactions of a single day in any one of our large houses often reach hundreds of thousands of dollars, and many of them are based upon the simple word of honor.” Beach, “Dry Goods Trade,” p. 559.

¹⁰ On business mortality in the nineteenth and early twentieth century see Hutchinson, Hutchinson and Newcomer, “Study”; Goldstein and Mayer, “Patterns”; Greer, “Business Mortality”; Phillips, “Chain Store Mortality”; and Bowen, “Turnover.” A review of several studies of business mortality is also provided in Kaplan, *Small Business*.

¹¹ U.S. Senate, *Memorial*, p. 7.

¹² On the expansion of the federal judiciary and the opposition to it see Merkel, “Origins”; Freyer, *Forums* and “Federal Courts”; and McCurdy, “American Law.”

¹³ The composition provision was seldom used. In 1930, only 695 of 60,548 cases closed were compositions. U.S. D.O.J., *Report*, 1930, p. 207.

¹⁴ Levi and Moore, “Bankruptcy,” p. 3.

¹⁵ See Billig, “What Price Bankruptcy,” pp. 413-15, for a description of the scandal that erupted in the bankruptcy courts of New York in early 1929. The reports of the government investigations are frequently referred to as the Donovan Report (Donovan, *Administration*) and the Thatcher Report (U. S. Senate, *Strengthening Procedure*).

¹⁶ Act of March 3, 1933, chap. 204, sec. 77, 47 Stat. 1474 (1933); Act of June 7, 1934, chap. 424, sec. 77B 48 Stat. 912 (1934); and Public Law No. 75-696, 52 Stat. 840 (1938). The 1938 Amendments are generally referred to as the Chandler Act.

¹⁷ Skeel, *Debt’s Dominion*, pp. 73-100.

¹⁸ *Ibid.*, pp. 131-59; Posner, “Political Economy”; and Nunez and Rosenthal, “Bankruptcy Reform.”

¹⁹ Nunez and Rosenthal, “Bankruptcy Reform.”

²⁰ Field, “Bankruptcy”; Bernanke, “Bankruptcy” and “Non-monetary Effects.”

²¹ Bernanke, *Essays*, p. 53.

²² Schiffman, “Shattered Rails.”

²³ Olney, “Avoiding Default.”

²⁴ Field, “Bankruptcy.”

²⁵ Field, “Bankruptcy,” p. 131.

²⁶ Field, “Bankruptcy,” p. 116.

²⁷ U.S. Administrative Office of the U.S. Courts, *Tables*. Previously published studies have used the occupation data for the post war period; see, for example, Apilado, Dauten and Smith, “Personal Bankruptcies.”

²⁸ For example, Balleisen, *Navigating Failure* and “Vulture Capitalism”; Hansen, “Commercial Associations”; Sauer, “Bankruptcy Law”; and Berglof and Rosenthal, “Political Economy.”

²⁹ Field, “Bankruptcy,” pp. 101-05. This error, along with Field’s failure to locate the post-1940 data, is ironic given his recent criticism of Northian institutional economic history for not being “informed by detailed knowledge of law in its particulars.” Field, “New Economic History,” p. 743.

³⁰ Dawsey and Ausubel, “Informal Bankruptcy”; White, “Why Don’t.”

³¹ Cover, *Business*, p. 13; U.S. Senate, *Strengthening Procedure*, pp. 81-82.

³² *Ibid.*, p. 81.

- ³³ Ibid., p. 82.
- ³⁴ Cover, *Business*, p. 13.
- ³⁵ Dawsey and Ausbel, “Informal Bankruptcy,” p. 8.
- ³⁶ Shepard, “Personal Failures”; Peterson and Aoki, “Bankruptcy Filings”; Scott and Smith, “Effect”; and Boyes and Faith, “Some Effects.”
- ³⁷ Sullivan, Warren, and Westbrook, *Fragile Middle Class*, p. 251.
- ³⁸ Domowitz and Eovaldi, “Impact.”
- ³⁹ Buckley and Brinig, “Bankruptcy Puzzle.”
- ⁴⁰ Fay, Hurst and White, “Household Bankruptcy Decision,” p. 710.
- ⁴¹ Gross and Souleles, “Empirical Analysis.”
- ⁴² Bhandhari and Weiss, “Increasing Bankruptcy Filing Rate”; Moss and Johnson, “Rise.”
- ⁴³ *Marquette National Bank v. First Omaha Service Corporation*, 439 U.S. 299 (1978).
- ⁴⁴ Moss and Johnson, “Rise.”
- ⁴⁵ Sullivan, Warren, and Westbrook, *Fragile*, p. 240.
- ⁴⁶ See Sturges and Cooper, “Credit Administration”; Douglas, “Wage Earner Bankruptcies”; U.S. Senate, *Strengthening Procedure*; Moss and Johnson, “Rise.”
- ⁴⁷ Cited in Moss and Johnson, “Rise.” On the expansion in consumer indebtedness as the cause of increased bankruptcy, see Sadd and Williams, *Causes*, p. 7.
- ⁴⁸ U.S. Senate, *Strengthening Procedure*, p. 13.
- ⁴⁹ Sturges and Cooper, “Credit Administration.”
- ⁵⁰ U.S. D.O.J, *Annual Report*, (1903), p. 125.
- ⁵¹ *Congressional Record* (February 23, 1910), p. 2277.
- ⁵² Robinson, “Scope,” pp. 49-56.
- ⁵³ U.S. Senate, *Strengthening Procedure*, p. 12.
- ⁵⁴ *Nation’s Business*, April 1926, p. 14, pp. 18-19; Sloan, *My Years*, p. 302.
- ⁵⁵ Olney, “Avoiding Default,” p. 326.

- ⁵⁶ Clark, *Financing the Consumer*, p. 141. See also, Olney “Avoiding Default,” p. 325.
- ⁵⁷ Clark, *Financing the Consumer*, p. 141.
- ⁵⁸ Olney, “Avoiding Default.”
- ⁵⁹ On the increased supply of credit see Olney, “Avoiding Default,” p. 319; and Persons, “Credit Expansion.”
- ⁶⁰ Olney, “Demand”; and *Buy Now*, pp. 117-130.
- ⁶¹ See Olney, *Buy Now*, pp. 126-28; and Calder, *Financing*, pp. 184-91 on the origins of finance companies.
- ⁶² Olney, “Avoiding Default,” p. 324.
- ⁶³ Lebergott, *Pursuing Happiness*, p. 137.
- ⁶⁴ Calder, *Financing*, pp. 134-36.
- ⁶⁵ White, “Banking,” p. 755.
- ⁶⁶ Sadd and Williams, *Causes*, p. 5.
- ⁶⁷ U.S. Dept. of Commerce, *Causes*, p. 26.
- ⁶⁸ U.S. Senate, *Strengthening Procedure*, p. 3.
- ⁶⁹ Hamilton, “Does Entrepreneurship Pay?” finds that non-pecuniary rewards are a substantial part of the benefits for many entrepreneurs.
- ⁷⁰ Hansen, “Peoples’ Welfare”; and Tufano, “Business Failure.”
- ⁷¹ Levi and Moore, “Bankruptcy,” pp. 4-5.
- ⁷² Hansen, “People’s Welfare.”
- ⁷³ Hansen, “Commercial Associations,” pp. 96-97; Billig, “What Price”; and Gamer “Comparing.” Similarly, companies were established in the 1920s to facilitate wage earner amortizations.
- ⁷⁴ U.S. Senate, *Strengthening Procedure*, pp. 68-92.
- ⁷⁵ Chapin, *Credit*, p. 522.
- ⁷⁶ U.S. Bureau of the Census, *Historical Statistics*, notes to series V23-26.
- ⁷⁷ Dun and Bradstreet’s business failure estimates are not comprehensive because the company was only concerned with firms that sought commercial credit, but bankruptcy tends to be dominated by the same firms that dominate Dun and Bradstreet’s records. For a description of the Dun and Bradstreet data see U.S. Dept. of Commerce, *Historical*

Statistics, print edition 1960, p. 567. It should also be noted that changes were made in the series in 1933 and 1939.

Prior to 1933 Dun and Bradstreet included real estate and financial firms in its “number of failures,” even though such firms were not part of its count of “total number of concerns in business.” After 1933, it excluded the real estate and financial firms from “number of failures” to make the two series more consistent. The change in the numerator was small. The original “number of failures” in 1933 was 20,307. The revised “number of failures” was 19,859. The number of listed concerns was 1,960,701. Consequently the failure rate was reduced from 1.03 percent to 1.01 percent.

See U.S. Bureau of the Census, *Statistical Abstract*, 1939, table No. 343.

⁷⁸ U.S. D.O.J., *Report*, for years 1933-1939.

⁷⁹ Kaplan, *Small Business*, pp. 8-59; Lane and Schary, “Understanding,” pp. 93-105.

⁸⁰ Lane and Schary, “Understanding,” p. 93. A number of studies have concluded that the age of the firm is significant determinant of the probability of discontinuance. See Caves, “Industrial Organization,” for a survey of the literature.

⁸¹ *Ibid*, p. 97.

⁸² Blau, “Time Series Analysis”; Fairlie and Meyer, “Trends.”

⁸³ The Administrative Office also reports on the use of the different chapters of the Bankruptcy Act.

Figure 1

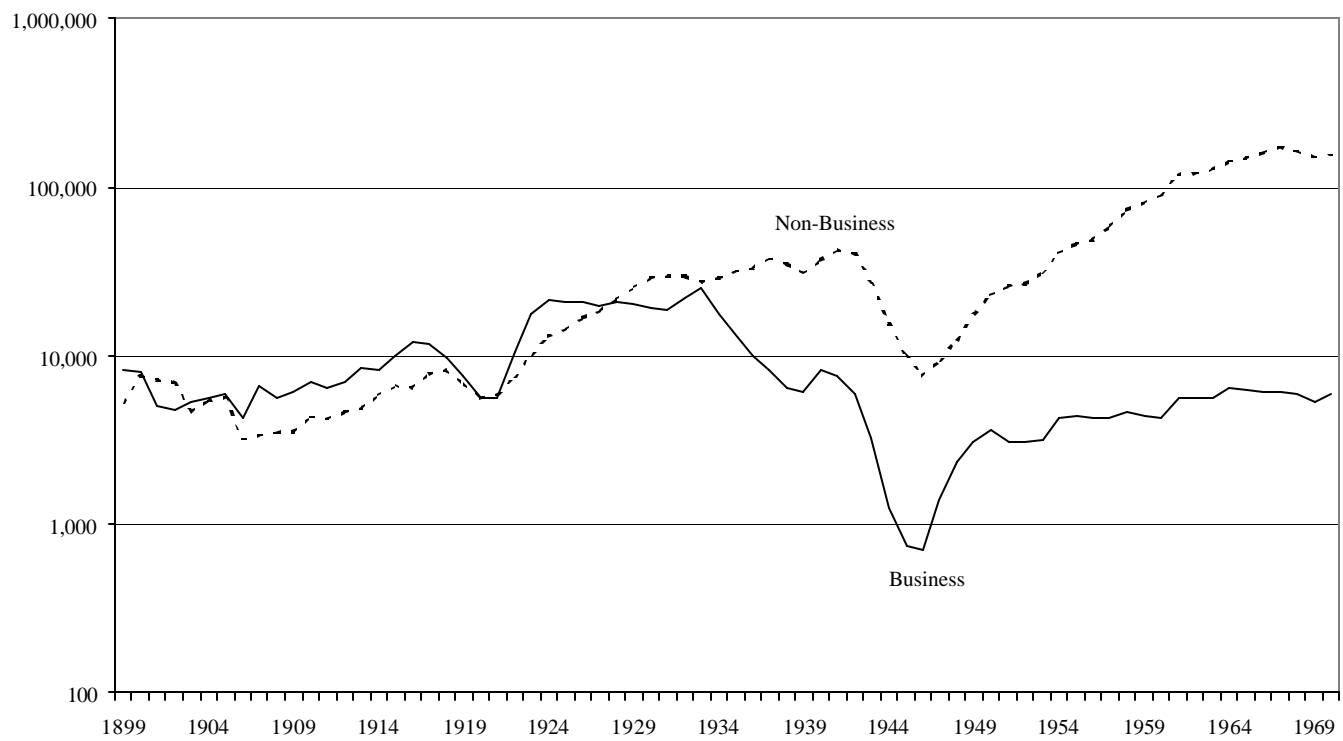


Figure 2

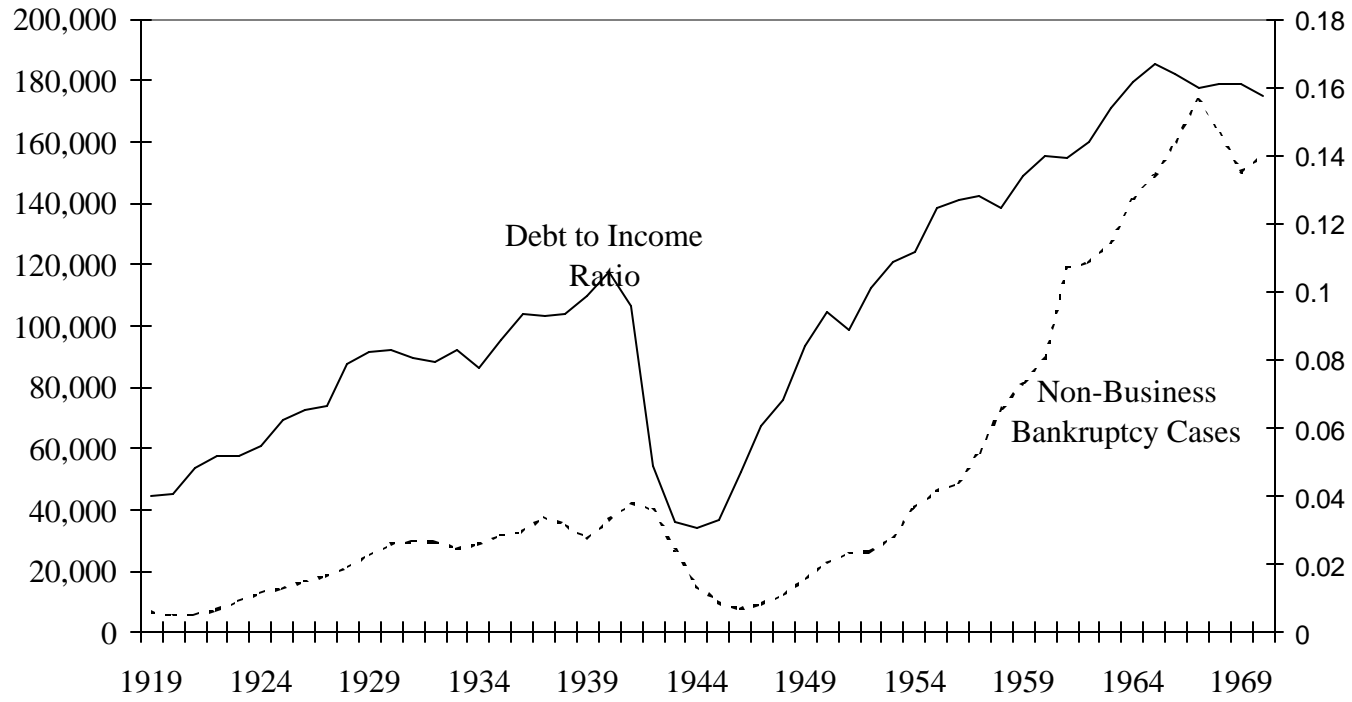


Figure 3

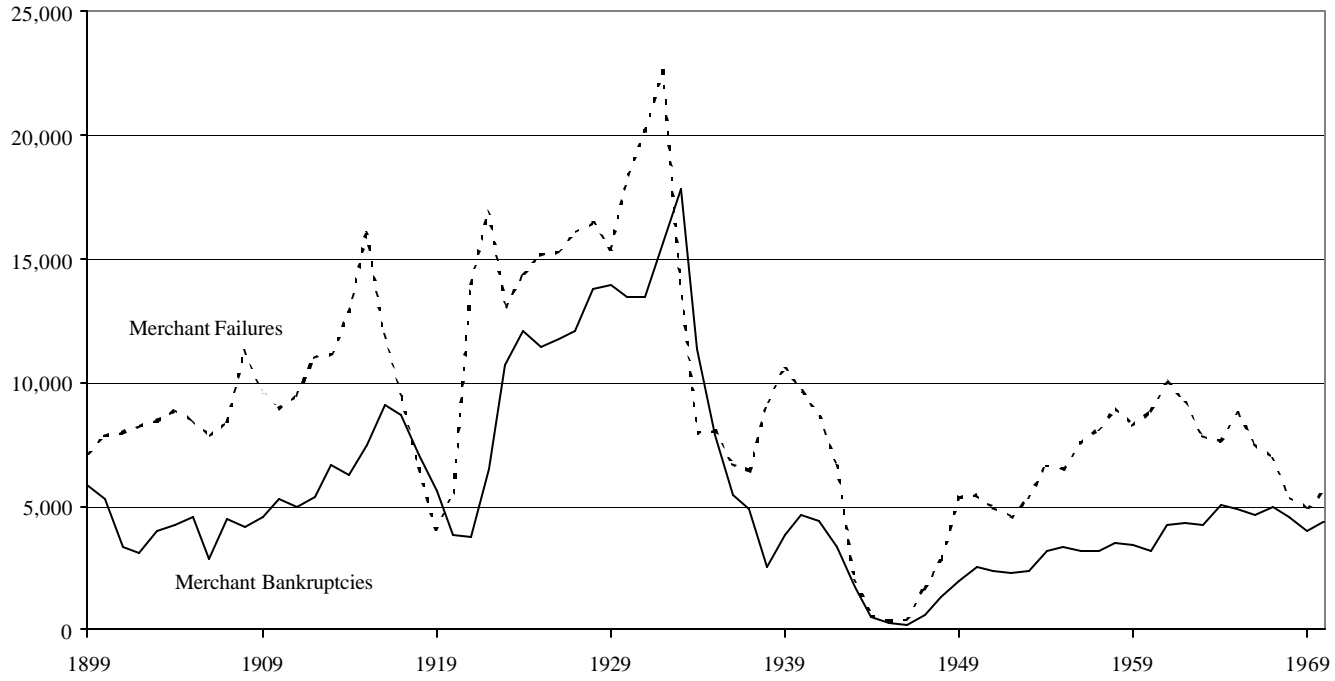


Figure 4

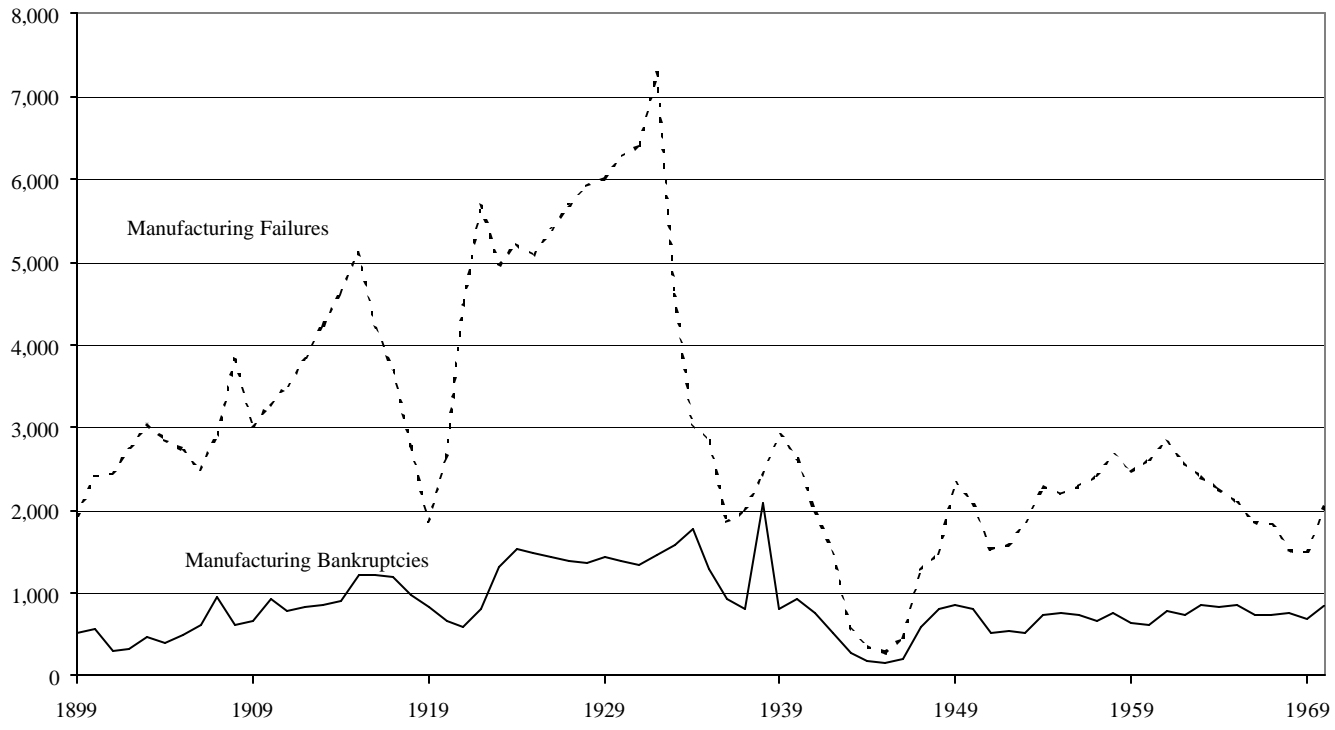


Figure 5

