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The Non-discrimination Clause and Credit Counseling: What Elements of U.S. Personal Bankruptcy System should be Introduced to Korea?

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Abstract

The first case of personal bankruptcy was filed in 1997 in Korea. Due to the Asian economic crisis, the number of filings has drastically increased, reaching 154,000 in 2007. However, the increase in number does not necessarily mean that the lives of debtors have improved. What is more important is how we can help debtors to make a fresh start. Now we should focus on the Post-bankruptcy and Pre-bankruptcy systems. Learning from the experiences of U.S. will be very helpful for this. In fact, some experts in Korea are deeply interested in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, and some of them are arguing that Korea should import new elements of it.

In this respect, this paper will deal with what elements of the U.S. personal bankruptcy system should or should not be introduced to Korea. Surely there are many elements to consider, but this paper will concentrate on two elements which could be the most influential to personal bankruptcy practice in Korea today: the Non-discrimination Clause and Mandatory credit counseling.

The Non-discrimination clause is the most powerful protection for the bankrupt. However, the non-discrimination clause of Korea is too ambiguous and not effective enough. Therefore, it is imperative that it be revised as soon as possible. The U.S. non-discrimination clause can be the best reference for this.

In addition, mandatory credit counseling is not needed in Korea. The history of U.S. credit counseling tells us that credit counseling does not mean that a generous helping hand is given to debtors. The main policy reason for mandatory credit counseling is to reduce the number of bankruptcy filings. However, Korea has struggled for the last 10 years to increase the number of bankruptcy filings, fighting against deep social stigma and ignorance on bankruptcy. What we need now is not building new barriers, but breaking down old barriers.

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I. Introduction

1. Background

> "The shoes of Mr. K and his wife were found on Seogang Bridge yesterday. They left a note which read, 'Please take care of our children.' The police believed that debt might have been the cause for the suicide. When Mr. K became unemployed, he borrowed money from private lenders and started a small street shop. However, it was too difficult to repay usurious interest while raising two children."

The above paragraph was printed in Segye-Ilbo, a Korean daily newspaper in June, 2005. The economic crisis, which suddenly overtook the Republic of Korea ('Korea') in late 1997, left many people in deep financial hardships. Companies went bankrupt and people lost their jobs. On May, 1999, as the economy remained in recession due to declining consumption, the government repealed the regulation limiting maximum cash advances in order to increase consumption. Soon, credit card companies entered into a fierce competition to expand their asset base, carelessly issuing lines of credit to consumers regardless of their income level. Consequently, people failed to resist the temptation of their newfound credit source, and consumer debt began to increase. Some even launched small-scale businesses with funds procured through cash advances.

However, before long, many began feeling the burden of interest payments that continued to snowball due to annual interest rates as high as 30 percent. As monthly payments became unmanageable, in order to pay off their credit card debt, people began borrowing at even higher interest rates from private lenders, resulting in interest payments many times the principal amount they had borrowed. In order to collect debts, credit card companies and private lenders pressured debtors, often using threats and violent languages via telephone, mail, or personal visits, completely destroying the debtors' privacy.

According to the statistics from the Korea Federation of Banks, the number of delinquent debtors in Korea totaled approximately 4 million in 2004. Also, according to the statistics from the Seoul Central District Court, the divorce

rate of those who filed for bankruptcy at the Seoul Central District Court in 2004 was 20.5%. This rate is a remarkably high figure compared to the average Korean divorce rate of 9.3%, demonstrating that economic hardship eventually affects family life. Debtors are often deprived of all their properties, including their houses, and driven out to the streets. Some send their children to orphanages, and some even take their own lives, unable to cope with threats from creditors.

A possible solution for rescuing people from such a tragedy lies in the establishment of an efficient bankruptcy system and public education of it. Even today, many Koreans are unfamiliar with the concept of bankruptcy and discharge. Most Koreans believe that debts must be repaid fully and unconditionally, and it is quite surprising for them to realize that courts can and will write off debts. Even some judges do not understand why debts of insolvent debtors should be discharged. The first case of consumer bankruptcy was filed in 1997, and in 2002 the number of consumer bankruptcy filings exceeded 1,000 nationwide. Since then the number of filings has drastically increased, reaching 154,000 in 2007, but compared to the total number of insolvent debtors, still only a small percentage of people come to the court in order to find a new life.

If the bankruptcy system is more widely established, creditors will consider the credit history and payment ability of people more carefully before providing loans or issuing credit cards. Furthermore, debtors could become free from the sisyphean labor of repeatedly borrowing just to repay the existing debt, and they can also protect themselves from unlawful debt collection. Debtors who are given an opportunity for a fresh start will be able to re-engage themselves in economic activities in hopes of a better life and this could eventually energize the economy of the entire nation. In addition, the government would be able to reduce the amount of welfare expenditures associated with people struggling from debt-related financial hardships.

Recently, some Koreans are strongly arguing that the expansion of the bankruptcy system could bring moral hazard to debtors. Creditors demand that delinquent debtors work until the end of their lives for a full repayment of debts. However, this will make debtors hopeless and consequently it could destroy their lives as well as the lives of their children. As the wise Portia could see through, Shylock is not able to scoop a pound of debtor's flesh without spilling blood.

The basic concept of a bankruptcy system lies in giving a second chance to the failed individual. Although a financially insolvent company should be withdrawn from the market, a financially insolvent human being should not be "withdrawn" from his or her life. Life should go on.

2. The purpose of this paper

As mentioned above, personal bankruptcy is a big issue in Korea, and it is only at the beginning stage. Learning from the experiences of the U.S. will be very helpful to Korea. And some experts in Korea are deeply interested in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, and some of them are arguing that Korea should import new elements of it.

In this respect, this paper will take into consideration what elements of the U.S. personal bankruptcy system should or should not be introduced to Korea. Surely there are a number of elements to consider, but this paper will concentrate on two elements which could be the most influential to personal bankruptcy practice in Korea today.

(1) The Non-discrimination Clause
(2) Mandatory credit counseling

II. The non-discrimination clause

1. Necessity

The number of filings has drastically increased, and most of the debtors who filed bankruptcy can get discharged. Still, Korea is confronting another problem: how can we help the debtors make a fresh start after filing bankruptcy? The Korean Development Institute did an empirical research on Korean personal bankruptcy cases in 2005. The report shows that even if the debtors get discharged, they still suffer from devastating financial hardships. They still need job opportunities, but usually confront many legal and social barriers.

The bankrupt are unqualified to be a lawyer, doctor, nurse, public official, dentist, pharmacist, qualified architect, director of company, and so on. There

are around 260 statues which restrict their qualification for a job in Korea. These statues restrict incompetents and quasi-incompetents as well, and treat the bankrupt as the same as quasi-incompetents in job qualification. If debtors who have these jobs go bankrupt, they would lose their jobs. For this reason, debtors who have these jobs generally do not file bankruptcy, but tend to negotiate with creditors for debt adjustment.

Additionally, most companies have rules of employment which provide that the bankrupt can be dismissed. If company workers are in debt, they are reluctant to file bankruptcy, due to fear of losing jobs. Yet credit card companies keep sending demanding notes to debtors' companies, and calling debtors at work to squeeze them, making it very difficult for debtors to keep their financial hardship a secret. If their financial hardship is revealed to their employers, they feel great pressure to quit. Once they lose their jobs, finding another job is even more difficult, for most employers regard bankrupts as being irresponsible and incompetent.

In this circumstance, a fresh start, which is the main purpose of filing personal bankruptcy, is very difficult to achieve. Even if debtors can get a discharge, it does not mean much to them. They need to earn a living for today, but nobody wants to hire them. Those who were stock traders or teachers before bankruptcy, have to find jobs at a moving company or a construction site. Regardless of their search for jobs, reduced income will soon make them insolvent again. Because it is very difficult to find a new job, bankrupts often want to run small shops or restaurants. However, once they declare bankruptcy, their chances of getting a new loan are extremely restricted.

As mentioned above, Legal and social discrimination against the bankrupt is the worst hurdle for delinquent debtors who are looking for a fresh start in Korea. Since these problems also existed in the U.S., looking into the history of the Non-discrimination Clause in U.S. would be very helpful in finding a way for the bankrupt in Korea.

2. History of Non-discrimination Clause in U.S.

There was a monumental case, Perez v. Campbell,[1)] which held that a State

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1) Perez v. Campbell, 402 U.S. 637 (1971).

would frustrate the Congressional policy of a fresh start for a debtor if it were permitted to refuse to renew a drivers license because a tort judgment resulting from an automobile accident had been unpaid as a result of a discharge in bankruptcy.

The U.S. Supreme Court declared remarkable principles in Perez v. Campbell: "the construction of the Bankruptcy Act is similarly clear. This Court on numerous occasions has stated that '(o)ne of the primary purposes of the Bankruptcy Act' is to give debtors 'a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt.," "There can be no doubt, given that Congress intended this 'new opportunity' to include freedom from most kinds of preexisting tort judgments."

Moreover, the U.S. Congress widened protection for debtors through legislation of 11 U.S.C.A. §525 (a) in 1978.

> 11 U.S.C.A. §525(a) Except as provided in the Perishable Agricultural Commodities Act, 1930, the Packers and Stockyards Act, 1921, and article 1 of the Act entitled "An Act making appropriations for the Department of Agriculture for the fiscal year ending June 30, 1944, and for other purposes," approved July 12, 1943, a governmental unit may not deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, or other similar grant to, condition such a grant to, discriminate with respect to such a grant against, deny employment to, terminate the employment of, or discriminate with respect to employment against, a person that is or has been a debtor under this title or a bankrupt or a debtor under the Bankruptcy Act, or another person with whom such bankrupt or debtor has been associated, solely because such bankrupt or debtor is or has been a debtor under this title or a bankrupt or debtor under the Bankruptcy Act, has been insolvent before the commencement of the case under this title, or during the case but before the debtor is granted or denied a discharge, or has not paid a debt that is dischargeable in the case under this title or that was discharged under the Bankruptcy Act.

But this was only the beginning. Bankrupt employees needed more protection. The Fifth Circuit Court denied protection for a bankrupt employee

from being fired on the basis of declaring bankruptcy.

> We find no law which restrains MPL (employer) from firing an employee for reasons of filing a petition in voluntary bankruptcy. No statutory provision shields a bankrupt from later economic consequences visited upon him by private individuals, whether acting alone or in concert. A thorough examination of the Bankruptcy Act and its legislative history discloses no explicit provision or intent to prohibit discriminatory action against an individual on the basis of his declaring bankruptcy. In addition, such Congressional intent cannot be reasonably inferred from the statute as it is now enacted, nor can such a right be legitimately derived from the Constitution's Bankruptcy Clause itself. As it has been pointed out, that empowering provision speaks only in discretionary terms and does not grant any individual a right which Congress has not specifically legislated.[2)]

After a number of Bankruptcy Courts refused to extend the protections of §525(a) to prohibit discrimination against debtors by private employers, Congress added a provision codified as 11 U.S.C.A. §525(b) in 1984.[3)]

> 11 U.S.C.A. §525 (b) No private employer may terminate the employment of, or discriminate with respect to employment against, an individual who is or has been a debtor under this title, a debtor or bankrupt under the Bankruptcy Act, or an individual associated with such debtor or bankrupt, solely because such debtor or bankrupt-
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> (1) is or has been a debtor under this title or a debtor or bankrupt under the Bankruptcy Act;
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> (2) has been insolvent before the commencement of a case under this title or during the case but before the grant or denial of a discharge; or
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> (3) has not paid a debt that is dischargeable in a case under this title or that was discharged under the Bankruptcy Act.

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2) McLellan v. Mississippi Power & Light Co., 545 F.2d 919 (C.A. Miss. 1977).

3) John E. Theuman, J.D., *Protection of debtor from acts of discrimination by private entity under § 525(b) of Bankruptcy Code of 1978 (11 U.S.C.A. § 525(b))*, 105 A.L.R. Fed. 555.

Despite the added provisions, there was another problem left. Denial of loan to the formerly bankrupt is another threat to bankrupts who want seed money for a fresh start. Congress limited lenders' discretion through 11 U.S.C.A. §525 (c), but it was not so broad.

> 11 U.S.C.A. §525 (c)(1) A governmental unit that operates a student grant or loan program and a person engaged in a business that includes the making of loans guaranteed or insured under a student loan program may not deny a student grant, loan, loan guarantee, or loan insurance to a person that is or has been a debtor under this title or a bankrupt or debtor under the Bankruptcy Act, or another person with whom the debtor or bankrupt has been associated, because the debtor or bankrupt is or has been a debtor under this title or a bankrupt or debtor under the Bankruptcy Act, has been insolvent before the commencement of a case under this title or during the pendency of the case but before the debtor is granted or denied a discharge, or has not paid a debt that is dischargeable in the case under this title or that was discharged under the Bankruptcy Act.
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> (2) In this article, "student loan program" means any program operated under title IV of the Higher Education Act of 1965 or a similar program operated under State or local law.

3. New legislations in Korea

Big progress was made in protection of the bankrupt in 2006. The Korean Democratic Labor Party proposed 79 revision bills to abolish restriction of job qualification on the basis of declaring bankruptcy in September, 2005. Before March of 2006, 17 revision bills were passed. Although there still are many remaining statutes limiting job qualification on the basis of being declared bankrupt, the important point is that a consensus to abolish discrimination against the bankrupt was made.

A more significant progress was made when the National Assembly of Korea adopted the Non-discrimination clause. In March of 2006, the Debtor Rehabilitation and Bankruptcy Law ("DRBL") was revised, and article 32-2 was added.[4)]

This is indeed a big progress, but unfortunately, it was made in a hurry. As mentioned above, the non-discrimination clause was not easily made in the U.S. Not only did it take a long time, but a number of cases, debates and research were also needed. Nonetheless, article 32-2 of DRBL is a kind of emergency measures. There have been no cases on this issue, and there are hardly any Korean papers on this issue even today. This provision came out of nowhere. It uses very broad and ambiguous language like "disadvantage," "right cause," without definition. So, how courts will interpret this provision is very important. U.S. case law on the non-discrimination clause would be the best reference for this.

4. Issues on Article 32-2 of Debtor Rehabilitation and Bankruptcy Law

Some prospective issues on the interpretation of article 32-2 in comparison with the U.S. non-discrimination clause are suggested:

(1) What is the scope of Article 32-2?

Which parties are protected by the statute? The U.S. non-discrimination clause is applied to a restricted scope. For example, §525(b) protects the "individual".

> §525(b) mandates that a plaintiff seeking to invoke this provision be an "individual." Here, the plaintiff is a corporation. Throughout the Bankruptcy Code, a distinction is drawn between an "individual" and a "corporation." For example, that distinction appears in §109(e) which states that only an individual with a regular income can file under Chapter 13. This excludes corporations.[5)]

In comparison, article 32-2 has no such limitation. It says "No one shall be at a disadvantage," so not only individuals but also any party, including corporations, can be protected. However it is questionable whether the legislator had intended to include corporations to be protected under this

4) "No one shall be at a disadvantage like restriction of employment or dismissal without right cause because he/she is a debtor under this title."

5) *In re* Madison Intern. of Illinois, P.C., 77 B.R. 678, Bkrtcy. E.D. Wis., 1987.

provision. Prohibiting discrimination against corporations under bankruptcy procedure in any contractual relationships is not the same as protection for individual bankrupts. Nevertheless, the language of article 32-2 protects all parties equally.

What parties are restricted by the statute? While §525 restricts "governmental unit," "private employer," and "a person engaged in a business that includes the making of loans guaranteed or insured under a student loan program," article 32-2 does not have any restrictions regarding this. Therefore, it prohibits discrimination by any parties. This applies to discrimination by a governmental unit, private employer, bank, normal citizens, and so on.

This makes an important difference. In the U.S., it has been suggested that the statute, which refers to the acts of a "private employer" with respect to "employment," applies only when there is an existing employment relation between the parties. Thus, it has been held that §525(b) does not protect prospective employees, such as parties who allegedly suffer discrimination while negotiating an employment contract.[6)]

> §525(b) prohibits discrimination by a "private employer." This implies that there should be an existing employer-employee relationship between the parties. Here, neither was the defendant a private employer of the plaintiff, nor the plaintiff an employee of either defendant. §525(b) is limited to discrimination in employment. It is not as broad as the ban on governmental discrimination contained in §525(a). Possibility of a contract between the parties is not sufficient enough.[7)]

In contrast to §525(b), article 32-2 prohibits discrimination by any party. It particularly prohibits "restriction of employment." Protecting prospective employees from employment discrimination may be one of the main intentions of this legislation.

(2) What actions are prohibited by the statute?

With regard to the types of conduct prohibited by §525(b), the courts have

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6) Theuman, *supra* note 3.

7) *In re* Madison Madison Intern. of Illinois, P.C., 77 B.R. 678 (Bkrtcy. E.D. Wis., 1987).

made it clear that the statute applies to only discrimination in employment, and have rejected efforts to extend the anti-discriminatory goal of the statute to non-employment-related actions such as an insurance company's refusal to extend a debtor's policy or a bank's decision to close out a debtor's checking account.[8]

Article 32-2 does not have such limitations. It does not specify the actions which are prohibited. Article 32-2 lists two actions: "restriction of employment" and "dismissal". But this does not mean that "disadvantage" in this article includes only discrimination in employment relationship. "Restriction of employment" and "dismissal" are only examples. No language in this article limits the prohibited actions. So, every kind of discrimination is prohibited. It provides an amazingly broad range of protection.

The only condition to apply article 32-2 is that discrimination should be "without right cause"and "because he/she is a debtor under this title. Burden of proof in this article would be an important factor.

§525 has a similar but more complex condition: "solely because such bankrupt or debtor is or has been a debtor under this title or a bankrupt or debtor under the Bankruptcy Act, has been insolvent before the commencement of the case under this title, or during the case but before the debtor is granted or denied a discharge, or has not paid a debt that is dischargeable in the case under this title or that was discharged under the Bankruptcy Act."

Majority cases interpret this condition very narrowly.

> In construing §525(b), most courts have applied the plain meaning of the statute. *E.g.*, *Stockhouse v. Hines Motor Supply*, *Inc.*, 75 B.R. 83, 85 (D. Wyo. 1987); *In re Hopkins*, 66 B.R. 828, 831 (Bkrtcy. W.D. Ark. 1986); *In re Hicks*, 65 B.R. 980, 983 (Bkrtcy.W.D.Ark.1986). In *Stockhouse*, for example, the court stated that "[a]n employer may dismiss an employee for any cause unrelated to the employee's recourse to the bankruptcy laws … [Thus], plaintiff's claim is defeated by a showing that his bankruptcy status was not the *sole reason* for his termination." *Stockhouse*, *supra*, 75 B.R. at 85 .
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> In reaching our decision, we apply the plain language of §525(b),

8) Theuman, *supra* note 3.

> which proscribes discrimination by a private employer against an individual "solely because" of her bankruptcy status. Appellants have failed to adduce sufficient evidence to raise a genuine issue of material fact.[9)]

However, this narrow interpretation could abridge the range of protection by the non-discrimination clause severely. Employers can almost always find good reasons to fire bankrupts or debtors other than bankruptcy. Furthermore it is extremely difficult for employees to prove that bankruptcy was the "sole reason" for them being fired. Burden of proof should be distributed rationally so that either party could prove their own reasons. Therefore, the broader interpretation of Bell v. Sanford-Corbitt-Bruker is more reasonable. This case could also be a good reference for interpreting article 32-2 also.

> [1] 2. The Court's construction of the term solely is determinative in whether there has been a violation of §525. If "solely" means that the adverse action would have been taken even if the plaintiff had been an ideal employee in all other aspects, then the plaintiff has not met her burden of proof. If, however, "solely" prescribes a "but-for" analysis, then the plaintiff has proven her case.
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> 3. The Bankruptcy Reform Act of 1978 directed the judiciary to fill in statutory interstices so as to "continue to mark the contours of the anti-discrimination provision in pursuit of sound bankruptcy policy." H.R. Rep. No. 595, 95th Cong., 1st Sess. 367 (1977); S. Rep. No. 989, 95th Cong., 2d Sess. 81 (1978).
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> 4. It is the policy of the Bankruptcy Act to rehabilitate debtors and provide those who will avail themselves of the Act's protections with a fresh start.
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> 5. It would be virtually impossible for a bankrupt to prove that bankruptcy was the sole reason for being fired, and that no other factor was considered in reaching the decision. To interpret the term "solely" as requiring the bankrupt to prove this scenario would be in conflict with the policies of the Bankruptcy Act.
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> 6. In In Re Metro Transportation, 64 B.R. 968 (Bkrtcy. E.D. Pa. 1986),

9) Laracuente v. Chase Manhattan Bank, 891 F. 2d 17 (C.A.1 (Puerto Rico), 1989).

the bankruptcy court stated that the policies of the Bankruptcy Act require that "solely" be given a broader construction. This court would have found an adverse action, in which a bankruptcy filing appears to have *played a significant role*, to be in violation of §525.

7. The Court views the term "significant role" to be consistent with a "but-for" analysis. The Court concludes that, if the defendants would not have fired plaintiff "but for" the bankruptcy petition, the defendants have violated §525(b).

10. The Court, in the absence of authority in the context of §525(b), concludes that burden of proof allocations for proving a discriminatory discharge due to bankruptcy should be framed by analogy to race, color, religion, sex, or national origin cases. See McDonnell Douglas Corp. v. Green, 411 U.S. 792, 802-03, 5 FEP Cases 965 (1973). Hence the plaintiff, a member of the class protected under §525(b), made out a prima facie case of discriminatory discharge, and it was up to the defendants to establish a legitimate, non-discriminatory reason for their actions. The defendants established that the plaintiff was a substandard employee whose performance had worsened. However, evidence established that the defendants did not want to fire the plaintiff for the reasons of poor work performance; instead, it was the filing of a bankruptcy petition that resulted in the plaintiff's discharge. This conclusion is supported by, *inter alia*, the defendants' continued toleration of the plaintiff's shortcomings, Mr. Bruker Sr.'s formerly stated policy of not hiring anyone who had been declared bankrupt, the fact that the plaintiff was fired three days after defendants received notice of her bankruptcy, and the credible testimony of the plaintiff that Mr. Bruker had told her he was firing her for having been declared bankrupt. Thus, the defendants were in violation of 11 U.S.C. §525(b).[10)]

Furthermore, article 32-2 includes the term "without right cause." It is impossible to prove the inexistence of a right cause for discrimination. So, parties who gave disadvantages to debtors should prove their right cause.

10) Bell v. Sanford-Corbitt-Bruker, Inc. (1987, SD Ga) 2 BNA IER Cas 914.

(3) What are the appropriate remedies for violations of the statute?

Even though the prohibition itself is broad, it would be useless without appropriate remedies for violations. The U.S. discrimination clause provides powerful remedies. Here is an explanation of the remedies provided by the U.S. discrimination clause.

Once a violation of §525(b) has been established, the plaintiff, who is an employee, may be entitled to a number of possible remedies. In cases where the employee had been terminated or involuntarily transferred to another position, a number of Bankruptcy Courts have held that they had the authority to order that the employee be reinstated to the position he or she would have held but for the employer's unlawful action, and that this would be an appropriate remedy under the particular circumstances presented.[11)]

In one case where the court refused to order reinstatement, it explained that such a remedy would be inequitable and inadvisable where the employee in question had worked only briefly in a probationary position and, since his termination, had not maintained the specialized skills and knowledge required for competent performance.[12)] In a case involving the denial of an employment benefit, an order enjoining further discriminatory actions by the employer against a bankrupt employee has been held to be a proper remedy.[13)] Contempt citations, however, have been held not to be an appropriate sanction against an employer violating §525(b).[14),15)]

Monetary awards are another common remedy for §525(b) violations. Employees who have been unlawfully terminated because of bankruptcy or insolvency in particular, have frequently been awarded back pay, or, in the case of an independent contractor, lost profits. It has been held that back pay awards are to provide the plaintiff with the wages he or she would have received from the date of the termination, including sick leave, pension and other benefits, and any raises the employee would be likely to have received; but the plaintiff is required to mitigate his or her damages by seeking other employment during this period, and the amounts earned thereby are to be

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11) *In Re* Hicks (1986, BC WD Ark) 65 BR 980, 15 BCD 26, 15 CBC2d 1097, CCH Bankr L Rptr; *In Re* Hopkins (1987, BC WD Ark) 81 BR 491.

12) *In Re* Sweeney (1990, BC ND Ohio) 113 BR 359, 20 BCD 691.

13) *In Re* Vaughter (1989, BC WD Tex) 109 BR 229, 20 BCD 109.

14) *In Re* Hopkins (1986, BC WD Ark) 66 BR 828, 15 BCD 234, 16 CBC2d 186.

15) Theuman, *supra* note 3.

deducted from the award. Damages for the emotional distress resulting from a wrongful termination have also been awarded in at least one case,[16] and a plaintiff who suffered no economic injury as a result of a discriminatory employment action has nevertheless been held entitled to receive at least nominal monetary damages.[17] Other decisions, without stating any general rules, have refused to award punitive damages,[18] and have held that a plaintiff was not entitled to prejudgment interest on an award of back pay where his §525(b) proceeding had not been promptly commenced or expeditiously prosecuted.[19] The availability of attorneys' fees and costs to a successful plaintiff under §525(b) has been under dispute; some courts have held that such awards are never appropriate, since there is no specific statutory authorization for them in such cases, but other courts have denied fee awards for reasons specific to the particular cases at hand, and at least one court[20] has awarded attorneys' fees to the prevailing plaintiff in a §525(b) case.[21]

How about remedies for article 32-2? Korea has a civil law system, and courts of Korea do not have equitable remedies. In the Korean legal system, all remedies must be in the statute. The problem is that article 32-2 does not include any remedies for violations. So, in cases where the employee had been terminated or involuntarily transferred to another position, Korean Courts do not have the authority to order that the employee be reinstated to the position he or she would have held but for the employer's unlawful action. This is a serious problem that undermines the policy reason of this provision.

Only monetary awards are possible remedies for violation of article 32-2. But in a many cases, the plaintiff would have difficulty proving the amount of damage by discrimination.

5. Conclusion

The protection provided by article 32-2 seems to be amazingly broad and

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16) Bell v. Sanford-Corbitt-Bruker, Inc. (1987, SD Ga) 2 BNA IER Cas 914.

17) *In Re* Vaughter (1989, BC WD Tex) 109 BR 229, 20 BCD 109.

18) Bell v. Sanford-Corbitt-Bruker, Inc. (1987, SD Ga) 2 BNA IER Cas 914.

19) *In Re* Sweeney (1990, BC ND Ohio) 113 BR 359, 20 BCD 691.

20) *In Re* Vaughter (1989, BC WD Tex) 109 BR 229, 20 BCD 109.

21) Theuman, *supra* note 3.

powerful in appearance, yet its effectiveness is questionable.

First, article 32-2 does not include specific remedies, and Korean courts traditionally demand strict proof of the amount of damages for monetary awards. Second, the language of article 32-2 is too broad and ambiguous. It prohibits literally every kind of disadvantage on the basis of bankruptcy by any parties, against any parties. But it has a very broad and ambiguous exception too. Dependents will argue that they have "right cause" besides bankruptcy. Due to the ambiguity of article 32-2, judges may feel obliged to limit the article's scope rationally. Moreover, the ambiguity of the term "right cause" would give much discretion to judges.

It seems like article 32-2 is only a symbolic manifesto. It looks beautiful, but might become useless. Article 32-2 should be revised so that it includes specific provisions like the U.S. non-discrimination clause, and provisions regulating effective remedies should also be added.

III. Credit counseling

1. Introduction

Some economists in Korea are arguing that Korea should import the credit counseling system.[22] According to their view, many debtors are in substance delinquent and need to adjust their debt, but they repeatedly borrow money, making their debt bigger and bigger. So, they argue that debtors need to be trained and educated to be in control of their debt. In their opinion, credit counselors can diagnose the financial circumstances of the debtors, give advice on the best way for debtors, and negotiate with creditors on behalf of debtors. They believe that through credit counseling system, debtors can choose the most appropriate and favorable way of debt adjustment for them, negotiate with creditors on an equal basis, and get information about the personal bankruptcy system.

Advocates of the credit counseling system are even more encouraged by the fact that the Bankruptcy Abuse Prevention and Consumer Protection Act

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22) KOREA DEVELOPMENT INSTITUTE, ECONOMIC ANALYSIS ON THE FUNCTION OF PERSONAL BANKRUPTCY SYSTEM 140 (2005) (in Korean).

of 2005 prevents a debtor from filing a petition under the Bankruptcy Code unless the debtor first receives "an individual or group briefing (including a briefing conducted by telephone or on the Internet) that outline[s] the opportunities for available credit counseling and assist[s] such individual in performing a related budget analysis."[23]

However their optimism should be taken under careful consideration: for whom will the credit counselors mainly work for? For the debtors' best interest, for the creditors' best interest, or for their own interest? To answer these questions, we should look into the history of U.S. credit counseling first.

2. History of credit counseling in U.S.

Credit counseling first emerged in the 1950's, when credit institutions helped establish local credit counseling agencies to limit bankruptcy filings and avoid potential losses. Traditionally, credit counseling agencies provided one-on-one counseling aimed at teaching the debtor how to budget effectively. Counseling was an effective way to ensure that debtors would alleviate current debt and avoid excessive indebtedness in the future. When appropriate for the debtor's financial condition, traditional credit counseling agencies also offered a debt management plan. A debt management plan is essentially an agreement by the creditor to give concessions to the debtor. The credit counseling agencies facilitates this agreement by negotiating creditor concessions. Traditional credit counseling agencies facilitated the process because of their familiarity with the concession policies of various creditors. The concessions commonly obtained included more favorable repayment terms, such as reduced interest payments, waiver of late fees, forgiveness of overdue payments, or "re-aging" of the account. Once the debt management plan was negotiated, the debtor agreed to make monthly payments to the credit counseling agencies in the amount of the debtor's monthly obligation under the debt management plan. Traditionally, the debtor only paid small, sometimes voluntary, fees to the credit counseling agencies. The primary funding for credit counseling agencies came from "fair share payments" paid by creditors. The amount of the fair share payment was simply based on a percentage of the funds collected from the debtors.[24]

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23) 11 U.S.C. §109(h)(1).

From the 1930s throughout the early 1970s, when the debt pooling industry was dominated by for-profit entities, the industry fell into disrepute. In the most egregious cases, debt poolers charged exorbitant fees, failed to remit payments to creditors, established infeasible payment plans, and assured debtors that all obligations would be settled by the plan, even though the debt poolers had failed to secure the participation and cooperation of all creditors. State legislatures responded to these problems with legislation that either prohibited or regulated for-profit debt pooling.[25)]

In the early 1960s, under the leadership of credit industry representatives, the National Foundation for Credit Counseling — a nonprofit trade organization — organized agencies that combined credit counseling and debt management services. These non-profit agencies generally required consumers to pay an administrative fee for debt pooling services.[26)]

During the 1960s and 1970s, legislators began to exempt non-profit debt poolers from the prohibitory statutes. Legislators distinguished for-profit debt poolers from non-profit ones and granted statutory concessions to the latter. Apparently legislators were convinced that the not-for-profit character of consumer credit counseling services was sufficient to protect the consumer and in some states were content to let consumer credit counseling services charge a fee to consumer clients, even though the commercial practice of debt pooling was so abusive as to require its prohibition.[27)]

In the 1980s and early 1990s, with the growth of consumer debt, the credit counseling industry expanded. As more debtors filed for bankruptcy, more sought the help of credit counselors. The industry grew increasingly competitive, and many new entrants aggressively targeted financially strapped debtors via Internet and television advertisements. Although creditors traditionally paid a "Fair Share" contribution of twelve to fifteen percent of the funds that agencies collected from their customers, creditors decreased this contribution to an average of nine percent during the 1990s.[28)]

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24) John Hurst, *Protecting Consumers From Consumer Credit Counseling*, 9 N.C. BANKING INST. 159, 160-62 (2005).

25) Lea Krivinskas, *Don't File!: Rehabilitating Unauthorized Practice of Law-based Policies In The Credit Counseling Industry*, AMERICAN BANKRUPTCY LAW JOURNAL 59 (2005).

26) *Id*, at 59, 60.

27) *Id*, at 60.

28) *Id*.

In 1994, a group of independent consumer credit counseling services sued the National Foundation for Credit Counseling and its member agencies under the Sherman Act, alleging that the National Foundation for Credit Counseling entered into unlawful agreements with creditors to limit competitive entry into the credit counseling market. The parties eventually entered into a settlement agreement under which creditors were prohibited from serving on the National Foundation for Credit Counseling's national board of directors. This antitrust suit opened up the credit counseling market to other trade organizations, including the American Association of Debt Management Organizations and the Association of Independent Consumer Credit Counseling Agencies.[29)]

Today, several creditors no longer pay a flat rate to all credit counselors, and instead have implemented "pay for performance programs," whereby creditors evaluate credit counselors according to several restrictive criteria. These programs calculate "Fair Share" contributions based upon the success rates of the debt management plans, often determined by a combination of the following: the volume of payments made under the debt management plans, the frequency of default by consumer credit counseling services, and the age of consumers' credit accounts. Additionally, to be eligible for creditors' "Fair Share" programs, consumer credit counseling services, must often meet certain "minimum standards," including agency accreditation, counselor certification, and non-profit status.[30)]

3. History of Credit counseling in Korea

Credit counseling services were first introduced to Korea in 2002, but it was different from credit counseling services in the U.S. It was a quasi-governmental service. Since the input of bailout funds from the IMF (International Monetary Fund) due to the foreign exchange crisis in 1997, the household loans increased in the process of recovering the economy, and default rates went up. According to the Korea Federation of Banks, it marked 2,382,000 credit defaulters at the end of August 2002. And then the number went up even further as a result of corporate restructuring. The credit

29) *Id*, at 61.

30) *Id*.

defaulters had to pay their debts by themselves to get out of the unlikable situation as there was no concrete government measures to help them out. Besides, starting from July 2002, all information related to personal loans had been centralized. The purpose of such system was to prevent household bankruptcy due to excessive debts and improve the efficiency of credit evaluation services. However, such a system had made it more difficult for people to get loans, and as a result default rates continuously increased, which caused many people to become unable to repay their debt and heavily suffer from it.

At that time, the Korean government (The Financial Supervisory Service) made a plan to introduce the 'Credit Recovery Program' to people who suffer from credit problems, and public hearings were held in order to make agreements among financial institutions. The Credit Counseling & Recovery Service (CCRS) was established in October 2002 to help heavy debtors from their troublesome situation. It is a non-profit organization based on the agreements among major financial institutions (banks, credit card companies). It offers a Credit Recovery Program, in which debtors can extend the payout period up to 8 years based on their loan type, total amount of debt, ability, availability of pledge, and their credit status. The interest may be reduced or eliminated in consideration of the above mentioned terms.[31]

However, there experts criticized the CCRS's Credit Recovery Program. It usually offered an 8 year payment program, and only reduced or eliminated interest or late fee. 8 years was too long a time for delinquent debtors and they could not afford monthly installment payments which the CCRS demanded. So, only a small number of debtors could successfully pay monthly installments regularly, and a lot of debtors fell into a deeper financial crisis. The worst thing was that if they failed to pay only one monthly installment, all of the interest and late fee, which had been reduced or eliminated through this program, would be revived. Debtors often did not know this, but their monthly payments were applied to the revived interest and late fee. So, they were often surprised that the total amount of debt was still the same or increased, even though they paid monthly payments through the Credit Recovery Program.

Considering the points mentioned above, it is clear that Korea needs a

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31) KOREA DEVELOPMENT INSTITUTE, *supra* note 22, at 28.

more powerful and pro-debtor debt adjustment system. Actually, Korea already had Bankruptcy law similar to that of Japan and Germany, but personal bankruptcy had not been filed until 1997. It was only written in the code. The first case of consumer bankruptcy was filed in 1997, and in 2002 the number of consumer bankruptcy filings exceeded 1,000 nationwide for the first time. Yet most of the debt adjustment cases were still handled by the CCRS then, and Korean judges applied extremely strict standards to personal bankruptcy and discharge cases. Also, it took very long for debtors to get a discharge.

From 2003, the Korean Supreme Court made a lot of effort to reform personal bankruptcy procedures. Education of policy and purpose of the personal bankruptcy system was given to judges and clerks. Personal bankruptcy procedures were totally computerized, and nationwide conferences and seminars on personal bankruptcy were held for judges to attend. More generous and pro-debtor standards were encouraged by the Supreme Court. In 2004, U.S. chapter 13 was introduced to Korean legislation, and in 2006, the Korean bankruptcy law was totally revised, and it approached closer to the U.S. bankruptcy law. At last, the number of personal bankruptcy filings had drastically increased, reaching 123,000 in 2006.

As the number of bankruptcy filings increased, complaints about the consumer credit industry also increased. Creditors argue that rapid increase of personal bankruptcy is causing moral hazard of debtors. The consumer credit industry is deeply interested in The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 due to its pro-creditor aspects. Creditors believe mandatory credit counseling can reduce bankruptcy filing and maximize debtors' payments to them.

On the other hand, rapid increase of bankruptcy filings implies growth in the market for credit counseling agencies. A number of private credit counseling agencies are emerging in the market. They are not lawyers, nor are they specially trained or educated, most of them being former credit card company workers. Finally, Korea does not have a regulatory statute on credit counseling at the present.

4. Criticism on Credit Counseling in U.S.

(1) Increased competition and cost-cutting in the credit counseling

industry and credit counseling agencies' frequent affiliation with for-profit corporations accentuate credit counselors' conflict of interest. Since creditors have decreased their "Fair Share" contributions, credit counselors must be increasingly look for consumers to support credit counseling agencies' operations. As a result, credit counseling agencies are more likely to place debtors indiscriminately in debt management plans, which are credit counseling agencies' primary source of revenue. This financial pressure has also caused credit counseling agencies to abandon more expensive, diversified service offerings in favor of "debt management plan-only" business structures.[32)]

As a result of credit counselors' creditor origins and pro-creditor bias, debtors may receive insufficient or misleading information about alternatives to debt management plans — such as Chapter 7 or Chapter 13 bankruptcy. Many credit counselors portray bankruptcy as a less desirable, more expensive, and more embarrassing alternative to credit counseling. Although this portrayal of bankruptcy could be dismissed as aggressive marketing — and is defended by creditors and legislators who wish to decrease bankruptcy filings — it raises concerns for unauthorized practice of law. Even though unauthorized practice regulations are notoriously ambiguous and vary in substance, several courts have held that non-attorneys may not provide debtors with advice about the proper timing of bankruptcy petitions. Credit counselors' subtle recommendations to consumers about when — or whether — to file for bankruptcy merit attention, not because the hegemony of lawyers in the debtor-creditor context is threatened, but because the services being offered by credit counselors through debt management plans and by bankruptcy attorneys represent two substantially different debt resolution regimes. Credit counselors and bankruptcy attorneys each have a service to provide, and these services are not interchangeable. Many credit counselors are erroneously treating bankruptcy and credit counseling as overlapping alternatives by suggesting to a debtor when — or whether — he or she should file for bankruptcy, and by encouraging a debtor to pursue credit counseling instead.[33)]

(2) Credit counseling agencies that have recently entered the market

32) Krivinskas, *supra* note 25, at 56.

33) Krivinskas, *supra* note 25, at 56, 57.

charge excessive fees for debt management plans. For example, Cambridge Credit charges the debtor a monthly charge of up to ten percent of his monthly payment. Recent entrants also charge excessive setup fees, often holding the entire first payment to the debt management plans as such. It should be remembered that many debtors cannot afford to make payments on their consumer debt, much less an additional payment to the credit counseling agencies in the same month.[34)]

Furthermore, many credit counseling agencies do not properly explain the practice of holding the first payment, often inciting debtors to prematurely cease their regular payments to creditors. In this case, the consumer's debts continue to increase even though payments according to the debt management plan are dutifully made. This has a compounding effect on consumers, as debts increase and their credit is damaged. Some credit counseling agencies even fail to explain to debtors which accounts are covered by the debt management plan, or that the debtors must contact their creditors to explain the new payment schedule. These errors and miscommunications also result in further failure of payment by the debtor, which similarly undermines the purpose of the debt management.[35)]

(3) Credit counseling is not a good alternative to bankruptcy. Consumer credit counseling relies on the voluntary cooperation of creditors, while a repayment plan according to Chapter 13 requires no cooperation from the creditor. There are a number of other significant differences. First, a Chapter 13 debtor is protected by an automatic stay, which may be extended to co-debtors. Generally, this prohibits any creditor from continued collection efforts against the debtor, co-debtor, or the bankruptcy estate. It also operates to stay clear of all non-criminal actions against the person or property of the debtor or co-debtor. Obviously, no such protection exists for a debtor who engages in credit counseling, as consumer credit counseling cannot stop a foreclosure sale. Unlike consumer credit counseling, a Chapter 13 debtor need not pay all creditors in full, but must usually devote all of the debtor's projected disposable income over the course of the repayment plan. This statutory requirement may produce little for unsecured creditors if the debtor

34) John Hurst, *Protecting Consumers From Consumer Credit Counseling*, 9 N.C. BANKING INST. 159, 166 (2005).

35) *Id*, at 167.

directs that income in large part to payments on secured claims. Moreover, a Chapter 13 plan may modify the rights — or strip down — the amount of the underlying secured or unsecured claim to the amount owed, unless the claim is a mortgage belonging to the debtor's principal residence. Of course, a Chapter 13 debtor may still cure and de-accelerate a home mortgage. The most significant advantage of a Chapter 13 plan is that, at the completion of the plan, the bankruptcy court will grant the debtor a relatively broad discharge. Such a discharge has two principal effects. First, the discharged debt is void of any judgment based on the debtor's personal liability. Second, it operates as an injunction, against any action to collect, recover, or offset any discharged debt as a personal liability of the debtor. Consumer credit counseling cannot accomplish any of these important protections given to distressed debtors and is virtually dependent upon the mutual cooperation of creditors. Moreover, a Chapter 13 plan is usually completed sooner than a plan sponsored by a consumer credit counseling service. Normally, a Chapter 13 plan is completed in three years, although the court can approve of an extension for cause for a period no longer than five years. In contrast, a plan sponsored by a consumer credit counseling service will usually last until the debts are completely repaid, which can last four to five years.[36)]

5. Is credit counseling needed in Korea?

Credit counseling seems to be helpful to both debtors and creditors in appearance.

> "Our advisors devote their time and efforts to thoroughly understand the situation and give relevant and specific advices for each case. We analyze the client's income, expenses, assets, and liabilities, then, we negotiate with the creditors to establish a reasonable and mutually acceptable repayment plan. We also help credit delinquents find jobs in order to make a living on their own and repay their debt. In addition, we educate people the importance of realizing the importance of managing their own credit and ways to

36) Howard B. Hoffman, *Consumer bankruptcy filers and pre-petition consumer credit counseling: is Congress trying to place the fox in charge of the henhouse?*, BUSINESS LAWYER 1637-38 (1999).

establish a healthy consumption behavior. We provide such education not only to our clients who apply for our 'Credit Recovery Program' but also to regular people and students so that they can recognize the importance of managing their own credit before they suffer from debt."[37)]

In spite of its appearance, The Credit Counseling & Recovery Service's Credit Recovery Program did not work well for debtors. Debtors could not "recover" through this program. This program caused delay of filing bankruptcy, and worsened the debtors' financial situation. The Credit Counseling & Recovery Service is a quasi-governmental service, but based on large financial institutions' agreements. Even though they are not paid by creditors, it still shows pro-creditor attitude.

How about the emerging private credit counseling agencies? They will have great incentive to mislead debtors to their own program instead of bankruptcy. We can easily predict this through the history of credit counseling in the U.S. Even though the credit counseling agencies are non-profit entities, they need monetary compensation to run the agencies, and the easiest source of it is debtors' monthly payments to creditors. The Courts of Korea have made great efforts to increase personal bankruptcy filings for years because bankruptcy is the best way to rescue the 4 million delinquent debtors of Korea. It was an emergency situation. Even though this effort was successful and the number of filing increased rapidly, ignorance on bankruptcy system and deep social stigma on bankruptcy still exists. If delinquent debtors meet credit counselors first, due to their pro-creditor bias, debtors may receive misleading information about personal bankruptcy. Advisors of The Credit Counseling & Recovery Service used to advise debtors that bankruptcy takes a long time, costs a lot of money for attorney fee, and even if debtors can get a discharge, they can hardly find a decent job due to social stigma. These kinds of advices can have a serious influence on the debtors' choice to manage their debts.

Misleading advices by credit counseling agencies is a more serious problem in Korea than in the U.S., because social and cultural bias on bankruptcy is more serious in Korea. As mentioned earlier, the personal

37) http://www.ccrs.or.kr/, internet homepage of CCRS.

bankruptcy system had not been used until 1997, fundamentally because the traditional ethics of Korea are not compatible with the bankruptcy system. Traditionally, failing to repay one's debt is a crime and brings shame to one's status in Korea. If a debtor cannot repay his/her debt, his/her whole family feels responsible for it. So, in many cases, excessive credit card debt makes a domino effect among family members. Parents borrow money to repay their son's debt, and vice versa. In this cultural background, debtors feel guilty when filing bankruptcy. The Supreme Court of Korea tried hard to fight against this social and cultural bias through public education, publicity using the mass media, books, public hearings, etc. Even so, credit counselors easily neutralize this effort through a more direct contact with debtors, and consumer credit industry will eagerly support credit counseling agencies for their own interest.

Those who support mandatory credit counseling generally argue that rapid increase of personal bankruptcy in Korea will cause serious moral hazard of debtors, and that mandatory credit counseling can be an effective way to control excessive increase of personal bankruptcy filings. However, control can and should be done in the bankruptcy system itself. The Debtor Rehabilitation and Bankruptcy Law is stricter than 11 U.S.C. to debtors. First of all, debtors should be insolvent to file bankruptcy,[38] they should prove his/her insolvency. Exceptions to discharge are very broad: "excessively wasteful expenditure," a very abstract and broad concept, is one of the most important exceptions to discharge.[39] Legislators of Korea were concerned about debtors' moral hazard, and they adopted the "substantial abuse clause" of 11 U.S.C. to the 2006 amendments of the Debtor Rehabilitation and Bankruptcy Law.[40] Also, creditors can freely appeal to the debtors' bankruptcy or discharge. There is no need for "control" outside of the bankruptcy system; credit counselors are no better than judges at scrutinizing debtors' insolvency. The Korean judiciary is capable of controlling excessive increase of personal bankruptcy and the moral hazard problem.

For the above-mentioned reasons, adopting mandatory credit counseling of U.S. to Korea is inadvisable.

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38) DRBL article 305.

39) DRBL article 564.

40) DRBL article 309.

IV. Conclusion

The rapid increase of personal bankruptcy in Korea is like an emergency measure in an emergency room. The economic crisis of 1997 was similar to the Great Depression of the U.S. Although the bankruptcy system was not compatible with the traditional culture of Korea, Korea became acquainted with bankruptcy in a very short time because there was no other choice. The number of filing itself has increased rapidly, and creditors are arguing that we should slow down. However, emergency measures do not guarantee a final cure. It is only the beginning of a medical care.

The more important thing is how we can help debtors make a fresh start. As mentioned above, the Korean society has a serious social stigma against bankrupts. Not just social, but even legal restriction against bankrupts still exists. Even though debtors could be granted a discharge, their nightmare has not ended yet. It is difficult to find a job to make a living, fighting against social bias.

The Non-discrimination clause is the most powerful protection for the bankrupt in this manner. However, the non-discrimination clause of Korea is too ambiguous and ineffective; it should be revised as soon as possible. The U.S. non-discrimination clause can be the best reference for this.

Last but not least, mandatory credit counseling is unnecessary in Korea. The history of U.S. credit counseling tells us that credit counseling does the mean that a generous helping hand is held out to debtors. The main reason for a mandatory credit counseling policy is to control, or more specifically, to reduce the number of bankruptcy filings, but Korea has struggled for the last 10 years to increase the number of bankruptcy filings, fighting against deep social stigma and ignorance on bankruptcy. Why should we turn back now? Have we gone too far? Definitely not.

The history of bankruptcy in Korea is just at its incipient stage. What we need now is not making new barriers, but breaking down old barriers.

KEY WORDS: non-discrimination clause, credit counseling, personal bankruptcy, Perez v. Campbell, 11 U.S.C.A. §525, article 32-2 of debtor rehabilitation and bankruptcy law