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Federal assistance may prolong bankruptcy filings

By: Maura Mazurowski June 1, 2020

With businesses closed, employees furloughed and sales plummeting, there will almost certainly be an increase in bankruptcy filings as a result of the pandemic. But with the recent outpouring of federal financial support, attorneys say the uptick in "COVID-caused" bankruptcy cases won't be seen for months to come.

"At some point, we're going to see a big increase in filings as people start looking at their realities and as the creditors start to get a little feisty," said Richmond attorney Ellen Ray. "My prediction is that we'll see a rise by the end of the year."

The first wave of financial support from the federal government came when the Coronavirus Aid, Relief and Economic Security Act – or CARES Act – took effect on March 29. The $2.2 trillion stimulus package was designed to mitigate the widespread economic effects the novel coronavirus has had on America since nonessential businesses began shutting down in early March.

And it worked. Though unemployment rates have continued to climb, bankruptcy filings decreased in April by 46% nationwide, according to the American Bankruptcy Institute.

ABI executive director Amy Quackenboss credits this halt in bankruptcy filings to financial federal aid.

"The extraordinary measures taken by Congress and the Administration to assist individuals and businesses weather the initial economic shock caused by the pandemic have likely staved off bankruptcy filings to date," Quackenboss said in a statement.

Ray said she noticed an immediate decrease in new clients after Gov. Ralph Northam closed down nonessential businesses on March 23.

Abingdon attorney Bob Copeland noticed the drop off even earlier when the Supreme Court of Virginia ordered all courts to close on March 15.

"With court closures, creditors weren't able to sue or get garnishments… So a lot of the creditor pressure put on individuals stopped," Copeland said.

Arlington attorney Andrea Davison, who focuses on creditor's rights, agreed. She said that banks are more preoccupied with assisting individuals and small businesses navigate loans stemming from the CARES Act – such as the Payment Protection Plan, a loan designed to provide a direct incentive for small businesses to keep their workers on the payroll – than work with creditors at this time.

"I think that banks specifically, and probably other creditors, are not doing a ton of enforcement right now," Davison said. "That will probably change once things level out a bit, but right now I would say that there's not a ton of credit enforcement going on."

"Frankly I think the biggest reason for that is the collection process has come to a halt, and when that happens people don't feel as anxious," Ray added.

According to the Virginia Employment Commission, as of May 14 nearly 400,000 Virginians were unemployed.

Though such a significant unemployment spike would typically lead to more bankruptcy cases, Copeland said that the extra $600 in weekly unemployment benefits provided by the coronavirus stimulus package eased financial pressures for individuals who may otherwise have considered filing bankruptcy.

"Depending on the nature of the employment, because of the increased unemployment wages…. Some folks are actually making more and doing better than they were before," Copeland said.

The enhancement for unemployed workers ends on July 31; in some states, it cuts off a week earlier. According to Senate Majority Leader Mitch McConnell, the next round of financial relief for Americans likely will not extend the benefit.

Davison said that this cutoff will likely be the first push for businesses and individuals considering a bankruptcy case.

"Things like medical bills are going to be up… Not all furloughed workers are going to be brought back," Davison said. "I don't know how fast a debtors counsel can work to get some of these bankruptcies filed, but I would anticipate that over the next six months we'll start to see an increase."

Copeland said his firm is fully expecting a spike in bankruptcy filings by the end of the year – so much so that they're looking to bring on another attorney to handle the anticipated increased workload.

"We're getting a lot of phone calls asking about what one would have to do to file," Copeland said. "By the end of July, I think you'll see some significant creditor pressure begin to build."

Ray anticipates that the "major uptick" in bankruptcy filings is still two years out. She added that recent closures of major retailers – including J. Crew and JCPenney, which filed for Chapter 11 bankruptcy on May 4 and May 15, respectively – may lead the public to believe that an increase in COVID-related bankruptcy filings already has begun.

However, Ray said these larger businesses were already on the "brink of bankruptcy" prior to the COVID-19 outbreak. The recent economic collapse was simply their last straw.

"Despite what you hear in the media, people don't run into bankruptcy as their first go to," Ray said. "It will take them a year or two before making that decision."

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