Discussion of:

Busy Bankruptcy Courts and the Cost of Credit

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Motivation

1) Does judicial efficiency affect the cost of financing?
2) How large are the welfare losses from judicial inefficiency?

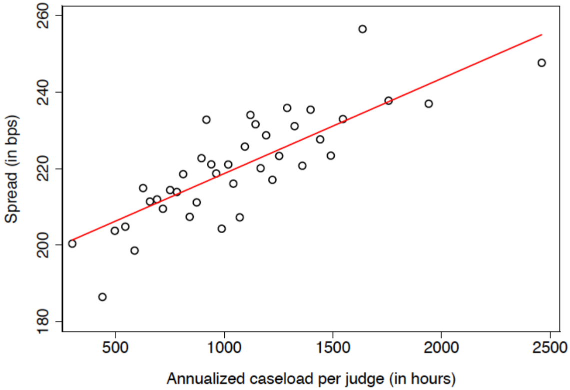
- Obviously important questions, but hard to answer...

$\Rightarrow$ **How to measure judicial efficiency?**
I would like to see more discussion of this in the paper

$\Rightarrow$ **Cross-sectional correlation between loan terms and judicial efficiency might be driven by unobservables**
e.g., poor areas have riskier firms and inefficient courts

Identification Challenge

(A) Interest Rate Spreads

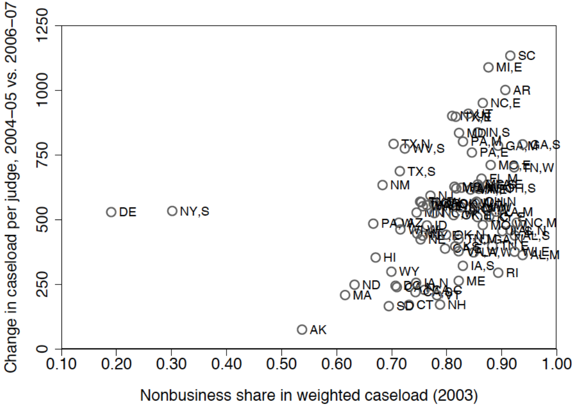


- Caseload is positively correlated with loan spreads
  e.g., poor areas have riskier firms and worse courts

Empirical Strategy

- **Introduction in 2005 of the BAPCPA**
  - Bankruptcy Abuse Prevention and Consumer Protection Act made it harder for individuals to default
  - Sudden reduction of the caseload of US bankruptcy courts
- **Judicial efficiency measured with the time-weighted number of cases filed per bankruptcy judge in a district**
  - Data on cases from USTP but no 1-1 mapping with districts
  - Use (representative?) sample of 27 states with one district
- **Exploit exposure to BAPCPA**
  - Share of district non-business bankruptcies pre-BAPCPA
  - Positive relationship b/w share of non-business filings and subsequent drop in the caseload
  - Iverson (2016): reduced the time firms spent in court, repeated filings, and banks charge-offs for business lending
  - The share of consumer cases is “highly persistent and largely driven by the concentration of economic activity”

First Stage



- More non-business filings, larger drop in caseload

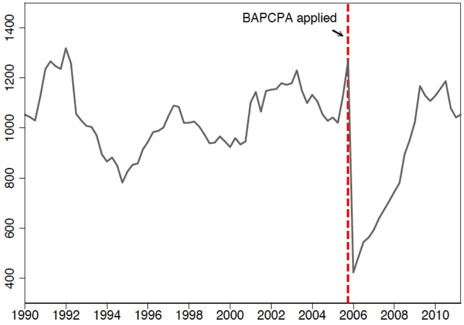
Results

- **Busy courts matter for the cost and maturity of credit**
  - $\downarrow$ of approx 2 work weeks per year for a bankruptcy judge $\Rightarrow \downarrow$ loan rates by 16 bps and $\uparrow$ loan maturities by 10%
  - Other aspects of the reform do not drive the results
  - Results not driven by easy credit from the the 2007-08 crisis
  - Larger effects for borrowers with higher default risk and lower expected liquidation values.

- **The induced drop in caseload saved US non-fin. corporates at least $10 bn in interest payments per year**
  - Still room for improvement: the social costs of busy courts today are at least $740 million per year
  - Solution? Adding a few judgeships in key districts (with highest return to judges)

Drop in Caseload after BAPCPA

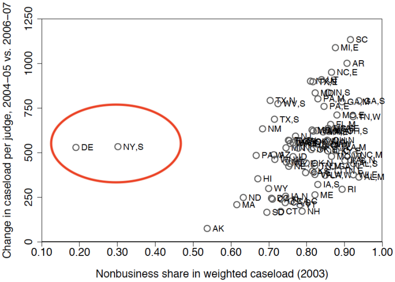
(A) Weighted Annual Caseload per Judge, 1990-2011



1) Great Recession blamed for the temporary effect
    - More evidence needed
2) In the DiD the "Pre" is 04-05 and the "Post" is 06-07
    - But policy passed in the Senate on March 10, 2005
    - But the drop in caseload happens at the end of 2005
    - "File to rush" before October likely affects the results

Treatment Across Firms

- **Are *all* firms "treated" based on their headquarter bankruptcy district?**
  - Firms can can file for bankruptcy where they
    - i) are incorporated
    - ii) have their principal place of business
    - iii) have an affiliate that filed for bankruptcy
  - Largest firms "shop" for districts (DL, NY)
- The exposure might be *wrong* for large firms



Aggregate Statements and Treatments Across Firms

- **Analysis run on very large loans (syndicated loans)**
  - Median borrower has more than \$1 bn in assets
  - Average loan size is \$208 million

→ **Very hard to extrapolate and aggregate estimates**
  - Elasticity of loan contract outcomes to court caseload considerably decreases with firm size

Theory Framework

- **Efficient courts associated to higher recovery values**
  - Time-constraint courts tend to be more friendly to debtor
  - BAPCPA makes courts less time constrained
  - Higher recovery rates for creditors
- **Higher recovery values should be priced in loans**
  - Especially for risky borrowers
  - What about other sources of funding (e.g., wholesale market funding)?
- **More discussion of the post-BAPCPA equilibrium**
  - Higher recovery values, lower loan rates
  - Bankruptcy more expensive
  - How do agents behave in the new equilibrium?
  - Characteristics of firms that file for bankruptcy?
  - Related to the seemingly temporary effect of BAPCPA

Conclusion

- Very important question
- More general than a bankruptcy/finance paper
- Careful discussion of identification challenges
- My comments:
  - Discuss timing and threat from anticipatory effects
  - Discuss how to measure "exposure" for large firms
  - Discuss new equilibrium when computing social costs
  - Discuss effects on other sources of funding