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Washington, DC 20548

September 30, 2010

Congressional Committees

Subject: *Military Personnel: Observations on the Use and Effects of the National Guard and Reservists Debt Relief Act of 2008*

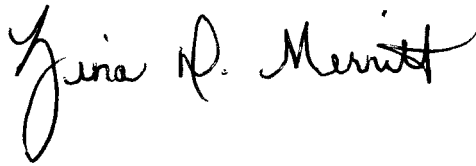
In section 3 of the National Guard and Reservists Debt Relief Act of 2008 (Pub. L. No 110-438 (2008)), Congress mandated that we provide information on the use and the effects of the provisions of law amended (and as amended) by the act. Specifically, the act amended the existing bankruptcy code to exempt qualifying members of the National Guard and Reserve Components from the means test process when they file a petition for Chapter 7 bankruptcy relief. We are fulfilling the act's requirement by transmitting the enclosed briefing slides to the President Pro Tempore of the Senate and the Speaker of the House of Representatives.

We provided a draft of the enclosed slides to the Administrative Office of the U.S. Courts, the Executive Office for U.S. Trustees, and the Department of Defense for review and comment. They provided us with technical comments, which we have incorporated as appropriate.

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We are sending copies of this report to the appropriate congressional committees, the Director of the Administrative Office of the U.S. Courts, the Assistant Attorney General for Administration at the Department of Justice, and the Secretary of Defense. The report is also available at no charge on the GAO Web site at <http://www.gao.gov>.

Should you or your staff have any questions concerning this report, please contact me at (202) 512-5257 or merrittz@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this report include Elizabeth McNally, Assistant Director; Jason Bromberg, Assistant Director; Jeremy Cluchey; Julie A. Corwin; Cynthia Grant; Stuart M. Kaufman; Shvetal Khanna; Joanne Landesman; Gregory A. Marchand; Jungjin Park; Terry Richardson; Michael Shaughnessy; Michael Silver; and Amie M. Steele.

A handwritten signature in black ink that reads "Zina D. Merritt". The signature is written in a cursive style with a large, looped initial "Z".

Zina D. Merritt
Acting Director
Defense Capabilities and Management

Enclosure

List of Committees

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Enclosure: Briefing Slides



MILITARY PERSONNEL: Observations on the Use and Effects of the National Guard and Reservists Debt Relief Act of 2008

September 30, 2010

GAO-10-1014R Debt Relief Act



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Introduction to the National Guard and Reservists Debt Relief Act of 2008

- The National Guard and Reservists Debt Relief Act of 2008 (Debt Relief Act)¹:
 - applies to members of the National Guard and Reserve Components who, after September 11, 2001, are ordered to active duty or to perform a homeland defense activity for at least 90 days² and
 - temporarily exempts these members of the National Guard and Reserve Components from certain proof requirements of the Chapter 7 bankruptcy process (specifically, undergoing an income/expense calculation, which is known as the means test).
- The Debt Relief Act also requires GAO to provide a study on the use and the effects of the act by December 2010. (See app. I for information on the reporting requirements.)

¹Pub. L. No. 110-438 (2008). The act went into effect on December 19, 2008, and will expire on December 19, 2011.

²The act defines active duty by reference to 10 U.S.C. § 101(d)(1) and homeland defense activity by reference to 32 U.S.C. § 901(1). Section 901(1) defines "homeland defense activity" as an activity undertaken for the military protection of the territory, domestic population of the United States, or infrastructure or other assets of the United States determined by the Secretary of Defense as being critical to national security from a threat or aggression against the United States. This statute applies to members of the National Guard.



Background: Types of Bankruptcy and the Bankruptcy Process

- Bankruptcy is a federal court procedure that can help provide relief for both individuals and businesses from debts that they cannot fully repay and help creditors receive some payment.³ An individual or an individual and spouse jointly may file a petition for bankruptcy relief. Individuals usually file a petition under Chapter 7 or 13 of the Bankruptcy Code.
 - Under Chapter 7, bankruptcy debtors may be eligible for discharge of most unsecured debts.⁴
 - Under Chapter 13, bankruptcy debtors submit a proposed repayment plan for the court's approval in which they agree to pay all or a portion of their unsecured debts over time.

³Generally, statutes pertaining to bankruptcy are found in Title 11 of the U.S. Code.

⁴Although a discharge protects the debtor from personal liability for secured debt, if the Chapter 7 debtor is delinquent the creditor may still foreclose on or repossess the property securing the debt. In a Chapter 7 case, any eligible nonexempt assets are gathered, reduced to cash, and distributed to creditors in accordance with distribution priorities and procedures found in the Bankruptcy Code.



Background: Types of Bankruptcy and the Bankruptcy Process (cont.)

- The Chapter 7 bankruptcy process employs a “means test” to weigh an individual debtor’s historical income against his/her debts and living expenses, according to a statutory formula, to determine if the debtor is eligible for Chapter 7 bankruptcy protection.⁵ In general, a debtor whose income minus allowable living expenses exceeds certain thresholds might not qualify for Chapter 7 bankruptcy protection and would have to either seek conversion to a different chapter of bankruptcy or have his/her bankruptcy case dismissed and receive no bankruptcy relief at all.

⁵The means test was added by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 102 (2005), codified at 11 U.S.C. § 707(b). The means test applies to individual debtors whose debts are primarily consumer debts. See § 707(b)(1). Even if a debtor does not “pass” the means test, he or she may be able to avoid dismissal or conversion by demonstrating special circumstances. See § 707(b)(2)(B). Debtors who “pass” the means test could still face dismissal or conversion for other reasons.



Background: Entities Involved with the U.S. Bankruptcy System

The U.S. bankruptcy system involves entities in both the judicial and executive branches of government.

- Within the judicial branch, the Administrative Office of the U.S. Courts serves as the central support entity for federal courts, including bankruptcy courts, and provides a wide range of administrative, legal, financial, management, and information technology functions. The Administrative Office of the U.S. Courts has developed and supports nationwide data systems to manage and maintain information on bankruptcy cases, but these systems are largely operated, managed, and maintained by the local bankruptcy courts.



Background: Entities Involved with the U.S. Bankruptcy System (cont.)

- Within the executive branch, the U.S. Trustee Program—a component of the Department of Justice—oversees the administration of most bankruptcy cases.⁶ The program’s Executive Office for U.S. Trustees provides a wide range of administrative, legal, financial, management, and information technology functions. Day-to-day operations are conducted by 95 field offices and 21 U.S. Trustees. The U.S. Trustees supervise the administration of federal bankruptcy cases and the approximately 1,400 private trustees who administer bankruptcy estates and distribute payments to creditors.
- The Department of Defense is not involved in the bankruptcy system and does not collect information about the rate of personal bankruptcy filings among military personnel. It does, however, maintain activation data on members of the National Guard and Reserve Components who are ordered to active duty. When authorized by law, the Department of Defense, via the secretaries of the military departments, places members of the National Guard and Reserve Components in active duty status. The Secretary of Defense also has the authority, by statute, to provide funds for members of the National Guard to perform a “homeland defense activity” under certain circumstances. This is a special status that is applicable only to the National Guard; it is not applicable to other components of the Reserves. It is defined by statute and, according to Department of Defense officials, has never been used.

⁶Bankruptcy cases in Alabama and North Carolina are not under the jurisdiction of the U.S. Trustee Program; instead, bankruptcy administrators within the judicial branch administer the cases in the judicial districts in those states.

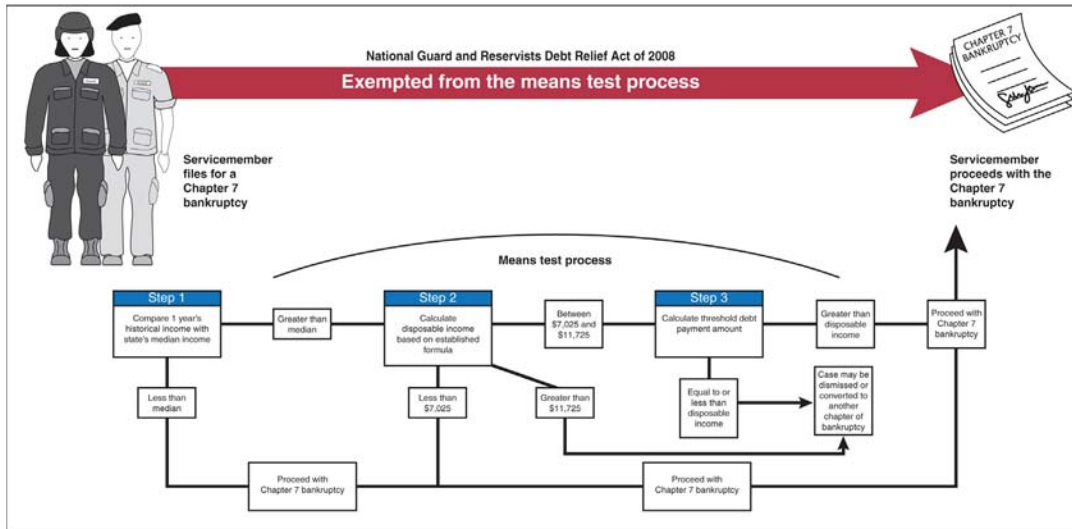


Background: The Debt Relief Act and the Means Test Process

The Debt Relief Act exempts qualifying members of the National Guard and Reserve Components from the means test process when they file a petition for Chapter 7 bankruptcy relief. See figure 1. However, qualifying members who “pass” the means test could still face dismissal of their case or conversion to another chapter of bankruptcy for other reasons.

Background: The Debt Relief Act and the Means Test Process (cont.)

Figure 1: The Means Test Process and Eligible Members of the National Guard and Reserve Components⁷



Source: GAO analysis of Pub. L. No. 110-438 and bankruptcy form B 22A (Chapter 7 Statement of Current Monthly Income and Means-Test Calculation).

⁷One year's historical income is calculated according to a statutory formula. See 11 U.S.C. §§ 707(b)(7) and 101(10A). The dollar amounts for comparison to disposable income are periodically adjusted. See 11 U.S.C. § 104(a). Finally, an individual who "fails" the means test may be able to proceed in Chapter 7 under certain circumstances. See 11 U.S.C. § 707(b)(2)(B) (special circumstances) and § 704(b)(2) (U.S. Trustee declines to bring a motion to dismiss).

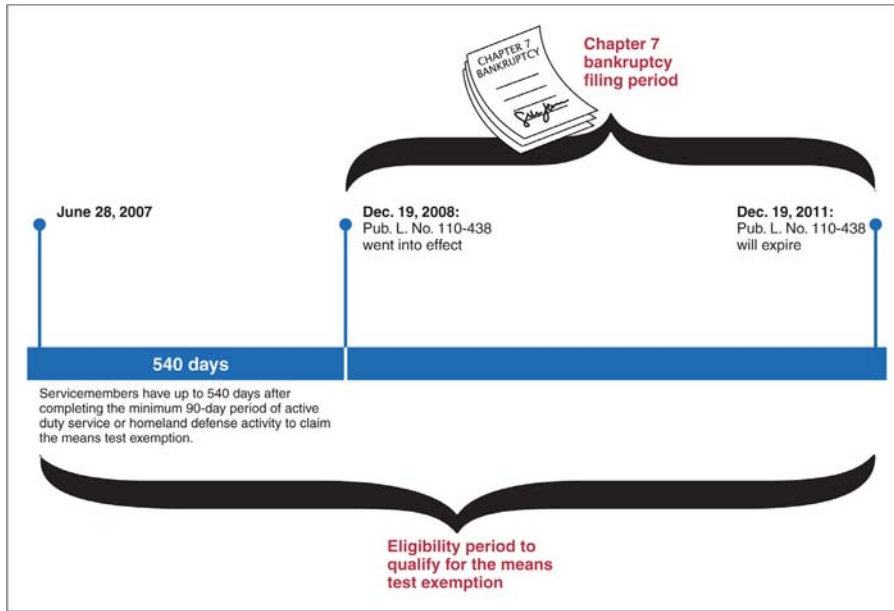


Background: The Debt Relief Act and Eligibility Requirements

Servicemembers who have served on active duty or performed a homeland defense activity, as defined by statute, for at least 90 days are eligible for the means test exemption if they file a petition for Chapter 7 bankruptcy relief between December 19, 2008 and December 19, 2011. Servicemembers may also be eligible for the exemption during this service or the performance of this activity if they believe that they will complete 90 consecutive days of service, according to officials from the Executive Office for U.S. Trustees. Servicemembers who have completed the minimum 90-day period of service and are no longer serving have a little less than 1.5 years (540 days) after they have completed the minimum 90-day period of service to claim the means test exemption. Servicemembers who completed their service periods dating as far back as June 28, 2007, may be eligible for the exemption if they filed for bankruptcy relief on December 19, 2008. (See fig. 2.) Servicemembers who are engaged in other military activities, such as response efforts related to a local natural disaster, are not eligible for this exemption if their service does not meet the definitions in the statute.

Background: The Debt Relief Act and Eligibility Requirements (cont.)

Figure 2: Eligibility for the Means Test Exemption



Source: GAO analysis of Pub. L. No. 110-438.



Objectives

The Debt Relief Act requires GAO to provide information on the use and effects of the means test as amended by the act. Our objectives include determining

1. the extent to which eligible members of the National Guard and Reserve Components (hereafter referred to as servicemembers) have claimed the exemption from the means test process for Chapter 7 bankruptcy filings, and the characteristics of these cases;
2. the extent to which eligible servicemembers who have claimed the means test exemption have attributed their debt to their active duty or performance of a homeland defense activity; and
3. the effects, if any, the Debt Relief Act has had on the bankruptcy system, creditors, and the debt incurrence practices of eligible servicemembers who have taken the exemption.



Eight Percent of Eligible Servicemembers Who Filed for Bankruptcy Relief Under Chapter 7 Have Claimed the Means Test Exemption

- The Debt Relief Act requires GAO to determine the number of bankruptcy cases in which eligible servicemembers claimed the means test exemption.
- Based on our analyses of bankruptcy data and activation records, we found that 2,122 eligible servicemembers filed a petition for Chapter 7 bankruptcy relief during the first year the Debt Relief Act was in effect.⁸ Of the 2,122 eligible servicemembers who filed a petition for Chapter 7 bankruptcy only 8 percent, or 176 eligible servicemembers,⁹ claimed the means test exemption.
 - Based on our analyses, we found the percentage of servicemembers who filed a petition for Chapter 7 bankruptcy relief to be small relative to the population of eligible members of the National Guard and Reserve Components.
 - Of the 701,309 servicemembers, derived from activation records, who potentially could have filed for bankruptcy during our review period and claimed the means test exemption, we found that the 2,122 eligible servicemembers who filed a petition for Chapter 7 bankruptcy relief represented 0.3 percent of the total number of eligible servicemembers.

⁸We use the term “eligible servicemember” to refer to members of the National Guard or Reserve Components identified in data provided by the Department of Defense as having served on active duty for a period of at least 90 days or beginning and not completing such service during the period of our study.

⁹Members who did not claim the exemption added by the Debt Relief Act may nevertheless have been covered by a different exemption. These 176 eligible servicemembers filed 173 bankruptcy cases. In 3 cases, the joint filers were both eligible servicemembers.



Eight Percent of Eligible Servicemembers Who Filed for Bankruptcy Relief Under Chapter 7 Have Claimed the Means Test Exemption (cont.)

- Most but not all of the 176 servicemembers completed the Chapter 7 bankruptcy process. (See table 1.)

Table 1: Types of Chapter 7 Bankruptcy Cases for Servicemembers Claiming the Means Test Exemption

Types of Chapter 7 bankruptcy case status	Number of eligible servicemembers
Successful completion (indicates servicemembers who received a discharge)	168
Dismissed cases or cases closed without discharge	4
Ongoing cases (as of August 9, 2010)	4
Total	176

Source: GAO analysis of bankruptcy data and activation records.



Eight Percent of Eligible Servicemembers Who Filed for Bankruptcy Relief Under Chapter 7 Have Claimed the Means Test Exemption (cont.)

- The Debt Relief Act requires GAO to determine whether there are any indications of abuse or potential abuse of the exemption.
 - We were unable to identify any clear indications of abuse or potential abuse of the exemption.
 - Although we were unable to identify any clear indications of abuse or potential abuse, we found 122 bankruptcy debtors who were reported as having claimed the means test exemption but did not appear eligible to do so based on the criteria established in the Debt Relief Act. It is unknown why potentially ineligible bankruptcy debtors might claim the exemption or why use of the exemption might be reported in the case file when it was not actually claimed. We did not examine the specific circumstances with regard to use of the exemption in these cases because the bankruptcy case files did not provide sufficient information. Accordingly, we are not suggesting that this use was indicative of abuse.¹⁰

¹⁰There are procedures in place in the course of a bankruptcy proceeding to verify information reported by the debtor.



Thirty-Two Percent of the Aggregate Debt Reported by Servicemembers Could Potentially Be Discharged

- The Debt Relief Act requires GAO to determine the aggregate amount of debt eligible servicemembers reported to have, the aggregate amount of this debt discharged by the bankruptcy process, and the aggregate amount of the debt in Chapter 7 cases that were converted to Chapter 13 cases.
- In our review of the bankruptcy case files of 168 eligible servicemembers who claimed the exemption and completed the Chapter 7 bankruptcy process, we determined that the aggregate amount of debt that these servicemembers reported was approximately \$43.7 million. The median amount of debt that these servicemembers reported was approximately \$198,413. Table 2 shows ranges of debt these servicemembers reported.

Table 2: Debt Ranges Reported by Eligible Servicemembers Claiming the Means Test Exemption

Debt in dollars	Number of eligible servicemembers with this range of debt
65,000 and less	42
65,001 to 260,000	58
260,001 to 360,000	24
More than 360,000	44
Total	168

Source: GAO analysis of bankruptcy data.



Thirty-Two Percent of the Aggregate Debt Reported by Servicemembers Could Potentially Be Discharged (cont.)

- Under bankruptcy law, certain types of debts are subject to be discharged. Generally speaking, discharge excuses the debtor from personal liability for many kinds of debt, subject to various exceptions. We could not determine the amount of debt actually discharged because bankruptcy case files do not include these data and this information was not available from other sources. However, the aggregate amount of debt that servicemembers could potentially have discharged was approximately \$13.8 million, or 32 percent, of the total amount of debt that they reported.¹¹ The median amount of debt that could potentially be discharged was approximately \$63,110.

¹¹Because bankruptcy case files do not indicate how much debt is actually discharged, we used a type of debt listed in the bankruptcy case file (unsecured nonpriority claims), which was identified by officials from the Executive Office for U.S. Trustees to typically represent the amount of debt potentially subject to being discharged. Unsecured nonpriority claims are listed in Schedule F of a Chapter 7 bankruptcy case file. Examples from the case files we reviewed included unsecured credit card debt and medical bills.



Thirty-Two Percent of the Aggregate Debt Reported by Servicemembers Could Potentially Be Discharged (cont.)

- Table 3 shows the ranges of debt these servicemembers could potentially have had discharged.

Table 3: Ranges of Debt That Potentially Could Have Been Discharged for Eligible Servicemembers Claiming the Means Test Exemption

Debt that could be discharged, in dollars	Number of eligible servicemembers with this range of debt
35,000 and less	39
35,001 - 80,000	71
80,001 – 100,000	16
More than 100,000	42
Total	168

Source: GAO analysis of bankruptcy data.



Thirty-Two Percent of the Aggregate Debt Reported by Servicemembers Could Potentially Be Discharged (cont.)

- Like bankruptcy debtors in the general population, servicemembers filing for bankruptcy relief under Chapter 7 often have a combination of dischargeable and nondischargeable debt. See table 4 for examples of both types of debt.

Table 4: Examples of Debt That Potentially Can and Cannot Be Discharged in Chapter 7 Bankruptcies

Debt that can be discharged	Debt that cannot be discharged
<ul style="list-style-type: none"> Many types of unsecured credit card debt Debt from bills for medical and other expenses Debts remaining following foreclosure on or surrender of property securing debt^a 	<ul style="list-style-type: none"> Most taxes Most types of student loans Most debt from domestic support obligations (e.g., alimony, maintenance, and child support) Mortgages and other debt secured by property (e.g., liens, many car loans)^a

Source: GAO analysis of the Bankruptcy Code.

^aAlthough a discharge protects the debtor from personal liability for secured debt, if the Chapter 7 debtor is delinquent the creditor may still foreclose on or repossess the property securing the debt.

- In addition to the 168 eligible servicemembers who claimed the means test exemption, there was 1 additional eligible servicemember who initially filed a petition for Chapter 7 bankruptcy relief and claimed the exemption, but whose case was converted to Chapter 13. The amount of debt the servicemember reported to have in this case was approximately \$980,000.



Ten of the 11 Eligible Servicemembers We Interviewed Did Not Attribute Their Debt to Military Service

- The Debt Relief Act requires GAO to study the extent to which eligible servicemembers who claimed the means test exemption when filing for bankruptcy relief under Chapter 7 had debts “substantially” or “materially” related to their military service.¹² We were unable to determine the extent to which debts were substantially or materially related to servicemembers’ military service because bankruptcy case files commonly do not identify the reasons individuals incur particular debts or declare bankruptcy and this information was not available from other sources.¹³

¹²According to Pub. L. No. 110-438, a case shall be considered “substantially” related to qualifying military service if more than 33 percent of the aggregate amount of an eligible servicemember’s debt is incurred as a direct or indirect result of such military service. A case shall be considered “materially” related to military service if more than 10 percent of the aggregate amount of the eligible servicemember’s debt is incurred as a direct or indirect result of such service.

¹³While Bankruptcy Schedules E and F ask for the consideration for each claim (i.e., each debt), debtors may not include some or all of this information on the Schedules. Moreover, the information listed may not sufficiently convey the circumstances surrounding the claim.



Ten of the 11 Eligible Servicemembers We Interviewed Did Not Attribute Their Debt to Military Service (cont.)

- We conducted interviews with 11 eligible servicemembers and found that 10 of the 11 randomly selected servicemembers did not attribute their debts to their military service; however, the results from this sample are not generalizable. Generally, they cited a combination of other reasons for filing for bankruptcy. Some of these reasons include unemployment or income decline, family breakup caused by divorce or separation, medical expenses, and housing reasons (e.g., increased mortgage payments or value of house declining). The servicemember who attributed some of his indebtedness to military service told us that he had to pay the costs of maintaining two households in different states—one for himself near his assigned military duty station and another for his family.
- Twelve of the private bankruptcy trustees with whom we spoke stated that in the cases they handled, they had not observed or did not recall military service having an impact on the bankruptcy debtors' financial condition. Three of the trustees told us that they would not have known some of the bankruptcy debtors were in the military if they had not taken the exemption.



Ten of the 11 Eligible Servicemembers We Interviewed Did Not Attribute Their Debt to Military Service (cont.)

- The Debt Relief Act also requires GAO to study whether the average levels of debt eligible servicemembers incurred increased before, during, or after their military service. We were unable to determine when eligible servicemembers incurred their debt in relation to their military service because bankruptcy case files commonly contain information only about debt that was outstanding at the time of the filing and information about when debtors incurred their debt was not available from other sources.¹⁴
- However, 7 of the 11 servicemembers with whom we spoke told us that the amount of their debt had decreased or remained the same during their military service. The other 4 servicemembers with whom we spoke told us that the amount of their debt had increased during their military service.
- Six of the 11 servicemembers with whom we spoke voluntarily indicated that their income from their military service was financially beneficial to them. For example, 1 of these servicemembers told us that he might not have lost his home had his military service and corresponding income begun earlier than they did.

¹⁴While Bankruptcy Schedules D, E, and F ask for the date each claim (i.e., debt) was incurred, debtors may not include some or all of this information on the Schedules. Additionally, the forms may not reflect debt incurred but paid off prior to filing.



Debt Relief Act Has Had Little Perceived Effect on the Bankruptcy System or on Creditors

- The Debt Relief Act requires GAO to study the effects that use of the act by eligible servicemembers has had on the bankruptcy system and on creditors.
- Based on our analyses, we found the number of servicemembers who filed for bankruptcy to be a small percentage of the total number of filings from the general population.
 - o Of the approximately 1 million Chapter 7 bankruptcy cases filed nationwide during the first year the Debt Relief Act was in effect, we found that the 2,122 eligible servicemembers who filed a petition for Chapter 7 bankruptcy relief represented 0.2 percent of total Chapter 7 bankruptcy filings.¹⁵

¹⁵These 1 million Chapter 7 bankruptcy cases include business entities and individual debtors.



Debt Relief Act Has Had Little Perceived Effect on the Bankruptcy System or on Creditors (cont.)

- According to interviews we held with public and private administrators of the bankruptcy system and officials from creditor and bankruptcy associations, the Debt Relief Act has had minimal effects on the bankruptcy system or creditor operations.
 - Although officials at the Administrative Office of the U.S. Courts and the Executive Office for U.S. Trustees could not provide implementation cost data to us, they described the procedural updates they made to implement the Debt Relief Act, which involved updating the relevant bankruptcy form to allow individuals to claim the exemption, training employees on how to administer the Debt Relief Act, and making minor changes to information technology systems. Officials told us that the cost of these actions was minimal.
 - Private trustees stated that the Debt Relief Act had little or no effect on their role in the bankruptcy system or on the resources they expended in cases. Additionally, representatives from the creditor association and from associations with legal expertise in bankruptcy stated that the Debt Relief Act has had little to no effect on their business operations or the bankruptcy system.



Servicemembers Report That Debt Relief Act Has Had No Impact on Their Debt Incurrence Practices

- The Debt Relief Act requires GAO to study the effects that use of the act has had on the debt incurrence practices of servicemembers.

- Interviews with 11 eligible servicemembers showed that the Debt Relief Act did not change servicemembers' debt incurrence practices because awareness of the exemption was limited. For example:
 - Five of the eligible servicemembers with whom we spoke stated that they only learned about the exemption from their attorneys after declaring bankruptcy.
 - Two of the servicemembers we interviewed told us that they learned of the means test exemption on their own during the bankruptcy proceedings.
 - Four other servicemembers told us that they were unaware of using the means test exemption until we contacted them.



Servicemembers Report That Debt Relief Act Has Had No Impact on Their Debt Incurrence Practices (cont.)

- Bankruptcy system and military association representatives also stated that it is unlikely that the Debt Relief Act has had any effect on the debt incurrence practices of servicemembers.
 - Representatives from associations with legal expertise in bankruptcy told us that in their experience, individuals who file for bankruptcy relief are typically unaware of their rights. In their view, it was unlikely that servicemembers using the means test exemption in a Chapter 7 bankruptcy filing would understand it well enough to be influenced by it.
 - Representatives from military associations told us that they did not believe servicemembers were aware of the Debt Relief Act.



Appendix I: The National Guard and Reservists Debt Relief Act of 2008

- Section 3 of the National Guard and Reservists Debt Relief Act of 2008 (Debt Relief Act) requires GAO to complete a study on the use and the effects of the law, as amended by the act.¹⁶ Specifically, we are required to provide information on the following:
 - Whether and to what degree servicemembers availed themselves of the benefits of the law.
 - Whether and to what degree such members are debtors in cases that are substantially or materially related to service that qualifies such members for the benefits of the law.
 - A case shall be considered substantially related to the service of a servicemember if more than 33 percent of the aggregate amount of his/her debt is incurred as a direct or indirect result of such service.
 - A case shall be considered materially related to the service of a servicemember if more than 10 percent of the aggregate amount of his/her debt is incurred as a direct or indirect result of such service.

¹⁶Pub. L. No. 110-438, § 3(a) (2008). The provision of law referred to in the act is 11 U.S.C. § 707(b)(2)(D) amended (and as amended) by the act.



Appendix I: The National Guard and Reservists Debt Relief Act of 2008 (cont.)

- The effects that the use of the law, as amended by the act, has on the bankruptcy system, creditors, and the debt incurrence practices of such members. As defined in the act, effects include
 - the number of cases in which servicemembers use the benefits of the act;
 - the aggregate amount of debt in these cases;
 - the aggregate amount of debt discharged in these cases;
 - the aggregate amount of debt in cases as of the time they are converted to Chapter 13;
 - the amount of resources expended by the bankruptcy courts and bankruptcy trustees in these cases;
 - whether and to what extent there is any indication of abuse or potential abuse of the exemption;
 - any increase in the average levels of debt incurred by servicemembers before, during, or after their military service;
 - any indication of changes in the debt incurrence practices adopted by servicemembers in anticipation of benefiting from the exemption; and
 - any indication of abuse or potential abuse of the exemption, reflected in the debt incurrence of servicemembers.



Appendix II: Scope and Methodology

Our review focused on members of the National Guard and Reserve Components—Army National Guard, Army Reserve, Navy Reserve, Marine Corps Reserve, Air National Guard, Air Force Reserve, and Coast Guard Reserve—who filed a petition for Chapter 7 bankruptcy between December 19, 2008 and December 18, 2009 (i.e., the first year the Debt Relief Act was in effect).

(1) To determine the extent to which eligible servicemembers¹⁷ have claimed the exemption from the means test process when filing for a Chapter 7 bankruptcy and to determine the characteristics of these cases, we did the following:

- o Obtained data from (1) the Administrative Office of the U.S. Courts for all Chapter 7 bankruptcy filings between December 19, 2008 and December 18, 2009; (2) the Administrative Office of the U.S. Courts and the Executive Office for U.S. Trustees for all Chapter 7 bankruptcy cases during the same time frame in which the means test exemption was claimed from both; and (3) the Department of Defense's Defense Manpower Data Center for all servicemembers who were activated between June 28, 2007 and December 18, 2009.

¹⁷We use the term "eligible servicemembers" to describe individuals whom the Department of Defense identified as members of the National Guard or Reserve Components and classified as having served on active duty for a period of at least 90 days (recently enough that they could have filed for bankruptcy during the period the Debt Relief Act was in effect) or still serving on active duty for any period of time as of December 18, 2009. Department of Defense officials informed us that the homeland defense activity classification had never been used.



Appendix II: Scope and Methodology (cont.)

- o Interviewed officials from and analyzed responses regarding the accuracy and completeness of the data provided by the Administrative Office of the U.S. Courts, the Executive Office for U.S. Trustees, and the Department of Defense to determine the reliability of the data. In addition we performed electronic testing of the data elements, checking for invalid and missing values. We found some invalid Social Security numbers and inconsistent names in both the bankruptcy and servicemember data. These problems were statistically insignificant but could result in an undercount of (1) the number of servicemembers who filed petitions for bankruptcy relief and (2) the number of eligible servicemembers who claimed the exemption. We determined that these data were sufficiently reliable for the purposes of reporting on the Debt Relief Act's requirements.
- o Matched records of all Chapter 7 bankruptcies against the activation data from Defense Manpower Data Center by using unique identifiers (e.g., name and Social Security number) for each bankruptcy debtor to ascertain how many eligible servicemembers declared Chapter 7 bankruptcy.
- o Compared these eligible servicemembers against the record of Chapter 7 bankruptcies in which the exemption was claimed to determine how many eligible servicemembers, as well as non-eligible bankruptcy debtors, who claimed the exemption.



Appendix II: Scope and Methodology (cont.)

- o For those eligible servicemembers who claimed the exemption, we reviewed the relevant bankruptcy court documents available in the Public Access to Court Electronic Records system to provide an approximate aggregate amount of debt these debtors reported and an estimate of how much of this debt was potentially subject to discharge. In addition, we reviewed the court information for those eligible servicemembers who had filed a petition for Chapter 7 bankruptcy and claimed the exemption but were later converted to Chapter 13, in order to determine how much debt they owed.
 - To provide a comprehensive estimate of how much debt was owed, we aggregated the total liabilities amount listed in the Summary of Schedules in the Voluntary Petition of each Chapter 7 bankruptcy case file (including those cases that were later converted to Chapter 13).
 - To provide an estimate of how much of this debt was potentially subject to discharge, we aggregated the total Schedule F (Creditors Holding Unsecured Nonpriority Claims) amount included in the Voluntary Petition of each Chapter 7 bankruptcy case file.
 - We decided to use the documents and types of debt referenced above on the expert advice of officials from the Executive Office for U.S. Trustees.



Appendix II: Scope and Methodology (cont.)

- The data that we used to estimate the debt amounts have the following limitations: (1) the debt amounts contained in court documents are self-reported by the bankruptcy debtor and have not been independently verified; (2) the debt amounts shown on the forms may not have been the final amounts, since some further actions by the parties could have affected the amounts in the cases; and (3) the amount of debt that could be discharged may not be final, since the amounts actually discharged are not verified after cases are closed and further actions could affect whether specific debts are considered dischargeable.¹⁸
- (2) To determine the extent to which eligible servicemembers who claimed the means test exemption attributed their debt to their military service, we did the following:
- Randomly selected 28 servicemembers, from the 176 eligible current and former servicemembers who claimed the exemption, for follow-up interviews. For these 28 individuals, we attempted to obtain recent phone numbers as well as recent addresses and e-mail addresses from the public records available through Lexis Nexis, an online information service, and personnel data available through the Defense Manpower Data Center. These 28 servicemembers reside in 17 states.

¹⁸For example, the debt listed in Schedule F may not include unsecured debt that is listed elsewhere in the bankruptcy petition, such as the unsecured portion of secured debt. Certain forms of debt are exempt from discharge, see 11 U.S.C. § 523(a), and other debt may remain undischarged as a result of a reaffirmation agreement between debtor and creditor under 11 U.S.C. § 524. The amount of debt considered discharged might also change as a result of the distribution of any assets. Because of the difficulty of determining whether or not specific claims were dischargeable, and since some of these actions could occur outside the record or after the bankruptcy proceeding has concluded, we used the claims listed in Schedule F as a proxy for the amount of debt potentially subject to discharge at the conclusion of the case.



Appendix II: Scope and Methodology (cont.)

- o Sent an advance letter to these servicemembers notifying them that we would be contacting them and requesting that they participate in a semistructured telephone interview. Afterward, we followed up with them via phone calls and e-mails (when available). We called each servicemember at various times, including during the mornings, afternoons, and evenings on both weekdays and weekends, for a maximum of 8 attempts, to ensure that those who wanted to participate had the opportunity to do so. We left voicemail messages when possible.
- o Obtained contact information for the 28 servicemembers; however, only 11 of these 28 servicemembers voluntarily agreed to be interviewed.
 - Reasons why we were not able to interview all 28 servicemembers included the absence of up-to-date contact information, overseas deployment, failure to respond to our phone and e-mail messages, or refusal to participate in the interview process.
 - GAO has no general authority to compel these individuals to be interviewed; therefore GAO's interactions with these servicemembers to collect information occurred on only a voluntary basis.
 - The group of 11 individuals we interviewed included eight members of the Army National Guard, two members of the Army Reserve, and one member of the Navy Reserve.



Appendix II: Scope and Methodology (cont.)

- o Administered a semistructured telephone interview that consisted of a series of structured closed and open-ended questions to all 11 eligible servicemembers who agreed to participate. After conducting the interviews, we reviewed the responses and summarized the key results. The views of this small group are not generalizable, and we could not independently verify the information they provided.
- o Supplemented these interviews by reviewing bankruptcy data where the means test exemption was claimed and sorted these bankruptcy cases according to the private trustee who administered them. We judgmentally selected 12 private trustees who had administered at least two cases and conducted semistructured telephone interviews with them.
- We were unable to determine the extent to which eligible servicemembers who claimed the means test exemption when filing for Chapter 7 bankruptcy had debts “substantially” or “materially” related to their military service, as required by the Debt Relief Act, because bankruptcy case files do not identify the reasons individuals incur particular debts or declare bankruptcy and this information was not available from other sources.¹⁹

¹⁹While Bankruptcy Schedules E and F ask for the consideration for each claim (i.e., each debt), debtors may not include some or all of this information on the Schedules. Moreover, the information listed may not sufficiently convey the circumstances surrounding the claim.



Appendix II: Scope and Methodology (cont.)

- (3) To determine the effect, if any, the Debt Relief Act has had on the bankruptcy system, creditors, and the debt incurrence practices of exempted servicemembers, we did the following:
- o Interviewed officials and representatives at the Administrative Offices of the U.S. Courts and the Executive Office for U.S. Trustees, a creditor association, and associations with expertise in either bankruptcy or the financial conditions of military personnel. We also interviewed 12 private bankruptcy trustees and 11 eligible servicemembers who had claimed the means test exemption.
 - o To identify the creditor association and associations with expertise in either bankruptcy or the financial conditions of military personnel, we reviewed congressional testimony related to the Debt Relief Act to identify expert witnesses who had testified, and we asked agency officials for recommendations. Also, we conducted Internet and database searches to identify creditor and other associations knowledgeable about either Chapter 7 bankruptcy or military personnel's financial issues.
 - o Reviewed the interview responses and summarized the key results; however, we could not independently verify the information we obtained during any of these interviews.



Appendix II: Scope and Methodology (cont.)

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- We visited or contacted the following departments and organizations during our review.
 - Department of Defense
 - Office of the Secretary of Defense
 - Office of Reserve Affairs
 - Office of General Counsel
 - Office of Legal Policy
 - Office of Personal Finance
 - Office for Military Community and Family Policy
 - Defense Manpower Data Center
 - Department of Justice
 - Executive Office for U.S. Trustees
 - Administrative Office of the U.S. Courts
 - National Guard Association of the United States
 - Enlisted Association of the National Guard of the United States
 - Reserve Officer Association
 - National Consumer Law Center
 - National Association of Consumer Bankruptcy Attorneys
 - American Financial Services Association



Appendix II: Scope and Methodology (cont.)

- We conducted this performance audit from July 2009 through September 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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