

# WHAT IS BANKRUPTCY?

Bankruptcy is a federal legal proceeding that allows individuals to reduce or eliminate some or many of their debts and get a fresh financial start. An individual who files for bankruptcy must usually turn over some property or income to creditors. Although bankruptcy is one option to deal with financial problems, it is generally considered the option of last resort. The reason: its long-term negative impact on a debtor's creditworthiness.

There are different types of bankruptcy used by individual debtors, Chapter 7 and Chapter 13. In Chapter 7 bankruptcy, a person's non-exempt assets are sold and the proceeds are used to pay off creditors. In that case, the Bankruptcy Code allows the debtor to keep certain "exempt" property; but a bankruptcy trustee will liquidate the debtor's remaining assets. Accordingly, potential debtors should realize that the filing of a petition under Chapter 7 may result in the loss of property.

In a Chapter 13 bankruptcy, the person's debts are consolidated and the person provides a plan to pay the creditors. In addition, individual debtors who have regular income may seek an adjustment of debts under Chapter 13. A particular advantage of Chapter 13 is that it provides individual debtors with an opportunity to save their homes from foreclosure by allowing them to "catch up" past due payments through a payment plan. In 2005, the law was rewritten to make it more difficult to file a Chapter 7 bankruptcy and restricted the relief available in a Chapter 13 bankruptcy.

# BANKRUPTCY ELIGIBILITY

Before a debtor can file for bankruptcy, they have to obtain credit counseling, in an individual or group briefing, from a counseling agency approved by the U.S. Trustee. Government-approved credit counseling agencies are listed at <https://www.justice.gov/ust/list-credit-counseling-agencies-approved-pursuant-11-usc-111>

To qualify for Chapter 7 bankruptcy, a debtor must show relief is necessary through a means test. The test identifies debtors who have the capacity to pay back some of their debts. Anyone with an income below a state's median family income is exempt from a means test and may then file a Chapter 7 bankruptcy. Chapter 13 bankruptcy does not require debtors to meet the

# HELPFUL RESOURCES

- **BANKRUPTCY FORMS**  
[www.uscourts.gov/forms/bankruptcy-forms](http://www.uscourts.gov/forms/bankruptcy-forms)
- **CREDIT COUNSELING AGENCIES**  
[www.justice.gov/ust/list-credit-counseling-agencies-approved-pursuant-11-usc-111](http://www.justice.gov/ust/list-credit-counseling-agencies-approved-pursuant-11-usc-111)
- **DEBTOR EDUCATION PROGRAMS**  
[www.justice.gov/ust/list-approved-providers-personal-financial-management-instructional-courses-debtor-education](http://www.justice.gov/ust/list-approved-providers-personal-financial-management-instructional-courses-debtor-education)
- **DEPARTMENT OF JUSTICE, U.S. TRUSTEE PROGRAM**  
[www.justice.gov/ust](http://www.justice.gov/ust)
- **FEDERAL TRADE COMMISSION**  
[www.consumer.ftc.gov/articles/how-get-out-debt#Bankruptcy](http://www.consumer.ftc.gov/articles/how-get-out-debt#Bankruptcy)
- **U.S. BANKRUPTCY COURTS**  
[www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics.aspx](http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics.aspx)



*Do you have additional questions? If so, contact the Misawa Air Base Legal Office and request to schedule a Legal Assistance Appointment.*

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# BANKRUPTCY

## THIS BROCHURE INCLUDES:

- **WHAT IS BANKRUPTCY?**
- **ELIGIBILITY FOR BANKRUPTCY**
- **SHOULD I FILE FOR BANKRUPTCY?**
- **FILING UNDER CHAPTER 7**
- **FILING UNDER CHAPTER 13**
- **HELPFUL RESOURCES**



The information in this brochure is of a general nature and is not intended as a substitute for legal counsel.

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## SHOULD I FILE FOR BANKRUPTCY?

Filing for bankruptcy is a serious decision that should be made only after consulting a bankruptcy expert. Some people declare bankruptcy because they have overspent on their credit cards and believe they have no way to pay them off. A better first step is to speak to a consumer credit counselor. Other people declare bankruptcy because of large expenses such as medical care. Whatever your reason for thinking bankruptcy is the answer, you should first consult a bankruptcy attorney.

Consulting a bankruptcy attorney and filing bankruptcy can be expensive. A typical bankruptcy case may cost between \$700 and \$1,500, plus filing fees. That cost is minimal compared to the other long-term consequences associated with filing bankruptcy. The long-term consequences could include bad credit ratings for up to 10 years, difficulty in renting apartments or getting car insurance, higher interest rates for home and car loans, having to disclose a bankruptcy on job applications, and the social stigma attached to being bankrupt. Bankruptcy, or any failure to pay just debts, can also have significant impacts on a military member's security clearance, which could ultimately result in separation from the service.

However, in some cases, bankruptcy is an appropriate option. These instances occur when a person's debt outweighs their ability to repay to such an extent that the debt will be nearly impossible to pay off. Bankruptcy helps an overburdened debtor start fresh.

### FILING CHAPTER 7

Under Chapter 7 bankruptcy, most debts are discharged/forgiven. Exceptions to discharge include:

- ⇒ Spousal and child support.
- ⇒ Certain taxes.
- ⇒ Most student loans unless the debtor shows undue hardship (*see* 11 U.S.C. §523(a)(8)).
- ⇒ Consumer debts on luxury items of \$500 or more or within 90 days of filing for bankruptcy (*see* 11 U.S.C. §523(a)(C)(i)(I)).
- ⇒ Cash advances aggregating \$750 or more taken on credit cards on or within 70 days prior to filing for bankruptcy (*see* 11 U.S.C. §523(a)(2)(C)(i)(II)).
- ⇒ Additional requirements (*see* 11 U.S.C. §523).

In exchange for discharging other debts, a Chapter 7 debtor must surrender all non-exempt assets. These assets are then sold and the proceeds distributed to creditors. This is called liquidation. Assets include such things as land, household goods, cash, jewelry, insurance policies, and retirement funds such as IRAs.

Some assets are exempt, which allows the debtor to keep them, or partially exempt. Exemptions vary from state to state. For example, many states allow a debtor to exempt some or all of a home. IRAs are partially exempt. Certified retirement accounts under the federal ERISA law are exempt.

Other assets may still be subject to liens by creditors, such as a car loan from a bank, and will not be exempt. These are called secured debts. If your debt is discharged under Chapter 7, you must wait eight years before filing again. For a Chapter 7 bankruptcy, there is a \$245 filing fee, a \$75 administrative fee, and a \$15 trustee surcharge.

### FILING CHAPTER 13

Chapter 13 bankruptcy, also called a wage earner's plan, enables individuals with regular income to develop a plan to repay all or part of their debts. Under this chapter, debtors propose a repayment plan to make installments to creditors over three to five years. During this time, the law forbids creditors from starting or continuing collection efforts.

Chapter 13 bankruptcy cannot be filed if the debtor received a discharge under Chapter 7, 11, or 12 less than four years ago or the debtor received a discharge under Chapter 13 less than two years ago.

To be eligible for Chapter 13, a debtor must have:

- ⇒ Less than \$360,475 in unsecured debts and less than \$1,081,400 in secured debts (total debts in a joint husband and wife chapter 13 case must be within the above limits) (*See* 11 U.S.C. 109(e) as amounts may change), AND
- ⇒ A regular income to pay off the debts over the next three to five years.

As a general rule, Chapter 13 discharge releases the debtor from all debts provided for by the plan or disallowed, with the exception of certain debts referenced in 11 U.S.C. § 1328. Debts not discharged in Chapter 13 include certain long-term obligations (such as a home mortgage), debts for alimony or child support,

certain taxes, debts for most government funded or guaranteed educational loans, debts arising from death or personal injury caused by DUI, and debts for restitution or a criminal fine included in a sentence on the debtor's conviction of a crime.

Chapter 13 bankruptcy's principal benefit is that it allows a debtor to keep his or her assets. Perhaps most significantly, chapter 13 offers individuals an opportunity to save their homes from foreclosure.

However, after a court-approved repayment plan is drafted, all of a debtor's "disposable" income goes to the creditors. The debtor pays the trustee (a person appointed by the court to administer the repayment plan) all of his disposable income each month. Disposable income is the amount left after all reasonable living expenses have been paid. The income that is used to pay back the debts need not be wages, but can include benefits, pension payments, investment income or receipts as an independent contractor. At the end of a three to five year period, the court will eliminate the remaining unpaid balance on the dischargeable debts.

The filing fee for a Chapter 13 bankruptcy can change annually, and can be found on the U.S. Courts website: [www.uscourts.gov/services-forms/fees/bankruptcy-court-miscellaneous-fee-schedule](http://www.uscourts.gov/services-forms/fees/bankruptcy-court-miscellaneous-fee-schedule).

### FINAL TIPS

Some concerns many people have in filing are:

- ⇒ **Can a debtor own property?** Yes. A debtor can keep exempt property and any property received after the bankruptcy is filed.
- ⇒ **Can a debtor keep their home?** It depends. Under Chapter 13, a debtor can keep a home if he or she agrees to continue making monthly mortgage payments as well as make up for past-due payments. Under Chapter 7, the answer will depend on the equity in the home and the exemption amount provided for by state law.
- ⇒ **Will a debtor's credit rating be adversely affected and if so, for how long?** Yes, a debtor's credit rating will be affected and for up to 10 years. However, in some cases a debtor can seek to have the bankruptcy removed after less than 10 years.