Book Review

Broke: How Debt Bankrupts the Middle Class

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Author: **Katherine Porter**
Publisher: Stanford University Press (2012)
ISBN: 978-0-8047-7701-8

Broke: How Debt Bankrupts the Middle Class is a must-read book for *Journal of Financial Counseling and Planning* subscribers who teach or counsel people about credit and related topics (e.g., bankruptcy, predatory lending, and student loans). Edited by Katherine Porter, a Professor at the University of California-Irvine School of Law and an expert in consumer credit law, its 12 chapters are authored by Professor Porter and 10 others including former Harvard Law Professor and Consumer Financial Protection Bureau advisor (and now Massachusetts Senator) Elizabeth Warren. Their fields of expertise include economics, housing and land use, health policy, psychology, sociology, and consumer law.

The content portion of *Broke* is 234 pages long and organized into 5 parts and 12 chapters. This content is followed by 61 more pages containing an *Appendix* that describes the methodology of the 2007 Consumer Bankruptcy Project (CBP), which provides data reported in this book, *Acknowledgement*s, and an extensive *Notes* section that provides data sources for facts, figures, and events that are cited. The book is meticulously researched and includes data from studies and reports by the Federal Reserve Board, RAND, the U.S. Department of Education, the College Board, the U.S. Census, the Bureau of Labor Statistics, the Joint Center for Housing Studies, and dozens of respected scholars as well as data from the CBP.

Broke begins with an introductory chapter*, Driven by Debt*, written by the editor, Katherine Porter. In this chapter, Porter compares the waiting room for a bankruptcy hearing to the emergency room of a hospital: "This is the room where people wait to be diagnosed with a financial emergency- bankruptcy" (p. 1). Readers learn that about 1.5 million families experienced bankruptcy in 2010 as Americans' increased consumption in recent decades was largely financed by debt. U.S. household leverage more than doubled since the mid-1980s, reaching a debt-to-personal disposable income ratio of 133% in 2007. Home mortgages and student loans are called "high-stakes economic gambles" (p. 6). The end of Chapter 1 describes the 2007 CBP dataset that builds on the work of Sullivan, Warren, and Westbrook in 1981 and 1991 and provides a brief overview of the content of each part and chapter of the book. Readers are also told about a supplemental Web site for additional information: www.sup.org/broke.

Chapter 2, *A Vulnerable Middle Class*, is authored by Elizabeth Warren and sociologist Deborah Thorne. Readers learn that income is an unreliable indicator of class status for those in bankruptcy. While incomes at the time of filing are quite low, most bankruptcy filers have prior middle class roots. Debtors since 2001 are more likely to have gone to college and bought a home. "This suggests that two traditional strategies for building wealth - college attendance and home ownership - are increasingly divorced from financial security" (p. 26). CBP data indicate that people in bankruptcy were 60% more likely than Americans in general to have attended college but left without earning a degree. The chapter then describes in detail occupational and homeownership status of the CBP sample which has "enduring indicia of middle-class achievement"

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(p. 38). It ends, as 10 subsequent chapters also do, with an Implications/Conclusion/Discussion section (it has different titles in different chapters) that recaps key data points and what they mean for individuals and families, public policy, and society in general.

*Out of Balance? Financial Distress in U.S. Househol*ds, Chapter 3, is written by Federal Reserve Board economist Brian Bucks. It compares and contrasts 2007 CPB data about bankruptcy filers with the 2007 Survey of Consumer Finances (SCF) or, more specifically four SCF subgroups of financially distressed families. Sharp differences between the two study samples are reported as are differences in the methodology used to create each dataset. Various comparison metrics such as ownership rates and conditional medians are explained and contrasted. Readers learn, for example, that 80% of bankruptcy filers have a negative net worth, more than twice the share for the SCF subgroups, and that bankruptcy filers are "much more likely than families in each of the SCF groups to have medical debt" (p. 55). Conversely, bankruptcy filers are less likely to have education debt than three of the four SCF subgroups.

In Chapter 4, *Home Burdens: The High Costs of Homeownership*, housing policy expert Jerry Anthony discusses the housing cost burdens of U.S. families for which housing is typically their largest expense. Housing expense ratios are discussed in general and then parsed and discussed through the lens of various household demographic characteristics (e.g., income, race, age, education, and family structure). The chapter also provides a nice summary of changes in mortgage lending practices during the past three decades. Examples are the rise of second mortgages on homes at the time of purchase in the 1990s (i.e., so-called "piggyback loans") and the use adjustable-rate mortgages (ARMs) with low "teaser rates" that reset to unaffordable levels after an introductory period. Research is cited that shows how sharp upticks in monthly ARM payments propelled many families into bankruptcy.

Editor Katherine Porter wrote Chapter 5, *College Lessons: The Financial Risks of Dropping Out*. In this chapter, she notes that, similar to earlier studies, the largest group of people in bankruptcy remains (in the 2007 CPB sample) those with "some college." Conversely, college graduates and those with advanced degrees are underrepresented. In addition, people with "some college" were found to have debt-to-income ratios similar to those with high school educations. Various categories of "some college" are discussed in detail (e.g., 4-year college dropouts versus those who earn academic or occupational associate's degrees). An overriding theme of this chapter is that those who attempt college but never complete a bachelor's degree incur student loan debt without the economic benefits that many college graduates realize. People with a 4-year degree earn one third more over their lifetime than those without such a degree and "the payoff from associate's degrees is quite marginal" (p. 89). Nevertheless, Department of Education data indicate only a 57.3% completion rate for those who seek a four-year degree. Failure to graduate increases student loan default probability by about 10 percentage points.

Chapter 6 is titled *Striking Out on Their Own: The Self-Employed in Bankruptcy*. This chapter was written by Robert Lawless, a University of Illinois law professor. The chapter starts out by comparing stories about successful entrepreneurs with those who did not succeed and were left awash in debt. About 14% of bankruptcy cases involve someone who reports self-employment at the time of filing. Characteristics of self-employed bankruptcies are discussed in detail, citing figures from various academic studies and noting that many small business loans require owners to personally guarantee business debts. Not surprisingly, debtors whose business failure pushed them into bankruptcy "are in worse shape than those without self-employment and those whose self-employment was not a reason for their bankruptcy" (p. 112). Furthermore, "credit card debt and general unsecured borrowing dominate the debt burdens of most self-employed filers" (p. 114). Small business cases are treated the same as typical consumer bankruptcies.

No Forwarding Address: Losing Homes in Bankruptcy, is the title of Chapter 7, which begins with this startling statistic: more than seven million homes will be lost to foreclosure by the end of 2012. The chapter, written by law school dean Marianne Culhane, then discusses the homeownership status of the 2007 CBP sample (with median mortgage debt of $104,000), how bankruptcy filers fare in Chapter 7 and Chapter 13 cases, and where those who lose their home live afterwards. It also introduces readers to a federal law that requires public school districts to permit children who become homeless to continue to attend their former school and often provide their transportation. An overall theme of this chapter is that home loss is part of the bankruptcy process for many families who ultimately fail to save their homes.

In Chapter 8, *Women's Work, Women's Worry: Debt Management in Financially Distressed Families*, the role of gender with respect to financial hardship and bankruptcy is explored. The author, Ohio University Sociology Professor Deborah Thorne, begins the chapter by citing studies, including the CBP, that show that women are disproportionately responsible for paying household bills. Not surprisingly, as bills mount, "unmanageable debt burdens are particularly emotionally distressful for women" (p. 138). Studies linking financial distress with marital strain and divorce and to poor physical health outcomes (e.g., anxiety, insomnia, depression) are also discussed. Thorne concludes by noting that personal bankruptcy is a "gendered" experience: "not only are women disproportionately more likely to go bankrupt, they appear to be disproportionately more likely to suffer from the experience" (p. 151).

Chapter 9, *The Do-It-Yourself Mirage: Complexity in the Bankruptcy System*, was written by University of Texas law professor Angela Littwin and discusses the feasibility (or, rather, generally the futility) of individuals filing for bankruptcy themselves. After 2005 amendments to the bankruptcy code, the process of filing bankruptcy became more complex and expensive (e.g., legal fees). Interestingly, those who file without a lawyer are better educated than those who use lawyers. The chapter describes in detail attorney bankruptcy fees, the bankruptcy filing process, characteristics of pro se (without a lawyer) filers, negative outcomes for unrepresented debtors (e.g., a dismissal without a discharge), and ways to redesign the bankruptcy process to reduce complexity and increase assistance to pro se filers.

Less Forgiven: Race and Chapter 13 Bankruptcy, authored by Dov Cohen (University of Illinois psychology/law professor) and Robert Lawless, is the title of Chapter 10, which concludes that "African Americans are much more likely to file Chapter 13 bankruptcy than bankruptcy filers from other races" (p. 189). The Chapter 7 means test, differences between Chapter 7 and Chapter 13 bankruptcies, and results of empirical studies of bankruptcy filing methods are described at the beginning of the chapter. Chapter 13 bankruptcy filings involve a 3- to 5-year debt repayment plan compared to Chapter 7s where "only a few debtors have to pay their creditors anything at all" (p. 189). Some interesting statistics are that only about a third of Chapter 13 debtors make all their required payments and receive a discharge and Chapter 13 cases cost two to three times more for legal fees than Chapter 7 filings do. The authors conclude by discussing their findings about African American bankruptcy filers and possible reasons for their high percentage of Chapter 13 filings (e.g., "local legal culture" in judicial districts).

Borrowing to the Brink: Consumer Debt in America is the title of Chapter 11, authored by Kevin Leicht, a University of Iowa Sociology professor and director of the Iowa Social Science Research Center. The theme of this chapter is the connection between U.S. wage stagnation and increased consumer debt burdens, particularly during the past three decades. Leicht argues that "the middle class has been loaned money as a substitute for being paid an appropriate, productivity-enhanced wage" (p. 196) and defends his thesis with data about declines in real income for the middle class and increases in the cost of four mainstays of middle-class life: single-family homes, health-care expenses, child care, and higher education. He also describes the increased use of credit and results of a simulation he conducted of the (much lower) debt of the 2007 CBP bankruptcy filers if 1970s credit underwriting standards had been in effect. While interesting, there is a glaring omission. How would the U.S. economy have fared in this simulation since it is so dependent upon consumer spending? Debt levels of various demographic groups are also discussed as well as components of the American Dream that so many families aspire.

Broke concludes with Chapter 12, *The Middle Class at Risk,* written by Yale political science professor Jacob Hacker. A major theme is the shift of economic risk onto middle-class families in several key areas: "their jobs, their retirement pensions, their homes and savings, their health care, their strategies for balancing work and family" (p. 218) which Hacker terms the "Great Risk Shift." America's fraying safety net is discussed in detail with data about employee health insurance coverage (or lack thereof), defined-contribution retirement savings plans, income instability, household indebtedness, and the impacts of technology and globalization. The chapter concludes with proposals for an improved safety net to help families deal with income interruptions and financial shocks that deplete household wealth.

As noted at the outset of this review, I recommend reading this book. What I particularly like about *Broke* is its "real world" treatment of consumer credit and debt topics, particularly bankruptcy. Instead of focusing on how the filing process is *supposed to* happen, *Broke* describes what *really* happens, warts and all. For example, inconsistencies in the application of federal laws within local judicial districts and the fact that so many bankruptcy filings ultimately fail to result in a discharge. The book is also current and makes numerous references to lingering effects of the 2008 financial crisis and, as noted earlier, is extensively well researched with 48 pages of endnotes citing the sources of facts and figures. It also contains dozens of helpful tables and figures that present statistical data in an understandable format.

It probably was not possible due to publication deadlines for *Broke*, but it would have been nice if 2010 Survey of Consumer Finances (SCF) data (released in June 2012) had been cited instead of 2007 figures. The finances of American families deteriorated significantly between 2007 and 2010 as Federal Reserve papers comparing SCF data from these two time periods have documented. Other minor comments include a noticeable amount of repetition within some papers, and no cross-referencing between, or summation of, the content of the individual chapters. *Broke* read more like a collection of papers in the proceedings of a conference than as a book. Since chapter authors presumably worked independently and would not have had access to each other's work, the editor could have melded their work together in a summary chapter.

The above quibbles notwithstanding, *Broke* is a tremendous resource for financial educators and counselors. All or part of the book could serve as a textbook or supplemental reading for college personal finance or financial counseling courses. For community financial educators and financial counselors, *Broke* provides valuable insights into the causes and effects of the financial distress experienced by many American families. Reading this book can help practitioners relate better to the publics that they serve. Public policymakers also will find valuable suggestions at the conclusion of every chapter to reduce the financial distress of millions of Americans who are…broke.