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Personal Bankruptcies High in Fed's Eighth District

ST. LOUIS — The seven states of the Federal Reserve's Eighth District--Arkansas, Illinois, Indiana, Kentucky, Mississippi, Missouri and Tennessee--have some of the highest personal bankruptcy rates in the nation. Those rates can be attributed to factors such as divorce, medical bills and gambling.

Michelle C. Neely, an economist with the Federal Reserve Bank of St. Louis, looked at personal bankruptcies in the region for the October issue of ***The Regional Economist***, the St. Louis Fed's quarterly magazine of business and economic issues.

Neely's research showed that Tennessee, at 9.6 bankruptcies per thousand residents in 1997, led both the District and the nation. At the same time, Arkansas and Mississippi had higher-than-average rates: 6.0 per thousand and 6.9 per thousand, respectively. Missouri was the only District state with a bankruptcy rate below the 1997 national average of five per 1,000 residents.

Neely cited high debt-to-income ratios as one of the primary economic culprits affecting nationwide bankruptcy rates. "Since 1980, lenders have reached out to borrowers who may not have met previous income and creditworthiness standards," she said. "Polls show that Americans filing for personal bankruptcy routinely list credit card bills as the pivotal factor in their decision."

Based on the numbers, Neely said, divorce may also play a large role in disrupting the finances of residents in the Eighth District. For example, she observed that all District states in 1996, except Illinois, had divorce rates higher than the national average of 4.3 per thousand. Tennessee, with a rate of 6.5 per thousand, was ranked second in the nation, behind Nevada. Arkansas and Mississippi trailed Tennessee only slightly.

Neely also cited major medical expenses as a factor, particularly for the uninsured. In Arkansas and Mississippi, for example, the proportions of residents without health insurance in 1996 (21.7 percent and 18.5 percent, respectively) are significantly higher than the national average of 15.6 percent. Illinois and Indiana, on the other hand, have uninsured rates well below the national average. "These lower rates," said Neely, "are partially due to the larger number of unionized manufacturing jobs -- jobs that tend to have medical insurance — in the two states."

With the proliferation of casinos in several District states, however, compulsive gambling is increasingly being blamed for the rising tide of bankruptcies. Said Neely, "Four of the District's seven states are home to riverboat casinos, and Tunica County, Mississippi, just south of Memphis, is the third-largest gambling mecca in the country, trailing only Las Vegas and Atlantic City.

She noted, however, that while gambling may be exacerbating the region's bankruptcy problem, it is by no means the sole cause.

Neely said that bankruptcy rates tend to vary geographically because of the differences in state laws as well as local bankruptcy courts. For example, rates tend to be higher in states in which creditors are permitted to garnish wages and assets, and garnishment is permitted in all seven District states. "Western Tennessee's historically high bankruptcy rate can partially be explained by the large number of Chapter 13, or ‘wage earner' petitions there," she said. "This option is very appealing, as well as heavily promoted, in the Memphis Yellow Pages to consumer who have jobs but can't pay their bills."

To help remedy the situation, Neely described several changes to reduce the chance of bankruptcy:

- an increase by debtors in personal savings to cover financial emergencies;
- strengthening of underwriting criteria by lenders; and
- reform of the bankruptcy code to help reduce the proportion of Chapter 7 liquidations and ensure that more filers repay a portion of their debt under a Chapter 13 reorganization plan.

"This may discourage any abuse in the current system,"said Neely.

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