The Determinants of Bankruptcy for US Households: Evidence from the 2010, 2013, and 2016 Survey of Consumer Finances

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Objective

When affected with financial hardships, some people decide to declare bankruptcy to establish a payment plan, eliminate debts and obtain legal protection from the courts. However, bankruptcy can remain on peoples' credit reports for 7 to 10 years, depending on the type of bankruptcy they choose to file for. Depending on state laws, a bankruptcy trustee can be forced to liquidate certain assets, which could delay or disrupt the financial goals of the persons filing for bankruptcy and negatively affect their future financial well-being. Based on the data provided by United States Courts, it demonstrates the bankruptcy filings that involve mainly consumer debt. Because of the economic downturn, bankruptcy filings peaked in 2010: More than 1.5 million bankruptcy cases were filed in federal courts for that year. Even though the number of total filings has declined since 2010 and remained relatively steady between 2015 and 2018, the factors leading to personal bankruptcy still remain unclear. The purpose of this study is to investigate the determinants of consumer bankruptcy decisions.

Significance

Previous studies have investigated factors influencing household decisions to file for bankruptcy. Miller (2012) compared characteristics between bankrupt and non-bankrupt households. He discovered that bankrupt households earned lower incomes and had lower levels of home equity than non-bankrupt households. Their findings implied that income and total household net worth were significantly related to filing tendency. Prior literature has indicated that after controlling for demographic characteristics, large medical and credit card debt significantly increased the likelihood of filing for bankruptcy. Furthermore, homeownership discourages the tendency of filing for bankruptcy (Domowitz & Sartain, 1999; Zhu, 2011).

Method

In this study, the 2010, 2013, and 2016 Survey of Consumer Finances (SCF) reports were used to examine the factors associated with bankruptcy filing. The total sample size for the 2010, 2013, and 2016 SCF reports were 6,482, 6,015, and 6,248, respectively. The dependent variable was a binary bankruptcy filing variable based on the survey question "Have you (or your {husband/wife/partner}) ever filed for bankruptcy? (yes=1 / no=0)." Independent variables included respondents' demographic characteristics, socioeconomic characteristics, and expectation variables. Binary logistic analysis was used in this study.

Results

Nearly 530,000 families file bankruptcy each year because of unpayable medical expenses. Poor health conditions were found to be significantly associated with respondents who filled bankruptcy, compared to those in excellent health. Hispanic respondents were less likely to file bankruptcy than White respondents. No previous studies have discovered similar results; however, studies have shown that Hispanics were more conservative and had lower risk tolerance levels than Whites (Craig & Richeson, 2018). They are less likely to make risky financial decisions. High living expenses made respondents who had children more likely to file bankruptcy.

Conclusions/Relevance

Seeking financial counseling for bankruptcy can be a challenging decision for many people. Financial professionals should help clients understand how bankruptcy works and any long-term future effects. Financial professionals also need to focus on educating clients who have a habit of overspending. When designing financial education programs, clients who are older and single and those who have

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children, lower household income, and poor health condition should be listed as priority target groups for financial professionals.

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