The American dream and a nightmare come true: The need for financial counseling

Rita W. Green, The University of Memphis

The purpose of this conceptual paper is to examine the financial decisions of two diverse couples against the backdrop of the current economic climate as they journeyed from the attainment of the American dream of home ownership to the nightmare destination of bankruptcy. The decisions of the couples will also be used to explore the need and potential for a culture of financial counseling.

Attaining the American Dream

The two couples, who are being profiled in this paper, were interviewed for a separate research study conducted by the University of Tennessee in early 2011. Luther and Josephine are African-American and age 65 and 62, respectively. Luther has worked for over 35 years as a truck driver. They did not have any emergency savings.

Phillip and Laura are Caucasian and in their fifties. Phillip is a Certified Public Accountant (CPA) and works as an accountant and Laura, who has obtained her PhD, has previously worked as a teacher. At one point, they had savings of about $75, 000 and were within about $5,000 of paying off their unsecured debt when their financial challenges began.

Both couples decided years ago to achieve their part of the American dream by purchasing a home of their own.

The American dream is a concept that encompasses several tenets and homeownership is one of them. The American dream of homeownership is a familiar refrain that has been culturally accepted and ingrained in the social conscious through mass media and world leaders. In 1984, Reagan signed a proclamation that stated "The provision of a decent home and a suitable living environment for every American family continues to be a national housing goal" (p. 1). As a result, this policy has been developed through various forms including legislation, new government agencies, a tax provision, and special treatment of institutions of mortgage finance.

Refinancing the Dream

At a certain point Luther and Josephine decided to refinance their mortgage. When asked about why they decided to refinance, Josephine comments that "we wanted to do some work on the house." Luther responded "We were short of cash. So, we said well, we'll refinance and borrow a little extra money. We can get back on board." They never were able to get back on board. Luther explains the results of refinancing their mortgage: "The house note doubles and is just putting you just that much further behind. We had to pay the taxes without going through the house note. That threw us behind."

Phillip and Laura decided to refinance their mortgage as well but for different reasons. Laura explains, "about five years ago, when the interest rates really started dropping I went back in and reworked our mortgage there, so we would have a fifteen year amortization, and hopefully be free and clear. [Although] that's a pretty hefty mortgage, it was all working very well." Phillip also shared that "We had one [home equity loan]. We spent seventy five to eighty percent of it on home improvements and repairs. It was an extremely good interest rate."

Economic data indicates Americans are living at a higher standard of living than any generation before them. Yet a closer look will reveal this standard of living is maintained by a high level of debt that continues to pose financial challenges for American households. Americans are now wealthier than previous generations because of increases in housing equity and stock market wealth (Manning, 2005). It is possible that household wealth has led to more spending as Americans have enhanced their standard of living through more debt. "The growth of consumer borrowing was influenced by traditional cultural attitudes (Puritan ethos) that promoted good debt such as accumulating an asset like a home over bad debt such as a rapidly depreciating new sports car" (Manning, 2005, p. 2). Loans are used to purchase cars, furniture, and electronics. Revolving credit through the use of credit cards, mortgage refinancing, and home equity loans has also been used to support a higher standard of living. In the 1980s, almost anyone could get a credit card, excessive growth in debt burdens in the American household characterized the 1990s, and the 2000s saw tremendous increases in mortgage debt as well as explosive growth in predatory and subprime lending (Lown, 2008).

Household debt as a percentage of disposable income rose from 73% in 1979 to 114% in 2003 and about 76% of these liabilities were due to escalating home mortgages (Manning, 2005). Home equity loans climbed from $86 billion in 2001 to $139 billion in 2003, according to the Joint Center for Housing Studies (2004). Mortgage foreclosure proceedings were initiated on 1.5 million homes in 2007, which represents an increase of 53% from 2006 (Bernanke, 2008). New foreclosures reached the highest level since 1979, rising to 0.99 percent of all U.S. home loans during the first quarter 2008, up from 0.83 percent in the fourth quarter 2007 (Armour, 2008). The delinquency rate, representing those at least 30 days behind on their bills and at risk of sinking into foreclosure, reached a record 6.35% during the first quarter of 2008 (Neil, 2008).

The Great Recession and its threat to the American Dream

An exploration of these case studies would be incomplete without a discussion of the economic environment in which these families must function. Each of the couples profiled sought bankruptcy protection and the timing of this action is important because it comes on the heels of an era in the U.S. economy, known as the Great Recession, which had the American economy in its grasp from December 2007 until June 2009 (The Great Recession, n.d.). The Great Recession was characterized by high unemployment, record numbers of foreclosures and high levels of bankruptcy filings. Shockwaves from this era are still being felt as consumers struggle with the prospects of financial failure.

In discussing the causes of the current U.S. economic crisis, Ben Bernanke (2010), Chairman of the Board of Governors of the Federal Reserve, stated "although a number of developments helped trigger the crisis, the most prominent one was the prospect of significant losses on residential mortgage loans to subprime borrowers that became apparent shortly after house prices began to decline" (p. 2).

According to Leeper (2009), those declines in house prices and the stock market reduced household wealth, which led to an inability of households and firms to obtain credit. That was followed by a sharply reduced demand for goods and services and as a result, firms began to cut back on investment and lay off workers (Leeper, 2009).

Unemployment and Underemployment.

Luther was one of millions who have recently gone through periods of unemployment. "Two jobs closed from under me. I'm working at the V.A. hospital. When I was driving the truck, I was working anywhere from sixty to seventy hours a week, and the money was coming in pretty good. According to Josephine, “Cause where as he's working for the V.A., he's making less money than he was making when he was driving the truck.” Because of two total knee replacements, Josephine no longer has the ability to work.

Phillip and Laura also joined the roll of the unemployed. Phillip shares, “I completed a consulting project. I'd been doing primarily consulting for eight out of the prior ten years which was right into the teeth of the worst part of this economic downturn. I started sending out resumes for permanent jobs. There's literally nothing. I mean I was either too experienced or, which I think probably means too expensive. The longer it went the harder it seemed to be to get responses, interviews, anything. Actually went fourteen months before I got another job, and Paula was, her contract wasn't renewed as a teacher, and they said it was because of the economy. So, it hit both of us pretty much at the same time.” Although Phillip finally landed a job, he’s not earning as much now. “It was a pretty serious downgrade but it has benefits, and one of the nice things, we can bring our son back on our health insurance now”. Laura has been unemployed for 18 months and is losing hope that there is an end in sight. She shares that “You know, hopefully, if I ever get hired again, and right now I feel like I'm going to be one of those older Americans who will never see work in my field again. I mean at least paid work. Maybe. I don't know. I mean I have no idea. You don't know how many rejection notices I've had.”

As of November 2010, the unemployment rate was 9.8%, which means that 15.1 million people were unemployed (Bureau of Labor Statistics, 2010). These results are grim for consumers who are experiencing large job losses, falling wealth, and less access to credit (Nutting, 2009). The harsh reality of unemployment has given rise to the term, “99ers”, which refers to unemployed Americans who have exhausted the maximum 99 weeks of unemployment insurance benefits that they can claim (Luo, 2010).

Experiencing the Nightmare of Bankruptcy to save the American Dream

Both couples made efforts to make negotiate payment plans with their mortgage companies. Luther mentioned they “did fall behind [on their mortgage]. And, we were trying to catch up. They [the mortgage company] said, well, you bring us twelve hundred dollars that ought to put you where you're supposed to be. Then after we did that they wanted twelve hundred more, and that will put you where you're supposed to be. So, you know, we said well we can't come up with no twelve hundred dollars every time they hollering twelve hundred dollars.” As a result, they ultimately filed bankruptcy to save their home. For Luther and Josephine, foreclosure was imminent because they had been in arrears with the mortgage payment. According to Josephine, “We hadn't received a foreclosure notice yet. But we filed to keep that from happening.” It appears that they may have received foreclosure notices in the past because the couple has two previous bankruptcy filings.

The decision to file bankruptcy had to be done quickly for Phillip and Laura. Time was of the essence since, according to Phillip, “the Monday after Christmas we got the foreclosure letter and they had a date that was only twelve days away.” The foreclosure notice was the answer to their attempts to work out payment arrangements with the mortgage company. Phillip says “We requested a loan modification from our mortgage lender, and their answer to that was to foreclose.” This couple was also in arrears on their mortgage.

Lessons Learned

The comparison of these two couples illustrates the fact that despite strong differences in standard of living, occupation, and education, financial failure can occur because of situations that are beyond a person's control. Bankruptcy is necessary in many situations but not the choice of many because it is the ultimate sign of financial failure. However, when compared to the possibility of foreclosure, many choose what they believe is the lesser of two evils.

There are also financial decisions these couples made that may not have been wise. When people make financial decisions, many factors guide their choices. And for better or worse, they have to live with the consequences of those choices.

When both couples sought to purchase a home and refinance it, the financial institutions were there to accommodate them. As we discussed earlier, homeownership is part of the American dream and the resources to support the pursuit of that dream are enormous. However, when both couples sought help, they did not encounter resources and extended hands to help them recover from their financial setbacks. I contend that there are two main reasons why this is the case. There is a stigma associated with financial failure and our society does not have an established system of financial counseling that is part of American culture.

Stigma associated with financial failure

Both of the couples I interviewed admitted they chose not to tell anyone, beyond a couple of immediate family members, that they were filing bankruptcy. Luther called bankruptcy a shameful thing. Phillip was determined to keep the matter hidden from his son, who is in college, because he was concerned that his child would think that their financial difficulties were as a result of his student loans. "Eighty-five percent of those who file for bankruptcy are struggling to hide that fact from families, friends, or neighbors" (Warren & Tyagi, 2003, p. 74-75).

"Anxiety and shame have become constant companions for Americans struggling with debt" (Warren, 2010, p. 5). More than 50% of Americans won't confide in friends about their credit card balances (Lazorony, 2006). In a 2005 survey by the National Opinion Research Council, families were asked to rank negative life events, from 1 through 100 (Smith, 2005). Respondents ranked filing for bankruptcy number three after listing the death of a child and being forced to live on the street or in a shelter as the most devastating possibilities.

When it comes to financial difficulties, there is a tendency to blame the "victim". When it comes to bankruptcy, the insistence that consumers were using the measure to escape personal responsibility for their debts was so strong that it led to the adoption of the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act. The new law was not debtor-friendly because it made it more difficult for debtors to get a fresh financial start (Kennedy, 2011). Debtors no longer have the option of choosing chapter 7 or chapter 13. In order to file chapter 7, debtors have to qualify for this option through the application of a means test based on income. If a debtor does not meet the standard for the means test, then they are forced into chapter 13.

Bankruptcy is also not a private affair. According to section 107a of the bankruptcy code, "a paper filed in a case under this title and the dockets of a bankruptcy court are public records and open to examination by an entity" (Department of Justice, Department of the Treasury, & Office of Management and Budget, 2000, pp.11-12). As a result, bankruptcy information is a matter of public record.

Financial Counseling in the United States: Implications and recommendations

Currently, there is no system of financial counseling that is part of American culture that establishes the practice as a beneficial norm and an infrastructure that makes it readily accessible to everyone. As discussed previously, we have a culture of homeownership. "Government initiatives created a culture of American homeownership: a national mindset that designated homeownership as integral to the economic and social well-being of the country" (Gibbons, 2009). In America, there is a culture that values physical health. Medical professionals, facilities and active research are a normal part of American life. When a person gets sick, the response to seek medical attention is automatic. But when a person is facing financial failure, in lieu of a culture that values financial counseling, and after their pleas for help have been ignored by creditors, filing bankruptcy may be the only option left for consumers to receive a lifeline that may help them hang on a little longer until their financial situation improves.

There are financial counselors available through numerous nonprofit organizations. One of the most well-known organizations includes the National Foundation for Credit Counselors, which has 800 member agencies in all 50 states (National Foundation for Credit Counseling, n.d.). However, they all have different names and for many agencies, financial counseling is just one of the services provided. Additionally, reputable financial counseling organizations don't have high visibility because their marketing budgets are low due to the limited budgets they have as nonprofit organizations. Meanwhile, there are plenty of financial predators, identified by the IRS, operating under disguise as "Christian Counselors" or "Family Services" (New York Times, 2006).

The new bankruptcy law actually requires credit counseling. However, because financial counseling is not a cultural norm, this requirement is not fulfilled in a logical way. The goal of credit counseling is to help consumers assess their financial situations and decide whether or not bankruptcy is the best option. While mandated counseling was designed to deter filings, the NFCC reports that only 3% of consumers seeking pre-bankruptcy counseling choose not to file (Lown, 2008). There is a reason why this is the case. As previously discussed, reputable financial counseling organizations are not widely marketed. However, commercials advertising the services of bankruptcy attorneys are plentiful. As a result, consumers often consult the attorney first before seeking counseling. At that point, most consumers have already made the decision to file bankruptcy. The attorney then directs them to a list of approved agencies that can conduct credit counseling. The ideal way for the process to flow is for the consumer to seek counseling first and then make a decision about filing bankruptcy. Since financial counseling is not a cultural norm, most consumers would probably not know to seek financial counseling or where to begin in a search of an organization that provides the service.

But financial counseling is not just for consumers in trouble. When decisions were being made to purchase their homes, the couples I've profiled could have possibly benefited from some good financial counseling. Financial counseling may well be warranted for a the purchase of a home, which represents the single most expensive item most consumers will ever buy - a commitment that lasts an average of 30 years. "The objective of financial counseling is not a narrow effort designed to increase money income or wealth to pay for a family's living expenses; rather it is to assist individuals in that household environment to learn to help themselves to live within available income and do so in a manner to successfully meet their personal financial goals" (Walker & Garman, 1992, pp. 786-787).

Numerous studies have concluded that homeownership is key to a family's financial well-being and the stability of their community (Joint Center for Housing Studies, 2006; Joint

Center for Housing Studies, 2001; National Association of Realtors, 2010). If homeownership is essential to financial well-being, then in this era of foreclosure crisis, the ability to keep that home is important. It is now time for society to strip away the stigma associated with financial struggle and establish a system for people to receive counseling.

Policies that establish financial counseling as an important tool to help consumers cope in the current economic environment are needed. Policies that support a system of financial counseling will go a long way in helping to remove the stigma of financial failure. Financial counseling is important because it gives consumers a safe place to vent their frustrations and receive professional assistance. The tears that Josephine and Laura were unable to hold back during our interview helped to relieve the pressure of their current circumstances. In America, we do not blame patients for being sick. We prescribe medicine, operate, and establish a system of recovery and future preventative health. And the same can be established through financial counseling for those who are on financial life-support.

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