Late-Life Bankruptcies

A Growing Safety Net

By James Frego and Glen Turpening

At a Glance

The concept of a late-life bankruptcy is one that attorneys working with older clients need to become familiar with as a way of helping these at-risk individuals. Bankruptcy is becoming a bigger part of the social safety net for senior citizens where the old system of a secure, lifelong income is being replaced by permanent debt relief.

***NOTE**: This article was originally written in January 2020, before the recent economic downturn. It has been updated to reflect some known changes in the law and national events, but the situation has been constantly changing. The authors attempted to include the most recent developments possible, but much of how the COVID-19 pandemic will affect the economy long term is unknown at this time. However, it is extremely likely that in the months to come bankruptcy as a financial safety net will become more necessary for individual Americans, but more complex and challenging for bankruptcy practitioners at the same time.*

What will your golden years look like financially? Do you envision travel, leisure, and long walks on a sunny beach? You likely have been planning for your retirement or near-retirement years for quite some time, using tools like financial advisors, estate planners, and various investments or retirement account holdings. Attorneys, doctors, and other professionals are often the exception to the norm. Many others are unable to avail themselves of these resources, and their golden years are anything but idyllic. For them, financial issues are lifelong struggles stemming from both an income problem and an expense problem.

Further, the recent COVID-19 pandemic and economic downturn have caused people already in retirement or near retirement age to lose sizable portions of any retirement investments in stocks or mutual funds, with little chance of making up the losses other than hoping the stock market bounces back to previous levels. Many are already retired or near retirement age, and have no "work years" left to replenish the lost funds that were expected to provide income during these later years of life.

For many retirees, there simply is not much money remaining after paying their bills. Most did not expect that, as they got older, their retirement years would so closely mirror their working years—only with considerably tighter margins. For these individuals, a late-life bankruptcy might be a perfect (and permanent) solution to their financial problems.

The income problem

Phased-in changes in the old retirement safety nets of pensions and Social Security affect a larger portion of the elderly population each year. Over the past three decades, the secure retirement that the baby boomer generation anticipated has gradually eroded. The number of retirees with defined benefit pensions has fallen precipitously, and the full retirement age for Social Security eligibility is now between 66 and 67 years old, leaving large numbers of seniors in a retirement fiscal deficit—especially if they begin drawing benefits at 62, the earliest eligibility age.[1]

For decades, Americans have been told to save for retirement, but the results have been middling. The average baby boomer currently in or approaching retirement age has $25,000 or less in savings,[2] with 29 percent of households headed by someone age 55 and older having no pension plan or retirement savings.[3]

There are options. Reverse mortgages allow homeowners to borrow against the equity in their homes in exchange for a lump sum of money that is usually paid back only when the homeowner passes away, and if not paid, the house reverts to bank ownership. Several government programs target seniors for help with everything from food and medical care to appliance repair and tax preparation. And societal changes have created an environment where more and more seniors want to work, even part-time, to stay mentally fresh and vigorous.

But each of these options has its problems. With most reverse mortgages, the family home can no longer be passed on to children and grandchildren because the lender takes ownership upon the borrower's death since often there is no equity remaining.[4] And while government assistance programs exist, they can be plagued with bureaucratic red tape, meaning many seniors will not seek help from the government, regardless of how critical their need might become. Finally, while jobs for seniors exist, issues like age-related deterioration of skills or health problems often limit the options to low-paying, entry-level positions.

The expense problem

Around the turn of this century, technological and societal changes led to a spike in household expenses that were unheard of in decades past. Cellular phones, home computers, and internet bills are all relatively new expenses now considered mainstays in the home.

Technologically challenged older Americans often find themselves victims of identity theft and phishing scams, alerting them to nonexistent "urgent issues" with their credit cards, vehicle warranties, tax filings, home loans, or Social Security benefits. These false warnings are particularly frightening to those past retirement age.

Increased healthcare costs also come with older age. While seniors are eligible for Medicare, it does not cover everything and can leave significant gaps. Dental, basic vision, over-the-counter medicines, and long-term care are just a few necessities not covered by Medicare.[5] Further, according to the Georgetown University's Health Policy Institute, Americans over 65 must pay out-of-pocket for more than half of their prescription drug expenditures.[6]

Whether because of an increase in everyday living expenses, healthcare costs, or an unexpectedly larger household as children and grandchildren move back home, many seniors have been forced to rely on credit cards to bridge monthly budget gaps. Also, at some point in the last 25–30 years, consumers were no longer encouraged to use credit cards as an emergency financial resource; instead, credit cards became a way of financing lifestyles beyond consumers' means for years and years as they worked.[7] When these seniors sought to retire, their lower incomes made it difficult to keep up with monies owed, leading to growing credit card balances.

What their daily lives look like

Pressured by lower incomes and unexpectedly greater expenses, many seniors struggle to make ends meet. As a result, fending off bill collectors may become routine for them.

At first blush, attorneys with a base familiarity of elder law issues might casually say, "Mr. and Mrs. Client, you are essentially judgment proof because Social Security benefits cannot be garnished. So just don't pay these people."[8] However, the problems go much deeper than Social Security benefits. In most instances, telling clients they shouldn't pay or that they are uncollectable is not sound advice.

Many pension payments are *not* judgment proof, and even then, funds can often be seized once they are placed into a bank account—an action where the garnishing creditor can receive the entirety of funds in an account. In this way, even exempt funds like pension payments can lose their protected status.[9] Savvy creditors can also seize state income-tax refunds and personal property from retirees through court-ordered assignments. It is no longer unusual to see a personal vehicle confiscated and sent to auction to pay for a judgment on an unsecured, non-purchase money security interest debt.

When seniors cannot make timely payments, other collection activity increases. They may receive 10 or more collection robocalls a day from each creditor. Bill collectors harass, shame, and threaten individuals until they find some way to make the harassment stop. More than 60 percent of older bankruptcy filers responding to a Consumer Bankruptcy Project survey reported spending in excess of two years trying to fend off creditors before finally deciding to file a bankruptcy case.[10]

Collection efforts can continue well beyond the few years mentioned above. Michigan law gives creditors six years to file a collection complaint for a breach of contract (like credit card debt) and, post-judgment, creditors have 10 years to collect—plus the possibility of an *additional* 10 years if allowed by the court.[11] This means that a 60-year-old who defaults on a credit card obligation could remain liable on that debt until he or she turns 86!

Many older Americans take out home-equity loans or pull from personal retirement accounts in an attempt to stay ahead of bill collectors. But if those funds do not provide a permanent solution, collection efforts will start again a few months down the line, and these unfortunate individuals then have fewer financial resources to support them throughout retirement.

Seniors are also carrying more debt than ever, increasing the likelihood of falling behind. *Forbes* recently noted, "According to the Federal Reserve's Survey of Consumer Finances, 60% of senior households had debt in 2016 and 29% of senior households owed money on mortgages or other housing debt. These rates represent a roughly 50% increase in the share of senior households holding debt over the last 25 years."[12] In 2015, the National Council on Aging noted the increase, indicating that the median amount of debt owed in older households more than doubled from $18,385 in 2001 to $40,900 in 2013.[13] In fact, the Consumer Bankruptcy Project reports that in bankruptcy cases from 2013 to 2016 where one member of the household was 65 or older, the average amount of unsecured debt was almost $44,000. This is primarily comprised of credit cards, loan deficiencies, and medical bills.[14]

With this increased debt comes a rising tide of older Americans filing bankruptcy cases, as shown in the table below.

Percent of U.S. Bankruptcy Filers by Age[15]

Age Group	1991	2001	2007 (Percent)	2013–2016	Relative percentage change: 1991–2016
18–24	8.7	5.3	4.2	2.1	–75.8%
25–34	36.7	26.1	21.9	15.5	–57.7%
35–44	30.6	33.7	28.1	20.4	–33.4%
45–54	15.8	23.2	23.6	28.3	+79.3%
55–64	6.1	7.2	14.7	21.5	+252.1%
65–74	1.8	3.0	5.3	8.9	+392.6%
65+	2.1	4.5	7.6	12.2	+478.9%
75+	0.3	1.5	2.3	3.3	+996.9%

Note: The percentages are based on total number of filers, not number of petitions. Thus, a joint bankruptcy petition from a married couple results in two filers.

Considering the above, attorneys working with older clients must become familiar with the concept of late-life bankruptcy as a way of helping these at-risk individuals. As the old system of a secure, lifelong income is replaced by permanent debt relief, bankruptcy is becoming a bigger part of the social safety net for senior citizens.

A general primer on consumer bankruptcy

Generally, there are two primary types of personal consumer bankruptcies: Chapter 7 and Chapter 13 (these refer to actual chapters of the U.S. Bankruptcy Code).

Chapter 7 bankruptcy

Chapter 7 is generally designed to wipe out most unsecured debts in a short period.[16] It is the most common form of bankruptcy and usually completed approximately four months from the date of case filing. It does not provide much help for issues with secured creditors or claims like student loans or income taxes that may be owed, but it is especially effective at helping relieve the burden of credit cards, loan deficiencies, and medical debt. The Bankruptcy Code limits the value of assets that can be protected in bankruptcy, meaning once a debtor's assets are beyond those limits, they are subject to liquidation by the Chapter 7 trustee for distribution to creditors.[17]

Chapter 13 bankruptcy

Chapter 13 allows an individual to repay some or all debts through a structured payment plan.[18] Instead of paying creditors directly, the debtor pays a certain amount every month to a Chapter 13 trustee who then distributes the money in accordance with the plan approved by the bankruptcy court. For clients with more assets to protect than allowed by law, Chapter 13 bankruptcy can impose structured payments that are made over 3–5 years *without risk to these assets*. Many older clients prefer a Chapter 13 bankruptcy because they are risk adverse, seek the tangible outcome of a payment plan, and, in some instances, simply feel good about paying back some of their creditors (even at pennies on the dollar).

The Coronavirus Aid, Relief, and Economic Security (CARES) Act, passed in March 2020, seems to have allowed an extension of certain existing Chapter 13 plans up to seven years total from the date of plan confirmation. However, little guidance has been given thus far regarding how to interpret these provisions and the factors that might trigger their allowance by the bankruptcy court. At the time this article went to press, the individual Chapter 13 trustees had been left to create guidelines as to the circumstances in which each would object to or allow such changes, and the mechanism for them. In the months to come, the full effect of these changes will be determined by rulings of the respective bankruptcy court judges themselves.

While both types of bankruptcy will usually yield a "discharge of debts" at their successful conclusion (meaning any remaining amounts owed to the pre-bankruptcy creditors have been eliminated), both also have benefits and dangers. To properly advise any client regarding bankruptcy, attorneys should be aware of several nuanced issues.

The benefits for clients are many

Peace of mind

Upon filing, either type of bankruptcy immediately imposes an automatic stay of proceedings.[19] This incredibly powerful tool stops harassing bill-collector calls, collection lawsuits, garnishments, repossessions, and foreclosure sales.

Eliminating overhead

The ability to wipe the slate clean of debt that has been accumulating for years can appeal to older individuals who seek a fresh start as they adjust to the lower income that retirement often brings.

Asset retention

The automatic stay allows a quiet and orderly process to unfold where clients, creditors, assigned bankruptcy trustees, and the bankruptcy court determine which assets the client will retain and which may be let go as part of the case. Generally, most bankruptcy clients keep and retain all personal assets (clothing, furniture, jewelry, etc.), including secured items for which they are current on payments, like houses and vehicles.[20] Except in rare circumstances, most ERISA-qualified retirement accounts are retained as well: clients do not have to fear losing their pension benefits, IRAs, or 401(k)s.[21] The ability to retain assets also allows seniors to eventually pass these items on to their children at death.

The ability to wipe the slate clean of debt that has been accumulating for years can appeal to older individuals who seek a fresh start as they adjust to the lower income that retirement often brings.

The dangers for practitioners are also many

Unless you have previous experience in consumer bankruptcy, be extremely wary of bankruptcy cases. Traps and pitfalls abound, and for the uninitiated they can deliver far more headaches than they are worth.

Every case is assigned to an experienced bankruptcy trustee who has one of two goals:

- Finding unprotected or improperly protected assets of your clients that can be seized and liquidated, with the proceeds split between creditors and the trustee's own commission (Chapter 7)[22] *or*
- Raising your clients' 3–5 years of bankruptcy payments as high as reasonably possible for the benefit of the creditors (Chapter 13).[23]

In even the most basic cases, expect to deal with 2–4 experienced opponents looking to get more money out of your client.

Additionally, consumer bankruptcy can include a litany of problem issues such as pre-filing asset transfers, genuinely "unknown" client assets, potential tort claims, hidden income, incorrect asset valuation, and pre-filing payments on old debts owed to insiders. Especially important when doing bankruptcy work for older individuals is the concern about new, additional assets that an individual may become entitled to in the six months *after* a bankruptcy petition has been filed, and these new assets being exposed to creditors for liquidation (for instance, cases where your client becomes eligible to receive an inheritance or life-insurance proceeds).

Finally, government response to the recent financial crisis has led to a flurry of temporary or permanent bankruptcy and collection law changes, such as those found in the CARES Act referenced above. In the months to come, the courts will determine what each of these changes mean to practitioners, and this will challenge even the most experienced bankruptcy lawyers to learn and adapt at a rate most have not seen since law school or at least since the passage of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

Consumer bankruptcy practice can be among the most grieved areas of the law and subject to a relatively high incidence of malpractice claims. Historical data from some in the insurance industry puts bankruptcy and collections work behind only plaintiff personal injury and real estate for the number of malpractice claims made.[24]

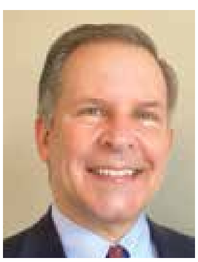
Unless you have previous consumer bankruptcy knowledge, look for an experienced bankruptcy mentor to help walk you through several cases and issues as they arise or find an experienced practitioner to whom you can refer these cases.

Conclusion

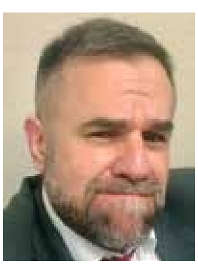
Over the past 70 years, the baby boomer generation has slowly worked its way across the American cultural landscape, and it will continue to affect our society for decades to come. It will be another 10 years before the youngest boomers reach the age of 65, meaning that issues facing older Americans are only going to become more acute, and they will need to be identified and addressed.

For many older Americans, long-term financial security is already established through a combination of Social Security benefits, pensions, part-time employment, IRAs, 401(k)s, and other savings and investments. But for a small (yet statistically significant) number, that isn't the case; for them, even small bumps in the road can be financially devastating. A $10,000 unsecured medical or credit card debt may seem manageable to someone with a full-time job, but to someone on a fixed monthly income of $2,000 or less, it can be overwhelming.

Whether an estate-planning tool or a way of helping people navigate financial problems in their golden years, late-life bankruptcy is a business decision for clients that lawyers must know about and many seniors may need to consider. The key is identifying those in need and offering assurance that they are not alone, and that the social safety net can provide much-needed help. ■



James Frego is the founder and managing member of Frego & Associates—The Bankruptcy Law Office, which is Michigan's largest consumer bankruptcy law firm. He is a certified specialist in consumer bankruptcy law.



Glen Turpening is a partner with Frego & Associates and has been practicing consumer bankruptcy for almost 20 years. The firm has offices in Dearborn Heights, Flint, Warren, Saginaw, and Ann Arbor.

ENDNOTES

1. See generally *Benefits Planner: Retirement*, Social Security Administration <https://www.ssa.gov/planners/retire/retirechart.html> [https://perma.cc/XBN6-UFRS]. All websites cited in this article were accessed April 3, 2020.
2. Reed, *What is the Average Retirement Savings?*, The Street.com <https://www.thestreet.com/retirement/average-retirement-savings-14881067> [https://perma.cc/4FLV-ZFNM].
3. Mack, *Living on $738 a month: As Boomers hit retirement, Social Security more important than ever*, MLIVE.com (January 22, 2020), available at <https://www.mlive.com/news/2020/01/living-on-738-a-month-as-boomers-hit-retirement-social-security-more-important-than-ever.html> [https://perma.cc/K86G-T25Q].
4. Sheedy, *What Heirs Need to Know About Reverse Mortgages*, Kiplinger (March 2014) <https://www.kiplinger.com/article/retirement/T021-C000-S004-what-heirs-need-to-know-about-reverse-mortgages.html> [https://perma.cc/RAM9-BYN3].
5. *What's not covered by Part A & Part B?*, Medicare.gov <https://www.medicare.gov/what-medicare-covers/whats-not-covered-by-part-a-part-b> [https://perma.cc/F5ZA-L6HW].
6. *Prescription Drugs*, Health Policy Institute, McCourt School of Public Policy, Georgetown University <https://hpi.georgetown.edu/rxdrugs/> [https://perma.cc/M7DU-DES4].
7. Wamala, *How America's Overspending Habit Affects Credit Card Debt*, Value Penguin (January 24, 2019) <https://www.valuepenguin.com/how-americas-overspending-habit-affects-credit-card-debt> [https://perma.cc/687H-GWJT].
8. 42 USC 407. In *Philpott v Essex Co Welfare Bd*, 409 US 413, 416–417; 93 S Ct 590; 34 L Ed 2d 608 (1973), the Supreme Court held that Social Security funds deposited in a savings and loan association retain their exempt status. The Court based its ruling on the fact that, when deposited in a savings and loan association, the funds retain the "quality of monies."
9. In *Whitwood, Inc v South Blvd Prop Mgmt Co*, 265 Mich App 651, 654–655; 701 NW2d 747 (2005), the Court discussed the garnishment of deposited teacher pension benefits under MCL 38.1683 compared to deposited Social Security benefits under 42 USC 407(a). The *Whitwood* Court held that, in contrast to the Social Security funds, the teacher pension funds lost their protection following deposit because MCL 38.1683 did not include the protective language contained in 42 USC 407(a) exempting "moneys paid."
10. Thorne et al, *Graying of U.S. Bankruptcy: Fallout from Life in a Risk Society*, Ind U Maurer School of Law Studies Research Paper No. 406 (August 5, 2018), p 14, available at <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3226574> [https://perma.cc/J3FY-ECWM].
11. MCL 600.5807 (9) and MCL 600.5809(3). Civil judgments in Michigan expire 10 years after entry but can be renewed for another 10-year term only by motion, which must be filed and have an order entered before its expiration date.
12. Ghilarducci, *Elderly Bankruptcy is on the Rise—Here's Why*, Forbes (August 15, 2019), available at <https://www.forbes.com/sites/teresaghilarducci/2019/08/15/elderly-bankruptcy-why/#7ff14aed4f51> [https://perma.cc/N7FT-28JS].
13. *Graying of U.S. Bankruptcy*, p 5.
14. *Id.* at 12.
15. *Id.* at 15.
16. 11 USC 524, 11 USC 727(b), FRBP 2003, and FRBP 4004(a).
17. 11 USC 522 and 11 USC 704.
18. 11 USC 1322 and 11 USC 1325.
19. 11 USC 362.
20. See generally 11 USC 522 (b) and (d).
21. 11 USC 522(d)(10)(E) and (d)(12).
22. 11 USC 704.
23. See generally 11 USC 1302, 11 USC 1325, and 11 USC 1326.
24. Metz & Reiher, *Malpractice Considerations in Bankruptcy* (December 8, 2015) <https://www.wieb.uscourts.gov/sites/default/files/chambers/svk/LouJones/12-08-2015.pdf> [https://perma.cc/XC3J-9BEY].